

**NYISO Board of Directors**  
**Deferral of Decision**  
**On the**  
**Supplemental Congestion Reduction Proposal Appeal**

**Introduction and Background**

***The Instant Appeal***

Con Edison and LIPA appeal from a February 20, 2003, decision of the Management Committee (MC) to approve a motion (MC Motion) regarding a supplemental congestion rent reduction proposal (SCRP). National Grid and NYSEG (together with Rochester Gas & Electric) have filed motions in opposition. On April 14, 2003, the Governance Committee heard oral arguments in this appeal.

The MC Motion presumes, based on the materials presented at the Business Issues Committee and MC in support of the MC Motion, that the SCRП could be an interim measure that might be implemented as early as May 1, 2003. The MC Motion further presumes that the SCRП could later be compared with another proposal, the so-called "LECG Proposal," now also under development and consideration by the market participant committees

"for a possible longer term solution." While the MC Motion presumes a May 1, 2003, implementation date for the SCRP, the MC Motion also requests that NYISO staff "estimate the approximate time and other resources needed to implement the [P]roposal."

***The April 17, 2002 Decision***

The instant appeal presents substantially the same issues raised in an appeal to this Board decided April 17, 2002 (April 2002 Decision). In the April 2002 Decision, the Board declined to file with the Federal Energy Regulatory Commission (FERC) a proposed congestion rent shortfall allocation proposal that, like the SCRP, would ostensibly have reallocated congestion rent shortfalls in a more equitable manner. In that opinion, we expressed our reluctance to file the then-proposed congestion rent shortfall allocation mechanism because the MC had not also addressed the underlying causes of such shortfalls; principally, the sale of TCCs over transmission facilities that subsequently are either derated or experience forced outages. Accordingly, we urged the NYISO staff and the MC to work toward a more comprehensive solution that would both reduce congestion rent shortfalls and allocate shortfalls that do arise in a more equitable manner.

### ***Efforts Since the April 2002 Decision***

Subsequent to the April 2002 Decision, the NYISO staff and the MC, with the assistance of NYISO's market consultant, LECG, have explored both the feasibility of reducing congestion rent shortfalls and methods to equitably allocate shortfalls among the transmission owners (TOs). Those efforts have yielded the SCRP presently before us as well as the LECG proposal, which appears to be close to completion and consideration by the MC. However, neither the SCRP nor the LECG proposal solves the underlying problem of reducing congestion rent shortfalls. Moreover, it is not clear that a feasible solution to the underlying causes of congestion rent shortfalls will materialize anytime in the foreseeable future. We address below each of these issues.

### **Discussion**

#### ***The SCRP Versus the LECG Approach***

Based upon papers filed by the parties, oral argument, and discussions with NYISO staff and LECG, we conclude that allocating congestion rent shortfalls on cost causation principles is more equitable than the current system which allocates shortfalls based on each TO's proportion of residual TCC auction revenues. Thus, we agree conceptually with the SCRP's approach, which would allocate congestion rent shortfalls to TOs

responsible for outages that caused the shortfalls. However, we cannot presently support filing the SCRP with FERC for a number of reasons.

The SCRP appears to be an interim fix that would ultimately be replaced by the LECG Proposal. During oral argument neither side seemed to dispute the fact that the LECG Proposal is a superior method to the SCRP for allocating congestion rent shortfalls. We understand that the LECG approach would provide a more complete method of assigning congestion rent shortfalls based on cost causation principles. This is because the LECG Proposal would capture both inter- and intra-zonal congestion rent shortfalls. The SCRP addresses only inter-zonal shortfalls and, therefore, socializes a greater portion of the congestion rent shortfalls. In short, the LECG Proposal assigns more completely the costs of shortfalls to the owners of transmission facilities that create the problem in the first place. We believe this approach sends appropriate economic signals and will provide incentives for TOs to efficiently schedule outages during periods of low congestion and manage transmission O&M in a manner that would minimize congestion rent shortfalls.

Moreover, we understand from discussions with NYISO staff that it is not possible to implement the SCRP by May 1, 2003. Under a best-case scenario, developing necessary data transfer protocols and software

adjustments and obtaining approval from the FERC likely will require the spring and summer periods. NYISO Staff advises that the LECG proposal, which we believe will soon be ready for consideration by the MC, could be implemented in about the same time frame. Thus, SCRIP could not be implemented faster than the LECG Proposal and neither proposal could be developed, tested, and approved by the FERC prior to early fall 2003. Given that both approaches can be completed and operational in the same amount of time, we think it is more prudent to focus NYISO's resources upon approving and implementing the LECG Proposal. We are not presently convinced that the markets are best served by making serial changes to the congestion rent shortfall formula in a relatively short time period.

***Working Toward A More Comprehensive Solution***

In the April 2002 Decision we urged NYISO staff and the market participants to develop a more comprehensive fix to the congestion rent shortfall problem. A year later, we appear to be close to solving much of the shortfall allocation problem by implementing cost causation principles that would improve upon the current cost sharing arrangement. That is a step in the right direction.

But several pieces of the entire problem remain unresolved. For example, neither the SCRIP nor the LECG Proposal eliminate entirely the

need to socialize certain congestion rent shortfalls that cannot be linked to specific outages. Furthermore, reducing congestion shortfalls *in the first instance* is a problem that apparently cannot easily be solved because there presently is no way to match TCCs sold to only those facilities that will *not* go out of service during the auction period. Neither the SCRP nor the LECG Proposal resolves this underlying problem and we urge the NYISO staff and market participants to continue to explore whether a feasible solution exists.

In light of the progress made on the shortfall allocation issue and taking into account the difficulty, and perhaps infeasibility, of reducing congestion rent shortfalls in the first place, we no longer believe it is either realistic or prudent to await an overall fix to this bundle of problems. Therefore, the Board is now prepared to take a staged approach and implement improvements in this area as, and if, they are developed.

### **Conclusion**

In order to support the stability of the NYISO markets, and to avoid expending significant NYISO resources to implement the SCRP for only an interim period, we have decided to defer a decision on this appeal in order to give the MC a reasonable time to complete development and consideration of the LECG Proposal.

We also urge the market participants and NYISO staff to continue to explore ways to resolve the remaining open issues, particularly the issue of reducing congestion rent shortfalls in the first place. Nonetheless, we are no longer convinced that we need to wait for a global solution to the congestion shortfall reduction issue to move forward with allocating congestion rent shortfalls based upon cost causation principles.

If the Management Committee finalizes and approves the LECG Proposal soon, this appeal likely will become moot. If the LECG Proposal is not finalized and approved within a reasonable time, then we will revisit this appeal and issue a decision.

We direct NYISO Staff to provide the Board with periodic reports on (i) the development and consideration of the LECG Proposal, and (ii) the efforts of NYISO Staff and the market participant committees to determine the feasibility of developing a method to reduce congestion rent shortfalls.

Finally, we note that nothing in the MC Motion or other materials presented to us addresses: (i) the project priority of either the SCRP or the LECG Proposal, (ii) the budget impacts and source of funding for these proposals in 2003, and (iii) the impacts, if any, these changes will have upon NYISO's transition to the SMD 2.0 systems now under development. Each

of these issues needs to be addressed in future NYISO committee deliberations.

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