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September 28, 2001

FILE NO: 55430.000046

The Honorable David P. Boergers, Secretary  
Federal Energy Regulatory Commission  
888 First Street, N.E.  
Washington, D.C. 20426

New York Independent System Operator  
Virtual Bidding Market Mitigation Measures  
Docket Nos. ER01- -000, ER01-3001-000 and ER01-3009-000

Dear Mr. Boergers:

On September 4, 2001, the New York Independent System Operator, Inc. (“NYISO”) filed revisions to its Open Access Transmission Tariff (“OATT”) and Market Administration and Control Area Services Tariff (“Services Tariff”) to implement bidding procedures that would allow Market Participants<sup>1</sup> to bid non-physical (*i.e.* “virtual”) generation and load into the Day-Ahead Market and settle those bids in the Real-Time Market (“Virtual Bidding”).<sup>2</sup> That filing (the “September 4 Filing”) noted that the NYISO was at that time resolving the details of appropriate Virtual Bidding market mitigation measures with its stakeholder committees for filing with the Commission. Having completed that process, the NYISO, by counsel, pursuant to Section 205 of the Federal Power Act, hereby submits revisions to its Market Mitigation Measures (Attachment H to the Services Tariff) to implement appropriate market mitigation measures for Virtual Bidding.

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<sup>1</sup> Capitalized terms not otherwise defined herein having the meaning ascribed to them in Article 2 of the Services Tariff.

<sup>2</sup> Docket Nos. ER01-3001-000 and ER01-3009-000.

The Honorable David P. Boergers  
September 28, 2001  
Page 2

The proposed revisions to Attachment H were approved by the NYISO members at the Management Committee's monthly meeting on September 11, 2001, and this filing was approved by the NYISO Board of Directors at its monthly meeting on September 18, 2001. The revisions were prepared with the advice of, and are endorsed by, the NYISO Market Advisor, Dr. David Patton.

#### I. Documents Submitted

Pursuant to Section 205 of the Federal Power Act and 18 C.F.R. § 35.13, the NYISO submits six copies of:

1. This filing letter;
2. Clean revised sheets from Attachment H of the Services Tariff incorporating new provisions setting forth market mitigation measures for Virtual Bidding (Attachment I);
3. Redlined revised sheets from Attachment H of the Services Tariff marking the new provisions setting forth market mitigation measures for Virtual Bidding (Attachment II); and
4. A form of Notice for the Federal Register (Attachment III).

#### II. Copies of Correspondence

Copies of correspondence concerning this filing should be served on:

Robert E. Fernandez  
General Counsel and Secretary  
John P. Buechler  
Director of Regulatory Affairs  
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### III. Summary of Virtual Bidding Mitigation Measures

As stated in the September 4 Filing, at 4:

The proposed virtual bidding procedures will open the NYISO-administered energy markets to non-physical customers by allowing for the submission of bids for purely financial purchases or sales of energy, rather than (or in addition to) purchases or sales associated with the physical input or withdrawal of energy. As proposed, the NYISO's virtual bidding procedures would allow a qualified customer to buy energy ("virtual load") in the Day-Ahead Market at Day-Ahead prices and sell it in the Real-Time Market at Real-Time prices or to sell energy ("virtual supply") in the Day-Ahead Market at Day-Ahead prices and buy energy to cover that sale in the Real-Time Market at Real-Time prices. Virtual bidding transactions ("Virtual Transactions") are financial transactions only and do not entail the physical generation or consumption of electricity.

In essence, upon the implementation of Virtual Bidding any qualified entity will be able to bid either virtual load or virtual supply, or both, into the Day-Ahead Market in any zone in the New York Control Area. As a result, the NYISO does not expect the implementation of Virtual Bidding to create market power problems, since there will be low barriers to entry into either the load or supply sides of the markets. Indeed, Virtual Bidding should alleviate market power problems in the Day-Ahead Market, increase market liquidity, contribute to convergence between Day-Ahead and Real-Time prices, and provide a valuable means of hedging the risks of price differences between the Day-Ahead and Real-Time markets. Moreover, because of the absence of barriers to entry, significant deviations of prices from competitive expectations should be self-correcting, because bidders should have the ability to arbitrage away any significant prices differences between the two markets.

Nonetheless, Virtual Bidding will be a new, untried feature of the New York markets, and may be subject to gaming or market power strategies that could result in distorted market outcomes. Alternatively, unexpected market conditions may arise that would permit virtual

bids to distort market outcomes. Thus, prudence dictates that an appropriate market mitigation measure be in place coincident with the initiation of Virtual Bidding. In this connection, the NYISO notes that the Commission has approved a mitigation measure to address similar concerns related to Virtual Bidding in PJM.<sup>3</sup>

Because Virtual Bids are settled in the Day-Ahead Market but covered in the Real-Time Market, any abuse of market power, or gaming of market rules or conditions, would be reflected in unexpected deviations between Day-Ahead and Real-Time prices. Consistent with the overall approach of the Market Mitigation Measures, mitigation action should not be undertaken unless a significant unwarranted deviation in prices between the two markets has occurred or is anticipated. Since arbitrage cannot be expected to cause the Day-Ahead and Real-Time prices to converge efficiently on an hourly or daily basis, an unwarranted deviation should be measured over a meaningful period. Thus, the attached filing proposes to evaluate price comparisons “over a rolling four week period or such other period determined by the NYISO to be appropriate to achieve the purpose of this mitigation measure.”<sup>4</sup> In addition, consistent with the expected self-correcting capability of the Virtual Bidding market, mitigation action should not be undertaken unless there is a substantial basis to conclude that a significant price deviation between the two markets will not be corrected by the markets themselves. The proposed revisions to the Market Mitigation Measures conform to these principles.

The proposed revisions also closely conform to the measure for mitigation of load bidding set forth in the existing Market Mitigation Measures and approved by the Commission. This is appropriate, because under the existing market procedures, load bidding involves a form of Virtual Bidding, since load bids in the Day-Ahead Market do not have to match actual or expected loads, and thus can involve a significant virtual component.

In general, Virtual Bidding strategies aimed at distorting Day-Ahead prices should be corrected by the market. Since there are no quantity ceilings on Virtual Bids, however, there is at least the potential for Market Participants to offer abnormal quantities of virtual load or supply in an effort to distort market outcomes. By the same token, limiting the quantities of

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<sup>3</sup> See Letter Order dated January 26, 2001 in Docket No. ER01-773-000.

<sup>4</sup> Attachment I, Sec. 4.6.2(b).

anomalous bids should be a sufficient remedy to cure any such market distortions, by eliminating the portion of one or more Virtual Bids for either load or supply that would create an artificial imbalance between load and supply. Under the proposed new section of the Market Mitigation Measures submitted with this filing, if the NYISO detects a significant deviation between Day-Ahead and Real-Time LBMPs that does not conform to expectations under conditions of workable competition, the NYISO would be authorized to limit the hourly virtual load or supply bids in a zone of one or more Market Participants whose bids have been determined to be contributing to an unwarranted and substantial divergence in LBMPs. Any such limitation would be designed to be in an amount and for a duration sufficient to eliminate the detected divergence between Day-Ahead and Real-Time prices.

In keeping with existing Market Mitigation Measures procedures, a Market Participant would be consulted about the reasons for its bids, and would be notified of a limitation on the quantity of its Virtual Bids before such a limitation is imposed.

The proposed revisions to the Market Mitigation Measures would also authorize the NYISO to limit the Virtual Bid quantities of all Market Participants, if such an across-the-board measure is determined to be necessary to avoid substantial deviations between Day-Ahead and Real-Time LBMPs. Any such limitation would be implemented by having the Virtual Bids of each Market Participant individually limited by hour and by zone. A market-wide limitation would be used only if limitations focused on individual Market Participants would not be effective. Such a market-wide limitation should only be necessary to deal with a market-wide condition having an adverse effect on Virtual Bids, or to deal with a market-wide defect in Virtual Bidding practices or procedures, and would only be left in place for so long as the market-wide condition continued or for so long as necessary to remedy the design defect. While the NYISO does not currently anticipate that such conditions or defects will arise, prudence again dictates that appropriate tools be in place to deal with the unexpected.

Finally, in light of the novelty of Virtual Bidding, the proposed revisions to the Market Mitigation Measures would require the NYISO Market Monitoring Unit and the Market Advisor to monitor Virtual Bidding, and to report the results of this monitoring after each of the first four Capability Periods in which Virtual Bidding is permitted. Annual reports would be required thereafter. These reports would include, among other things, an assessment of the effects of Virtual Bidding, and any mitigation of Virtual Bids, on the NYISO's Automated Mitigation Procedures ("AMP"), and on the in-City Local Mitigation Measures administered by the NYISO in New York City.

#### IV. Description of Proposed Changes

The proposed mitigation measures for Virtual Bidding are set forth in a new Sec. 4.6 in Attachment H to the Services Tariff.

Subsection 4.6.1 sets forth the purpose of the Virtual Bid measures.

Subsection 4.6.2 sets forth the implementation methodology for Virtual Bidding mitigation, and is closely patterned on the load bidding mitigation measures in Sec. 4.4.2 of the currently effective version of Attachment H. Subsection 4.6.2 specifies that Virtual Bidding mitigation will be based on detection of a persistent hourly deviation between Day-Ahead and Real-Time LBMPs.

Subsection 4.6.3 describes the mitigation measures that may be imposed if an unwarranted deviation between Day-Ahead and Real-Time LBMPs is detected. Under subsection 4.6.3(a), the NYISO may limit the hourly quantities of the Virtual Bids of a Market Participant whose Virtual Bidding practices have been determined to contribute to an unwarranted divergence between Day-Ahead and Real-Time LBMPs, with the divergence generally measured over a rolling four week period. The quantity and duration of the limitation is to be no greater than necessary to remedy the price divergence. Subsection 4.6.3(b) requires the NYISO to consult with any Market Participant about the reasons for any Virtual Bids that may warrant mitigation. The NYISO is also obligated to notify the affected Market Participant in advance before imposing a Virtual Bidding limitation.

Subsection 4.6.4 authorizes the NYISO to impose limits on the quantities of Virtual Bids that may be offered by all Market Participants, if necessary in order to avoid substantial deviations of LBMPs between the Day-Ahead and Real-Time markets. Any such limitation would remain in place only for the minimum period necessary to remedy the price deviation or reliability problem.

Subsection 4.6.5 obligates the NYISO Market Advisor and Market Monitoring Unit to monitor and assess the impact of Virtual Bidding on the New York Electric Markets. The Market Advisor is required to report on the results of these efforts not later than 45 days after the end of each of the first four Capability Periods following the commencement of Virtual Bidding, and annually thereafter. Such reports are to include any recommendations of the Market Advisor or the Market Monitoring Unit for improvements in the New York Electric Markets, or in the monitoring and mitigation of Virtual Bidding.

#### V. Stakeholder Approval

The proposed revisions to Attachment H submitted herewith were approved by the NYISO Management Committee by a show-of-hands vote at its monthly meeting on September 11, 2001, and this filing was approved by the NYISO Board of Directors at its monthly meeting on September 18, 2001. Accordingly, pursuant to the provisions of Sec. 19.01 of the ISO Agreement, this filing is submitted under Sec. 205 of the Federal Power Act.

#### VI. Proposed Effective Date and Request for Waiver

In the September 4 filing, the NYISO stated, at 6, that:

The NYISO has determined that certain modifications to its market monitoring and mitigation tools should be in place before the virtual bidding is implemented. The NYISO is currently resolving the details of these modifications with its stakeholder committees and will soon make a filing proposing necessary revisions to its market monitoring and mitigation plan. In that filing, the NYISO will ask for expedited consideration so that the market monitoring and mitigation changes may become effective at the same time as the virtual bidding provisions proposed herein.

Accordingly, the NYISO respectfully requests that the Commission waive its usual sixty-day notice period and make this filing effective no later than November 1, 2001, pursuant to Section 35.11 of the Commission's regulations.<sup>5</sup> Waiver is appropriate in order to allow the proposed mitigation measures to go into effect coincident with the implementation of Virtual Bidding. Waiver and expedited treatment are also appropriate because the proposed measures have been reviewed and approved by the NYISO market participants, as well as the NYISO Board of Directors and the Market Advisor.

#### VII. Parties on whom Copies have been Served

The NYISO has mailed a copy of the filing to all parties that have executed Service Agreements under the NYISO's Open-Access Transmission Tariff or Services Tariff, to the

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<sup>5</sup> 18 C.F.R. § 35.11.

The Honorable David P. Boergers  
September 28, 2001  
Page 8

New York State Public Service Commission, the electric utility regulatory agencies in New Jersey and Pennsylvania and to all parties in Docket Nos. ER01-3001 and ER01-3009. In addition, in order to facilitate accelerated Commission action, the NYISO has e-mailed an electronic copy of this filing to all subscribers to the NYISO Technical Information Exchange (“TIE”) list, which encompasses virtually all NYISO Stakeholders.

VIII. Federal Register Notice

A form of *Federal Register* Notice is provided as Attachment III hereto. A diskette of the Notice is also provided in WordPerfect format.

IX. No Costs Relating to Discriminatory Employment Practices

The NYISO has no expenses or costs that have been alleged or judged to be illegal, duplicate, or unnecessary costs that are demonstrably the product of discriminatory employment practices.

X. Conclusion

WHEREFORE, for the foregoing reasons the New York Independent System Operator, Inc., respectfully requests that the Commission approve the proposed revisions to the NYISO Market Mitigation Measures, Attachment H to the Services Tariff, submitted herewith and implementing market mitigation measures for Virtual Bidding.

Respectfully submitted,

William F. Young  
Counsel for  
New York Independent System Operator, Inc.



The Honorable David P. Boergers  
September 28, 2001  
Page 9

cc: Alison Silverstein, Advisor to Commissioner Wood, Rm. 11B-3, Tel. 202/208-0388  
Mary C. Morton, Advisor to Commissioner Brownell, Rm. 10F-09, Tel. 202/208-0642  
Office of Commissioner Breathitt, Rm. 11C-3, Tel. 202/208-0377  
Wilbur C. Earley, Advisor to Commissioner Massey, Rm. 11D-2, Tel. 202/208-0366

Daniel L. Larcamp, Director, Office of Markets, Tariffs & Rates, Rm. 8A-01,  
Tel. 202/208-2088

Alice M. Fernandez, Director, Division of Tariffs & Rates-East, Rm. 82-15,  
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Andrea C. Wolfman, Lead Counsel for Market Oversight and Enforcement, Rm. 9E-01,  
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Stanley P. Wolf, Office of the General Counsel, Rm. 101-03, Tel. 202/208-0891

Michael A. Bardee, Lead Counsel for Markets, Tariffs & Rates, Rm. 101-09,  
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**ATTACHMENT I**  
**(Clean Revised Sheets)**

**ATTACHMENT II**  
**(Redline Sheets)**

**ATTACHMENT III**  
**(Notice)**

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document upon each person that has executed a Service Agreement under the NYISO's Open Access Transmission Tariff or Market Administration and Control Area Services Tariff, as well as the regulatory commissions of New York, New Jersey and Pennsylvania and to all parties in Docket Nos. ER01-3001-000 and ER01-3009-000 in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 2010 (2001).

Dated at Washington, D.C. this 28<sup>th</sup> day of September 2001.

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UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator, Inc.     )     Docket Nos. ER01-\_\_\_\_-000,  
ER01-3001-000 and ER01-3009-000

NOTICE OF FILING

Take notice that on September 28, 2001, the New York Independent System Operator, Inc. ("NYISO"), at the Direction of its independent Board of Directors, made a filing under Section 205 of the Federal Power Act to propose changes to Attachment H of its Market Administration and Control Area Services Tariff ("Services Tariff") designed implement market mitigation measures for virtual bidding. The NYISO has requested that the Commission act on this filing in an expedited manner and that it shorten the usual period for comments. The NYISO has also requested that the Commission waive its usual 60-day notice requirement and make the filing effective no later than November 1, 2001.

The NYISO has served a copy of the filing on all parties that have executed Service Agreements under the NYISO's Open-Access Transmission Tariff or Services Tariff, on the New York State Public Service Commission, on the electric utility regulatory agencies in New Jersey and Pennsylvania and on all parties in Docket Nos. ER01-3001-000 and ER01-3009-000. The NYISO has also emailed a copy of this filing to all of the subscribers to the NYISO's Technical Information Exchange list.

Any person desiring to be heard or to protest this filing should file a motion to intervene or protest with the Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426, in accordance with Rules 211 and 214 of the Commission's Rules of Practice and Procedure (18 C.F.R. §§ 385.211 and 385-214). All such motions or protests should be filed on or before \_\_\_\_\_. Protests will be considered by the Commission in determining the appropriate action to be taken, but will not serve to make protestants parties to the proceeding. Any person wishing to become a party must file a motion to intervene. Copies of this application are on file with the Commission and are available for public inspection.

David P. Boergers  
Secretary