UNITED STATES OF AMERICA 96 FERC ¶ 61,059
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Curt Hébert, Jr., Chairman;
William L. Massey, Linda Breathitt,
Pat Wood, III and Nora Mead Brownell.

New York Independent System Operator, Inc. Docket No. RT01-95-000

Central Hudson Gas & Electric Corporation
Consolidated Edison Company of New York, Inc.
Niagara Mohawk Power Corporation
New York State Electric & Gas Corporation
Orange & Rockland Utilities, Inc.
Rochester Gas & Electric Corporation

ORDER ON RTO COMPLIANCE FILING

(Issued July 12, 2001)

On January 16, 2001, New York Independent System Operator, Inc. (NYISO), and six of the members of the Transmission Owners Committee of the Energy Association of New York State (Member Systems)[1] filed a compliance filing in accordance with the Commission's Order No. 2000 on Regional Transmission Organizations (RTOs).[2]

[1] These six members are Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., Niagara Mohawk Power Corporation, New York State Electric & Gas Corporation, Orange & Rockland Utilities, Inc., and Rochester Gas & Electric Corporation. The Long Island Power Authority and the Power Authority of the State of New York, which are also members of the Committee, did not participate as applicants in the filing.

[2] Regional Transmission Organizations, Order No. 2000, 65 Fed. Reg. 809 (January 6, 2000), FERC Stats. & Regs. ¶ 31,089 (1999), order on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (March 8, 2000), FERC Stats. & Regs. ¶ 31,092 (2000), petitions for review pending sub nom., Public Utility District No. 1 of Snohomish County, Washington v. FERC, Nos. 00-1174, et al. (D.C. Cir).

As discussed below, we find that NYISO's compliance filing does not minimally satisfy several of the characteristics and functions set forth in Order No. 2000, which we deemed necessary to achieving RTO status.

In a companion order issued today in PJM Interconnection, L.L.C., et al.,[3] we provisionally grant RTO status to the PJM Interconnection, L.L.C. (PJM). In another contemporaneous order, issued in Bangor Hydro-Electric Company, et al.,[4] we grant in part, and deny in part, ISO-NE's request for a declaratory order seeking a determination that the New England RTO would satisfy Order No. 2000's requirements. Our directives in these orders are based, in part, on a finding that applies equally here, namely, that at a minimum, the Northeast United States constitutes a single region that should not be divided up into multiple RTOs. Consistent with these orders, we deny NYISO's application primarily because its proposed size does not meet the Scope and Regional Configuration Characteristic. However, we also find that its proposed governance structure does not satisfy the Independence Characteristic of Order No. 2000. We appreciate the time and effort invested by NYISO in developing its proposal. However, NYISO must negotiate with its neighbors and trading partners to form a single Northeastern RTO. Because the work undertaken on NYISO's proposal may be applicable to the Northeast region as a whole, we will address each of the RTO characteristics and functions as they apply to NYISO's filing. We expect that our order will provide guidance for negotiations to create a single Northeast RTO.

The Commission has been attempting to facilitate the development of large, regional transmission organizations reflecting natural markets since we issued Order No. 2000. We favor the development of one RTO for the Northeast, one RTO for the Midwest, one RTO for the Southeast and one RTO for the West. Through their independence from market participants, RTOs can ensure truly non-discriminatory transmission service and will instill confidence in the market that will support the billions of dollars of capital investment in generation and demand side projects necessary to support a robust, reliable and competitive electricity marketplace. RTOs are the platform upon which our expectations of the substantial generation cost savings to American customers are based.

While there will be "start up" costs in forming a larger RTO, over the longer term, large RTOs will foster market development, will provide increased reliability, and will result in lower wholesale electricity prices. However, these savings will be delayed, perhaps significantly, if RTOs are permitted to develop incompatible structures and systems, or if we approve RTOs that do not encompass wholesale market trading patterns. Accordingly, we today direct the parties in the Northeast and Southeast to mediation, under an expedited schedule.

## I. Background

[3] 95 FERC ¶ 61,____ (2001).

[4] 95 FERC ¶ 61,____ (2001).

In Order No. 2000, the Commission stated that a public utility that is a member of an existing Independent System Operator (ISO) that has been approved by the Commission as in conformance with the eleven ISO principles set forth in Order No. 888[5] must make an RTO filing no later than January 16 , 2001. We stated that this filing must explain the extent to which the ISO meets the minimum characteristics and functions for an RTO, and either propose to modify the existing institution to the extent necessary to become an RTO, or explain the efforts, obstacles and plans with respect to conforming to these characteristics and functions.[6]

NYISO states that it will satisfy all of Order No. 2000's requirements by its existing characteristics, bolstered by: (1) proposed changes to its tariffs and enabling agreements to clarify and reinforce its governance structure and to provide for a comprehensive transmission planning process; and (2) an intensification of efforts to more closely coordinate its markets and operations with those of neighboring transmission entities in the PJM region, New England and Ontario. NYISO states that its RTO proposal is the result of an extensive open process in which all of its market participants were invited to participate, and that it was approved by the NYISO Board of Directors, the Member Systems, and the NYISO Management Committee. NYISO requests that the Commission rule that NYISO's proposed RTO complies with Order No. 2000.

## II. Notices and Responsive Pleadings

Notice of NYISO's filing was published in the Federal Register,[7] with interventions, comments, or protests due on or before February 22, 2001. Notices of intervention and motions to intervene were submitted by the entities listed in the Appendix to this order. Protests and comments were filed by the parties noted below in the discussion section of this order and are also noted in the Appendix.[8]

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[5] Promoting Wholesale Competition Through Open Access Non-discriminatory transmission services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 Fed. Reg. 21,540 (1996), FERC Stats. & Regs. ¶ 31,036 (1996), order on reh'g, Order No. 888-A, 62 Fed. Reg. 12,274 (1997), FERC Stats. & Regs. ¶ 31,048 (1997), order on reh'g, Order No. 888-B, 81 FERC ¶ 61,248 (1997), order on reh'g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), aff'd in relevant part, remanded in part on other grounds sub nom., Transmission Access Policy Study Group, et al. v. FERC, 225 F. 3d 667, Nos. 97-1715 et al (D.C. Cir.), cert. granted in part, New York v. FERC, 121 S.Ct. 1185 (2001).

[6] Order No. 2000 at 30,994-5.

[7] 66 Fed. Reg. 8,214 (2001).

[8] The Appendix lists abbreviations used throughout this order to identify the parties that filed comments, answers, and protests.

Answers to protests and answers to answers were filed by NYISO; Central Hudson Gas & Electric, Long Island Power Authority, New York State Electric & Gas Corporation, and Rochester Gas and Electric Company; Member Systems; Public Service Commission of the State of New York.

On February 23, 2001, Enron Power Marketing, Inc. filed a motion to consolidate NYISO's RTO filing with PJM's RTO proposal filed in Docket No. RT01-2-000 and ISO-NE's RTO filing in Docket No. RT01-86-000 and to appoint a settlement judge. Responsive pleadings were filed by NYISO; Central Hudson Gas & Electric, Long Island Power Authority, New York State Electric & Gas Corporation, and Rochester Gas and Electric Company; Member Systems; New York State Reliability Council; PJM Industrial Customer Coalition; ISO New England Inc.; PJM Interconnection, L.L.C.; New York State Electric & Gas Corporation; Shell Energy Services Company, L.L.C.; New England Conference of Public Utilities Commissioners and Vermont Department of Public Service. We will accept Enron's protest and the pleadings filed by the parties in response to this protest. These pleadings clarify the issues and enhance our understanding of the proceeding. Further, we deny Enron's request that we the Commission appoint a settlement judge and establish other procedures, as discussed below.

## III. Procedural Matters

Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,[9] the notices of intervention and the timely, unopposed motions to intervene submitted by the entities noted in the Appendix to this order serve to make them parties to this proceeding. In addition, we will accept the unopposed late-filed interventions submitted by Connecticut Department of Public Utility Control; Edison Mission Energy, Edison Mission Marketing & Trading, Inc. and Midwest Generation EME, LLC; Long Island Power Authority and LIPA; New York State Reliability Council; and Ontario Independent Electricity Market Operator.

## IV. RTO Characteristics

### RTO Characteristic No. 1: Independence: The RTO must be independent of any market participant

#### 1. NYISO's Proposal

NYISO argues that its proposal meets the independence criteria, primarily because NYISO has already been authorized by the Commission as an ISO under Order No. 888. NYISO indicates that it is proposing certain modifications to NYISO's enabling agreements solely to clarify the relationship between the ISO staff and the several ISO committees. NYISO states that because the

[9] 18 C.F.R. § 385.214 (2000).

Commission has previously found its governance structure and existing sector voting rules to be sufficient to protect the NYISO's independence, there is no reason for the Commission to alter its conclusion in this proceeding.

According to NYISO, its governance structure will continue to be based upon the delegation of considerable responsibility for overall NYISO management to committees of market participants. It states that Order No. 2000 notes that NYISO's decisionmaking is shared by a non-stakeholder Board of Directors and stakeholder Management Committee.[10] NYISO will continue to rely on sector voting procedures and the NYISO Board's review of committee actions to prevent any market participant (or class thereof) from dominating the RTO.

NYISO's Board has the authority to make Section 205 filings with the Commission on its own motion, without prior approval by the Management Committee, in exigent circumstances. However, that filing will automatically expire 120 days after filing unless the Management Committee files with the Commission a written concurrence, or the Commission acts upon the filing under section 206 of the Federal Power Act (FPA).[11] NYISO proposes to extend this period to 180 days.

2. Intervenors' Comments

Several parties argue that NYISO's proposal does not meet the independence requirement. Enron asserts that the RTO will not be independent of the parochial interests of transmission owners represented by the New York State Reliability Council (NYSRC). Enron claims that NYSRC is dominated by stakeholders, and retains substantial authority to establish local reliability rules and practices. Sithe claims that the authority retained by stakeholders is inappropriate, and that stakeholder governance should be replaced by a fully independent Board of Directors. In particular, Sithe asserts that NYISO's shared governance proposal will lead to incessant governance and independence problems which will require constant resort to the Commission to achieve resolution. Morgan Stanley states that NYISO's lack of full operational control over the transmission grid will impair its independence from market participants. The New York Commission states that it has found the NYISO governance and committee structure to be inefficient and cumbersome, and that it would expect any new structure to be more refined.

Reliant argues that NYISO will be susceptible to excessive influence by the Public Service Commission of the State of New York (New York Commission) and New York's own politics and priorities. Shell asserts that the proposed governance structure may have been appropriate for an ISO operating under Order No. 888, but is inadequate to meet the independence criteria for an RTO. Shell also contends that NYISO's proposal to retain a weighted voting formula hampers independence.

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[10] Order No. 2000 at 31,073 n.329.

[11] 16 U.S.C. § 824e (1994)

Williams claims that the independence of the proposed RTO is "fatally undermined" by the power retained by the Management Committee, and by the ability of certain NYISO stakeholder committees to act even in the face of the NYISO Board disapproval. EPSA likewise argues that the proposed RTO's continuation of the ISO's shared governance structure would impair the RTO's independence by giving market participants control over key RTO decisions.

Other parties claim that NYISO's proposal is only a modest change from the existing ISO structure.

3. NYISO's Answer

NYISO denies that its single-state status will make it susceptible to undue influence by the New York Commission and asserts that its shared governance structure will satisfy the Commission's RTO requirements because the structure satisfied the Commission's ISO requirements.

4. Discussion

In several orders, the Commission has reiterated the requirement in Order No. 2000 that the independence of an RTO from control by market participants is of critical importance.[12] The Commission has stated that RTOs "need to be independent in both perception and reality."[13] The Commission's regulations require that:

> (1) ... The Regional Transmission Organization must be independent of any market participant. The Regional Transmission Organization must include, as part of its demonstration of independence, a demonstration that it meets the following: (i) The Regional Transmission Organization, its employees, and any non-stakeholder directors must not have financial interests in any market participant. (ii) The Regional Transmission Organization must have a decision making process that is independent of control by any market participant or class of participants. (iii) The Regional Transmission Organization must have exclusive and independent authority under section 205 of the Federal Power Act (16 U.S.C. 824d), to propose rates, terms and conditions of transmission service provided over the facilities it operates. [note: Transmission owners retain authority under section 205 of the Federal Power Act (16

[12] See, e.g., Alliance Companies, et al., 94 FERC ¶ 61,070 (2001).

[13] Order No. 2000 at 31,061.

U.S.C. 824d) to seek recovery from the Regional Transmission Organization of the revenue requirements associated with the transmission facilities that they own.][14]

NYISO correctly notes that its organizational governance plan, which was implemented to comply with Order No. 888, was accepted by the Commission in that context. However, NYISO's assertion that compliance with the Commission's requirements for ISOs satisfies the Commission's RTO requirements is not correct. The Commission's approval of the governance of an ISO is not equivalent to Commission approval of the independence of an RTO.

Identical to its ISO governance structure, NYISO's proposed RTO governance structure gives responsibility for decision making to market participants that compose various ISO committees. We are concerned that NYISO's governance structure may allow market participants to exert undue influence over the decision-making process. As we explain below in our discussion of the Tariff Administration function, NYISO's RTO proposal does not meet the minimum requirements of that function, because it lacks the requisite Section 205 filing authority.

Since we find below that NYISO's scope and regional configuration also fails, and that the regional RTO must incorporate other transmission entities, we will not discuss possible governance remedies for NYISO at this time. An RTO must limit the authority of committees of the type NYISO employs to an advisory role, at most.

RTO Characteristic No. 2: Scope and Regional Configuration: The RTO must serve an appropriate region

1. NYISO's Proposal

NYISO asserts that its existing size meets the requirements set forth in Order No. 2000 regarding scope and regional configuration. NYISO argues that its size is sufficient because it encompasses a contiguous geographic area, as well as a highly interconnected portion of the grid, and also comprises an existing control area. NYISO also states that its size has proven to be sufficiently large to properly manage transmission congestion and help deter the exercise of market power. Furthermore, NYISO argues that its scope is sufficient because its present size is large enough to effectively operate a statewide Open Access Same-Time Information System (OASIS) and make accurate and reliable Available Transmission Capability (ATC) calculations.

In the long run, NYISO claims that it is actively pursuing interregional coordination arrangements that will result in the elimination of seams issues among the Northeastern ISOs and create

[14] 18 C.F.R. § 35.34(j)(1) (2000).

a "virtual" RTO in the Northeast. NYISO contends that this Northeastern virtual RTO will meet Order 2000's requirements by its large scope. NYISO is pursuing the establishment of the virtual RTO through: (1) its participation in the Northeastern ISOs' Memorandum of Understanding process (MOU);[15] (2) its sponsorship of a feasibility study concerning the creation of an integrated Northeastern day-ahead energy market; (3) its involvement in the Northeast Power Coordinating Council's (NPCC) interregional coordination program; and (4) its execution of emergency services agreements with PJM and ISO-NE. In addition, NYISO states that the boards of NYISO and ISO-NE have recently executed an agreement that will create a joint task force to expedite the MOU process and to coordinate the two ISOs' market monitoring activities.

NYISO states that the Commission should encourage the Northeastern ISOs to develop the virtual RTO, including the Ontario Independent Market Operator (IMO), while the Northeastern ISOs consider whether further functional or structural integration, including possible mergers or other alternative RTO structures, is warranted. NYISO claims that a premature and inadequately considered attempt to move toward an RTO merger could be disruptive and wasteful and result in a degradation of system reliability and disruptions in the competitive markets. It further states that it cannot be assumed that a single operator would be able to maintain the real-time security of the Northeast's transmission grid.

2. Intervenors' Comments

Some intervenors, while generally supporting NYISO's RTO proposal, request that the Commission accept NYISO's filing conditioned upon demonstration of the ability of the three Northeastern ISOs to create a regional market. The NY City of and the New York Commission propose to impose a reporting requirement providing for quarterly status reports until interregional coordination issues are fully resolved. Aquila argues that the Commission should condition its approval of the proposal upon more extensive interregional coordination. NYSEG claims that the MOU process to

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[15] The Memorandum of Understanding was entered into by ISO-NE, NYISO, and PJM on August 9, 1999. The stated goals of the MOU agreement are to: (1) place a high priority on studying the feasibility of increasing intertie capacity as a part of the respective regional transmission planning activities, in the interest of enhancing bulk power supply reliability and facilitating more robust trading on an interregional basis; (2) identify and address market interface issues with the goal of facilitating broader competitive markets; (3) proactively engage forums and support user groups whereby market participants or other interested parties can promulgate ideas, suggestions, or concepts to achieve the purposes of the agreement; and (4) require cognizant staff of the ISOs to report periodically to the ISO Chief Executive Officers, market participants and other constituencies on the status and progress of their joint interregional coordination activities.

date has been plagued by inconsistent ISO and market participant participation and diligence in deliverable work product. NRG argues that a lack of progress by the MOU process means that it is unreasonable to rely on this and other voluntary mechanisms to fulfill the integration of markets mandated by the scope characteristic of Order No. 2000. NRG requests a more structured process to reach interregional coordination goals involving Commission oversight. These intervenors have reservations about the proposal and claim that the concept of an effective virtual RTO will remain dubious until a more detailed plan and timetables are submitted.

Some intervenors object to the concept of interregional coordination as a substitute for scope. Williams argues that seams problems can be best resolved through the formation of a single Northeast RTO. Morgan Stanley, while supporting NYISO's efforts at interregional coordination to date, argues that the Northeast ISOs should be required to submit a plan for all proposed Northeast RTOs to merge their operations and form one Northeast RTO within a specified period of time. PPL contends that immediate benefits of a single RTO will be realized in areas such as pancaked rate elimination, parallel path flow issues, congestion management, regional congestion, transaction coordination, transmission grid expansion, software improvement, disparate market operating procedures and other rule discrepancies that impede energy trading.

Many intervenors find the NYISO-proposed scope and configuration to be simply insufficient. They argue that the proposal falls short of the integration between the ISOs that is necessary to further the Commission's goals regarding scope and regional configuration. Calpine dismisses the concept of a single state RTO. It argues that NYISO's proposal provides for an opportunity to structure an RTO to the advantage of internal interests, not interregional coordination. Reliant contends that NYISO and -- if accepted -- the New York RTO are subject to the influence of the New York Commission and New York's political leadership, as well as the indirect oversight of key market participants. Enron argues that the lack of standardized interregional market rules and interface practices proves that the scope and configuration requirements have not been met. Enron argues that separating New York from the rest of the Northeast region divides patterns of both existing and potential trade that could reduce reserve requirements and produce other economies for the region.

Also, Enron states in its motion to appoint a settlement judge that the Northeast should be one RTO, not three. Enron believes that a settlement judge is needed to develop milestones for achieving the various steps needed for unification of the three Northeast ISOs. If the three RTO proposals are accepted, Enron states that they should only be accepted on condition that they unite promptly, no later than Fall 2002. Various parties filed answers and comments either in support or in opposition to Enron's protest and motion.

3. NYISO's Answer

NYISO defends its proposed scope as sufficient to qualify it as an RTO. NYISO states that it did not claim to be creating an ideal RTO, but rather it was focusing, as a first step, on ensuring its full compliance with all of Order No. 2000's requirements while building the consensus necessary to make a voluntary RTO filing. It claims that it is proposing a realistic approach aimed at maximizing the benefits to the Northeastern energy market as quickly as possible while minimizing the time and effort spent on secondary structural issues. NYISO claims that in the short-term, it is focusing on inter-ISO coordination to ensure its compliance with Order No. 2000's scope, configuration, and interregional coordination requirements. It states that in the longer term, these efforts will provide the foundation for greater functional and, if it is determined to be appropriate, structural integration. NYISO states that it would be irresponsible to risk major market and reliability disruptions by rushing haphazardly to adopt a single RTO structure.

NYISO claims that its proposed virtual scope is similar to that of GridSouth, whose scope the Commission provisionally accepted as a starting point to serve as a platform for the formation of a larger RTO in the Southeast.[16] It argues that the Commission should not treat NYISO and GridSouth differently.

4. Discussion

In Order No. 2000, we held that an RTO must serve an appropriate region, i.e., a region of sufficient scope and configuration to permit the RTO to effectively perform its required functions and to support efficient and non-discriminatory operation of power markets.[17] We also stated that in evaluating an RTO's proposed scope and regional configuration, we would consider, among other things, the extent to which the proposed boundaries recognize trading patterns:

> Given that a goal of this initiative is to promote competition in electricity markets, regions should be configured so as to recognize trading patterns, and be capable of supporting trade over a large area, and not perpetuate unnecessary barriers between energy buyers and suppliers. There may exist today some infrastructure or institutional barriers unnecessarily inhibiting trade between regions that could be economically reduced. RTO boundaries should not perpetuate these unnecessary and uneconomic boundaries.[18]

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[16] See Carolina Power & Light Company, et al., 94 FERC ¶ 61,273 (2000).

[17] Order No. 2000 at 31,079.

[18] Order No. 2000 at 31,084.

Applying this criterion, we note, first, that interregional trading among the three Northeastern ISOs is significant and growing.[19] Indeed, to a certain extent, the Northeastern ISOs rely on each other to meet their energy needs, whether to acquire supplies or to sell unused capacity.[20] The interconnected nature of this market is often reflected in the Northeastern ISOs' respective market prices.[21] As this evidence suggests, there is a natural market which spans the Northeast region.

However, the vitality of this natural market is hampered by the balkanized set of market rules that have developed in the Northeastern ISOs since their inception. These market rules vary in numerous ways, from limits placed on ramping rates for external transactions to the manner in which transmission rights are allocated and from transaction scheduling to the type of ancillary services available in the spot market. Moreover, the divergence of these rules creates uncertainty among market participants and may discourage trade among the Northeastern ISOs.[22] In sum, the narrow configuration of the existing Northeastern ISOs creates artificial constraints within the broader market that spans the Northeastern region.

We note that the Northeast ISOs have recognized the constraints placed on trade by their different market rules, and have entered into a MOU that sets forth their commitment to seek

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[19] NYISO, for example, reports that energy imports of 1000 MW or greater into NYISO from PJM were scheduled approximately 56 percent of the time during the year 2000. NYISO's exports to New England of at least 500 MW or more were scheduled approximately 37 percent of the time, and NYISO scheduled imports from ISO-NE approximately 12 percent of the time. See New York Independent System Operator, Inc.'s Combined Compliance Filing and Report, Docket No. ER00-3591-000, Attach. VI (Ricardo T. Gonzales Aff.) (September 1, 2001).

[20] NYISO notes that in the year 2000 it was a net importer of energy, importing energy about 97 percent of the time. In January 2000, import energy scheduled from neighboring control areas exceeded 1000 MW nearly 85 percent of the time, and exceeded 2000 MW 34 percent of the time. Id.

[21] In January 2001, for example, ISO-NE's 5-minute energy clearing price was set by external dispatchable contracts 14.6 percent of the time. See ISO-NE's January 2001 Monthly Market Report, at 12.

[22] In March 2000, for example, PJM threatened to discontinue prescheduling transactions with the NYISO due to the frequency of transaction curtailments imposed by the NYISO under its market rules. See New York State Electric & Gas Corporation's Complaint, Docket No. EL00-70-000, Attach. B (Letter from Bruce M. Balmat, PJM Vice President, System Operations Division, to Charles King, NYISO Vice President, Market Services, of 03/20/00) (April 24, 2000).

interregional coordination amongst themselves.[23] Pursuant to the MOU and its spirit of greater coordination, the Northeastern ISOs have taken some preliminary steps toward addressing constraints on trade, including: (i) sponsoring of a study addressing the feasibility of implementing a combined day-ahead energy market for the Northeast; (ii) an agreement that provides for the sharing of 10-minute reserves between the NYISO and ISO-NE; (iii) an interregional congestion management redispatch mechanism that may be implemented between PJM and the NYISO; and (iv) a commitment among the Northeastern ISOs to identify and implement the "best practices" followed by each.

These efforts, which, at the outset looked promising, have proved disappointing. In fact, the MOU process does not go far enough to address seams issues in the Northeastern market. This may be due to the fact that the MOU process, to date, has failed to comprehensively address the fundamental market rule differences that exist in the region.. The existing MOU process is insufficient to be considered a sufficiently strong cooperative agreement with neighboring RTOs to establish a "seamless" trading area. The MOU process has resulted in missed deadlines and few significant solutions that address the seams issues and market design differences between the three Northeast ISOs. We find that the existing MOU process has not been effective in addressing the competitive goals set forth by the Scope and Interregional Coordination features of Order No. 2000.

In Order No. 2000, we held that an RTO application that proposes to rely on "effective scope" to satisfy our scope requirement would be required to show that its plan would be the functional equivalent of a larger RTO.[24] NYISO has not demonstrated that a seamless, virtual RTO, even were it to be achieved, would be the functional equivalent of a single Northeastern RTO.

NYISO must work with its neighbors and trading partners to form a single, fully-integrated RTO with a single set of market rules and one market design in the Northeast . In a contemporaneous order acting on PJM's RTO proposal, we conclude that while PJM's proposed scope and configuration are provisionally consistent with Order No. 2000, it represents only a first step, a platform which must be built upon. PJM must be open to changes and improvements suggested by others . We encourage the three ISOs to look at the best practices in all three ISOs to develop market rules for a Northeast RTO.

In order to facilitate formation of single RTO in the Northeast, we are issuing concurrent with this order, a separate order that directs the parties in this proceeding and the parties in the proceedings in Docket Nos. RT01-86-000 (New England), RT01-2-000 (PJM), and RT01-98-000 and RT01-10-000 (PJM West), to participate in settlement discussions for 45 days before a mediator

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[23] The MOU was executed by ISO-NE, the NYISO and PJM in August 1999. The Ontario IMO joined the MOU later in 1999.

[24] Order No. 2000 at 31,083.

and appropriate consultants to assist and provide advice during the mediation.[25] The order directing mediation requires the mediator to file a report within 10 days after the 45 day period, which includes an outline of the proposal to create a single Northeastern RTO, milestones for completion of intermediate steps and a deadline for submitting the joint proposal. We intend to review the report and may issue a subsequent order.

We encourage the state commissions to actively participate in these efforts. We believe their participation will further the resolution of this matter. Similarly, we encourage Canadian entities that are part of the NPCC to participate in the discussions to the extent consistent with their status as subjects of a foreign sovereign nation.

RTO Characteristic No. 3: Operational Authority: The RTO must have operational authority for all transmission facilities under its control

1. NYISO's Proposal

NYISO asserts that, as currently organized, it fully complies with the operational authority characteristic requirement. NYISO, therefore, does not propose to amend the operational authority, which it now possesses as an ISO. NYISO states that it has day-to-day operational control over the transmission facilities that are its responsibility, and notes that it is the security coordinator for the New York Control Area (NYCA). NYISO acknowledges that its member transmission owners retain authority to re-assert control over the transmission system in the event of certain emergencies. NYISO commits to re-assess its operational authority over transmission facilities after two years of operation, and to then propose any needed modifications.

2. Intervenors' Comments

Morgan Stanley asserts that NYISO's claims of operational authority are inadequate, because NYISO has no operational control over significant facilities. Morgan Stanley is particularly concerned that NYISO's lack of authority over phase angle regulators will impair its control over the transmission system.

Enron asserts that excessive operational authority remains vested in NYISO's transmission owners and LIPA, thereby limiting NYISO's actual operational authority. Enron claims that a

[25] 65 FERC ¶ 61,--- (2001).

transmission owner may trump NYISO's scheduling instructions for its own economic reasons, thereby impairing competition and inappropriately limiting NYISO's operational authority.

3. NYISO's Answer

NYISO claims that transmission owners may reassert rights to control the grid only under limited circumstances, such as emergencies. NYISO also says that it has already answered arguments concerning its operational authority over particular facilities in a pleading filed in another proceeding,[26] which it incorporates by reference.

4. Discussion

NYISO's proposal addresses many of the Commission's concerns in connection with operational authority.[27] For example, NYISO serves as security coordinator for the facilities it controls. However, in other respects, NYISO's proposal does not fully meet the Commission's requirements for this RTO characteristic.

Reserving to transmission owners the right to re-assert operational control during emergency periods could enable those market participants to affect operation of the transmission grid when it may be most constrained or facing peaking demands. A transmission owner should not have the authority to unilaterally revoke the RTO's operational authority over transmission facilities.

An RTO proposal must explain why certain transmission facilities or transmission-related facilities are excluded from its operational authority. For example, should NYISO not have full operational authority over phase angle regulators, it must justify that. We find that NYISO's commitment to re-assess the adequacy of its operational authority two years after its commencement of service does not substitute for seeking, at start-up, to include within its control all facilities necessary in order to provide transmission service. After all, we set as our goal in Order No. 2000 the creation of viable, stand-alone transmission businesses. An RTO with insufficient operational authority at the outset cannot qualify as "viable."

RTO Characteristic No. 4: Short-Term Reliability: The RTO must have exclusive authority for maintaining the short-term reliability of the grid that it operates

1. NYISO's Proposal

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[26] New York Independent System Operator, Inc.'s Reply Comments, Docket No. ER00-3591-000, et al., (Feb. 21, 2001).

[27] See 18 C.F.R. § 35.34(j)(3)(2000).

NYISO claims that it meets the requirements of RTO Characteristic No. 4 because it has the responsibility for short-term reliability matters. It states that it has authority to receive, confirm and implement all interchange schedules, the authority to balance generation and load, to dispatch and redispatch all generation bidding into its Locational Based Marginal Price (LBMP)[28] markets, and authority over bilateral transactions involving the NYCA. It states that it has the right to coordinate maintenance schedules and approve outage schedules for bulk power transmission facilities that are under its operational control. It states that transmission owners are permitted to schedule outages of non-NYISO-controlled transmission facilities, but must notify the NYISO. It also states that because the NYISO operates under reliability standards that are established by North American Electrical Reliability Council (NERC), the Northeast Power Coordinating Council (NPCC) and the NYSRC, it will monitor the effects of these standards and will report to the Commission in the event that it concludes that these standards are hindering its ability to provide reliable, non-discriminatory, and efficiently-priced transmission service.

2. Intervenors' Comments

Williams agrees that NYISO's RTO proposal minimally satisfies Characteristic No. 4. However, Williams argues that as presently structured, NYISO's shared governance proposal, allowing the three stakeholder committees to impermissibly intrude upon decision-making authority of the Board, could undermine the effectiveness of the Board to ensure the short-term reliability of the grid.

3. Discussion

Order No. 2000 requires that an RTO: (i) must have exclusive authority for receiving, confirming and implementing all interchange schedules; (ii) must have the right to order redispatch of any generator connected to transmission facilities it operates if necessary for the reliable operation of these facilities; (iii) when the RTO operates transmission facilities owned by other entities, it must have authority to approve and disapprove all requests for scheduled outages of transmission facilities to ensure that the outages can be accommodated within established reliability standards; and (iv) if the RTO operates under reliability standards established by another entity (e.g., a regional reliability council), the RTO must report to the Commission if these standards hinder its ability to provide reliable, non-discriminatory and efficiently priced transmission service.[29]

We agree that NYISO meets our Order 2000 requirements for Short-Term Reliability. Our review of NYISO's Market Administration and Control Area Services Tariff (Services Tariff), its Open Access Transmission Tariff (OATT), its ISO/Transmission Owners agreement, its ISO Agreement, and

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[28] LBMP is a pricing methodology under which the price of energy at each location in the New York transmission system is equivalent to the cost to supply the next increment of load at that location.

[29] Order No. 2000 at 31,092.

its ISO/NYSRC agreement confirm that NYISO has exclusive authority for maintaining the short-term reliability of the grid that it operates.

Williams argues that NYISO's governance structure may have implications for the proposed RTO's ability to ensure short-term reliability. However, because we address the problems of NYISO's independence above, we will not address it further here.

RTO Function No. 1: Tariff Administration and Design: The RTO must administer its own transmission tariff and employ a transmission pricing system that will promote efficient use and expansion of transmission and generation facilities

1. NYISO's proposal

NYISO believes that it meets these requirements and that the changes it proposes will further reinforce its independence and filing authority. It states that the Commission has accepted NYISO's currently effective interconnection procedures for merchant generators that do not seek to obtain transmission service separately, and previously held that NYISO's current OATT provisions governing the interconnection of new transmission facilities are consistent with or superior to those of the pro forma OATT. It also reports that in response to the Commission's directive that NYISO and market participants jointly develop guidelines for cost responsibility with regard to new interconnections, NYISO and market participants have formed an Interconnection Issues Task Force that has completed several projects and will complete its work well before December 2001. Finally, it states that previous Commission orders, including Order No. 2000, have determined that NYISO's OATT eliminates rate pancaking for the use of multiple systems.

2. Intervenors' Comments

Williams disagrees that NYISO meets the Function No. 1 requirements. It believes that a serious question exists as to the exclusivity of the NYISO Board's authority with respect to interconnection requests and its independence to make tariff modifications. EPSA makes a similar argument and asserts that PJM already has Commission-approved interconnection procedures in effect, which could be adopted by NYISO. EPSA also argues that NYISO, not the transmission owners, should be responsible for ensuring timely completion of studies and negotiations of transmission upgrades.

Enron argues that NYISO should allow virtual bidding and also asserts that NYISO should be the sole entity that bills for the transmission service it provides. Enron maintains that billing is currently too complex and subject to numerous revisions, and that NYISO's transmission service charges for exports or wheel transactions are based on various factors that result in a large number of prices (over 1200) that vary by source bus and sink region.

Dynegy asserts that NYISO's interconnection procedures are inadequate when compared with the detailed interconnection procedures filed with the Commission recently by other transmission providers which, among other things, include procedures for requesting interconnection service and the criteria for evaluating those requests. Dynegy believes that NYISO should be required to file interconnection procedures, which, among other things, provide for standardized forms to be posted on the New York RTO's OASIS, and flexibility to allow for generator construction of facilities. In addition, Dynegy maintains that interconnection studies must be undertaken pursuant to clear and consistent study timelines and a study model that realistically portrays the RTO's system.

Morgan Stanley asserts that the recent California utility defaults on California ISO transactions demonstrate that the tariff for any RTO must have clear and comprehensive provisions that identify events of default and defaulting counterparties, provide specific and meaningful remedies for defaults, and specify the order in which those remedies will be implemented.

3. Discussion

Order No. 2000 requires that the RTO be the sole administrator of its own open access tariff and have the independent authority to file tariff changes.[30] Exclusive tariff filing authority is also critical to fulfilling the requirement of the Independence characteristic.[31] NYISO's Board can only make Section 205 filings on its own motion, absent market participant committee approval, under exigent circumstances. The Commission finds that NYISO does not meet the requirements of RTO Function No. 1.

The Commission shares the concern of EPSA and Williams that NYISO, and not the transmission owners, be responsible for the processing of interconnection requests.

Dynegy and EPSA make a strong argument that NYISO's interconnection procedures are inadequate compared to the detailed procedures of other ISOs, RTOs and utilities. Because we are requiring a single, fully-integrated RTO in the Northeast, we expect that this issue will be addressed within that process. Also, the Commission intends, in the near future, to evaluate the importance of standardizing generation interconnection procedures.

NYISO states that virtual bidding is scheduled to be implemented by Fall 2001. The Commission will not address this issue further in this proceeding. However, we encourage NYISO and the parties to simplify the export and wheeling transaction billing process described by Enron.

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[30] Order No. 2000 at 31,108.

[31] Id. at 31,075.

Similarly, the Commission will not here address Morgan Stanley's proposal concerning utility default procedures, although Morgan Stanley is free to pursue that proposal through the NYISO committee process and other proceedings at this Commission, as appropriate.

> RTO Function No. 2: Congestion Management: The RTO must ensure the development and operation of market mechanisms to manage transmission congestion. The RTO must satisfy the market mechanism requirement no later than one year after it commences initial operation. However, it must have in place at the time of initial operation an effective protocol for managing congestion

1. NYISO's Proposal

NYISO notes that, consistent with the example of the PJM Locational Marginal Price (LMP)[32] congestion management system described in Order No. 2000, it employs a Commission-approved LBMP system and uses transmission congestion contracts (TCC) to establish financial rights for firm transmission service. NYISO asserts that the NYISO LBMP system has been recognized by the Commission as comparable to PJM's LMP system.[33] NYISO states that it has implemented LBMP and TCC auctions successfully and that it administers its congestion management system independently of any control or affiliation with any market participant. Further, NYISO is conducting a study of the possibility of an inter-ISO congestion management system to more efficiently coordinate its own congestion management with that of its neighbors.

2. Intervenors' Comments

Enron claims that NYISO has not adopted a market mechanism for managing inter-RTO congestion that recognizes firm transmission rights. Enron notes that the TCC, when added to the LBMP to create financial rights, may arguably work intra-RTO, but that such mechanisms do not allow for exchanges between RTOs because they are coordinated on a physical basis and because each RTO uses a different market model to calculate prices. Further, Enron notes that the proposed scope of the RTO does not internalize parallel path flows, which compromises congestion management and the ability to determine accurate ATC. Enron says that the PJM congestion management system works through use of the LMP and a fixed transmission right (FTR), which

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[32] See Pennsylvania-New Jersey-Maryland Interconnection, et al., 81 FERC ¶ 61,257 (1997) , clarified, 82 FERC ¶ 61,068 (1998), on reh'g, 92 FERC ¶ 61,282 (2000).

[33] See Central Hudson Gas & Electric Corporation, et al., 86 FERC 61,062, at 61,223 (1999).

Enron notes is a financial hedge. Enron recommends that this model be used to implement a Northeast Regional congestion management system, with the exception of PJM's administrative allocation of FTRs to existing firm customers only.

Dynegy says that congestion management proposals should address the needs of the market and be market-driven. Dynegy suggests that the industry's experience with highly structured markets is that they are slow to adapt, unwieldy, and always behind the curve. It suggests that any congestion model be judged against its ability to serve the needs of the customer, which are described as liquidity, certainty of price, certainty of delivery, and transmission flexibility. Dynegy claims that LMP, when judged against these standards, lacks as a congestion management system. It suggests that other models, such as flowgate and zonal pricing, hold a great deal of promise. Dynegy requests that the Commission express its openness to other options for congestion management.

Calpine argues the NYISO-proposed congestion management system does not meet the Commission's requirement that such a system provide all transmission customers with efficient price signals, nor is it a market-based approach. Calpine states that the LBMP and TCC approach, along with numerous NYISO market interventions to correct prices have resulted in a very complicated transmission regime that breeds confusion and pricing disputes. Calpine charges that the slow pace of corrections to the Balancing Market Evaluation (BME) software,[34] which NYISO sees as an essential element of the congestion management system, has resulted in market uncertainty and erroneous transactions cuts, and has unnecessarily added to transmission costs and uncertainty of price signals. Calpine suggests use of the PJM model, which consolidates exports and imports into one billing settlement within the pool. Finally, it says that the short-term nature of the TCC, being only 6 months in duration, creates instability in generation investment and results in lower liquidity in the market as the lack of long-term firm transmission rights hinders the ability of participants to enter into forward contracts for their requirements.

Williams recommends that the Commission adopt a uniform congestion management strategy. Its congestion management system would be a hybrid of LMP with generators receiving a nodal price at the point of injection, customers paying a zonal price, and firm financial transmission rights established between all pricing points, to be auctioned off with the full ability to establish a secondary market for these rights. Revenues from the auction of rights would be committed to the offset of

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[34] BME is a computer algorithm that forecasts operations in the hour-ahead market and computes advisory prices based on these conditions.

congestion on the path for which the rights were purchased. Williams claims that congestion management system lacks details regarding firm transmission rights. Williams believes that the market participants should bid on all FTRs within the system to facilitate a more open, efficient and liquid market.

3. NYISO's Answer

NYISO states that intervenors' suggestions that the existing financial based transmission reservation system be replaced with a physical system should be rejected as beyond the scope of this proceeding. It notes that the Commission has approved NYISO's financial-based system. Further, NYISO alleges that intervenors have not presented any evidence that a physical reservation system is superior to the current financial-based reservation system. NYISO states that it is considering revisions to the ISO interface systems in response to known seams issues and request the Commission not to prejudge the question.

4. Discussion

The congestion management system will need to be redesigned to take into consideration the requirements of a larger market. We note that a number of market participants filed complaints in regard to NYISO's congestion management practices.[35] The parties in the Northeast RTO discussions should pay attention to the comments of intervenors in this case when preparing a new congestion management proposal.

Enron, Calpine, and NYISO refer to the PJM LMP method of congestion management noted in Order No. 2000.[36] We affirm that LMP is an acceptable approach to congestion management. However, the Commission does not prescribe any particular congestion management scheme, and the parties are free to propose an alternate method. Enron says that the various congestion management approaches of the ISOs are inconsistent with and undermine the effectiveness of each other. Order

[35] See, e.g., NRG Power Marketing, Inc. v. New York Independent System Operator, Inc., 91 FERC ¶ 61,346 (2000); Niagara Mohawk Energy Marketing, Inc. v. New York Independent System Operator, Inc., 92 FERC ¶ 61,060 (2000); New York State Electric & Gas Corporation v. New York Independent System Operator, Inc., 92 FERC ¶ 61,073 (2000).

[36] Order No. 2000 at 31,127.

No. 2000 allows the RTOs the flexibility to propose congestion schemes that are best suited to each RTO's circumstances.[37] We agree with Enron that the NYISO proposal for congestion management is inward-focused, and does not address the need for more interregional coordination in the solution to congestion management. The NYISO study to facilitate this effort is a laudable first step. Varying congestion management systems within a natural regional energy market such as the greater Northeast can operate as a barrier to entry to new market participants. This is why it is critical for the market participants in the greater Northeast to reach agreement on market rules.

Regarding Dynergy's and Williams' comments, we agree that highly structured markets are slow to evolve and that any congestion management proposal must be market-based. We have granted RTOs the flexibility to experiment with different market approaches, but as noted above, we will not prescribe any one method at this time.

We recognize that the NYISO market model is not yet perfected and may distort price signals. These issues, however important, are currently being resolved in other arenas and are not within the scope of this filing.

RTO Function No. 3: Parallel Path Flow: The RTO must develop and implement procedures to address parallel path flow issues within its region and with other regions. The RTO must satisfy this requirement with respect to coordination with other regions no later than three years after it commences initial operation

1. NYISO's Proposal

NYISO states that NYISO's large, single control area, with free-flowing ties between transmission owners' systems, internalizes parallel path flows associated with transactions between companies inside its control area. Order No. 2000 allows up to three years to address interregional parallel path flow problems and NYISO points to its substantial progress in this area as a participant in the Lake Erie Emergency Re-dispatch Agreement (LEER).[38] The LEER Agreement provides for intra-control area and inter-control area redispatch, reconfiguration of the transmission system and/or phase angle regulators as necessary throughout the Lake Erie Region to prevent a LEER member from having to shed load during emergency situations. NYISO also points to the Northeastern ISO MOU, in which it is also an active participant, as an example of its effort to develop a common congestion management system that would better enable

[37] Order No. 2000 at 31,126.

[38] See Northeast Power Coordinating Council, 92 FERC ¶ 61,209 (2000).

participants to address interregional parallel path flows. NYISO states that its efforts to develop common regional markets with neighboring RTOs will enhance the efficient treatment of parallel path flows. Additionally, NYISO states that it is evaluating interregional transfer capability studies developed jointly by Mid-Atlantic Area Council (MAAC), East Central Area Reliability Council (ECAR), and NPCC, and will cooperate in NERC's efforts to develop the information to address parallel path flows on an interconnection-wide basis. Lastly, NYISO points to its experience with managing parallel path flows experienced by one party as a result of external purchases of the other party with PJM since 1985.

2. Intervenors' Comments

Williams disagrees that NYISO has addressed parallel path flows in its proposal and contends that the interregional parallel path flows problems are best addressed by a single Northeast RTO. EPSA states that Order No. 2000 requires a larger scope than NYISO proposes and thus that the solution to parallel path flow internalization cannot be achieved by the NYISO RTO. Enron says that scope is the key to the parallel path flow issue, arguing that NYISO is too small to internalize parallel path flows.

3. NYISO's Answer

NYISO rejects intervenors' concerns, noting that Order No. 2000 does not require the RTO to preform this function until December of 2004. NYISO states that it is pledged to comply with this requirement by that date.

4. Discussion

We find that NYISO addresses the issue of parallel path flows internal to its control area. However, NYISO has not addressed how parallel path flows would be internalized within the Northeast and neighboring regions, and therefore has not satisfied this Function's requirements. Order No. 2000 requires that RTOs have implemented measures to address parallel path flows between RTOs within three years.[39] With the requirement for additional scope, NYISO may better internalize the existing parallel path flows and will have the allotted time to address interregional parallel path flows. Nevertheless, we expect parallel path flow issues to be addressed in the settlement discussion before the mediator relating to the formation of a single RTO in the Northeast, and to be addressed in the mediator's report.

[39] Order No. 2000 at 31,130.

RTO Function No. 4: Ancillary Services: The RTO must serve as a provider of last resort of all ancillary services required by Order No. 888 and subsequent orders

1. NYISO's Proposal

NYISO asserts that although it does not own any generation facilities, it serves as the provider of last resort of ancillary services because it administers bid-based ancillary services markets for operating reserves and regulation and allocates cost-based voltage support (and reactive supply) charges and payments. NYISO maintains also that its transmission customers have access to a real-time balancing market operated by NYISO and, citing various provisions of its OATT and Services Tariff, that it has the authority to decide the minimum required amounts of ancillary services and the locations at which services must be provided. Noting that it operates a larger number of competitive ancillary services markets than any ISO, NYISO states that it encourages the development of competitive ancillary services markets to the extent feasible.

NYISO states that it is in compliance with the requirement that it allow market participants to arrange for self-supply or third party supply because its tariffs allow them to self-supply regulation and frequency response service and operating reserves. However, NYISO admits that in our November 8, 2000 order convening a technical conference,[40] the Commission held that NYISO was not in compliance with the Commission's requirements and NYISO's own tariff provisions requiring that customers be permitted to make physical self-supply arrangements for operating reserves. NYISO states that it does not currently have the technical capability to allow such self-supply arrangements, but that it is willing to work with market participants to create the requisite mechanisms or to try to develop acceptable enhanced financial alternatives. NYISO intends to resolve this self-supply issue as soon as possible.

2. Intervenors' Comments

Enron maintains that RTO customers must have the right to self-supply ancillary services backstopped by the RTO. NYSEG asserts that as an intermediate objective, ancillary services, including reserves, should be shared with the other Northeast ISOs to the maximum extent feasible, and that ultimately ancillary services should be consolidated across the Northeast ISOs. Dynegy states as a general principle that to the extent the New York RTO requires redispatch VAR[41] support, and other ancillary services, generator provision of such services must be voluntary, the generator must be compensated for providing such services, and such generator compensation must include opportunity costs.

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[40] New York Independent System Operator, Inc., 93 FERC ¶ 61,142 (2000).

[41] VAR is an acronym for Volt-Ampere, Reactive.

3. Discussion

Order No. 2000 also specifies that all market participants must have the option of self-supplying or acquiring ancillary services from third parties, that the RTO must ensure that its customers have access to a real-time balancing market, and that the RTO must have the authority to decide the minimum required amounts and locations of each ancillary service and must promote the development of competitive markets for ancillary services whenever feasible.[42]

With the exception of the self-supply issue, the Commission finds that NYISO is in compliance with the Order No. 2000 requirements concerning ancillary services. The Commission recognizes that NYISO offers a wide variety of ancillary services and that the markets for such services generally have functioned well. However, NYISO's failure to effectively offer its customers physical self-supply arrangements for operating reserves remains a serious problem. While NYISO has a full schedule of market enhancements that it needs to work on to ensure reliable and economic service this summer, it should allocate sufficient resources to address the self-supply issue as soon as possible consistent with that schedule. With regard to NYSEG's suggestion that as an intermediate term objective, NYISO maximize the sharing of all ancillary services with other Northeast ISOs, including reserves, to the extent technically feasible, the Commission notes the March 13, 2001 joint NYISO - ISO New England press release announcing their agreement to a reserve sharing procedure during short-term periods of generation or transmission line loss. The Commission expects that similar coordination will expand to the extent technically feasible as NYISO works toward a single, fully-integrated RTO in the Northeast.

RTO Function No. 5: OASIS, Total Transmission Capability (TTC) and ATC: The RTO must be the single OASIS site administrator for all transmission facilities under its control and independently calculate TTC and ATC.

1. NYISO's Proposal

NYISO states that it already fully complies with this requirement. It states that it provides the single OASIS site for facilities under its control and that where individual transmission owners in the NYCA are required to provide utility specific information such as organization charts, personnel changes, codes of conduct, etc., on their individual OASIS sites, links to these sites are posted on NYISO's web site. NYISO states that its LBMP system and congestion pricing model are fundamentally different from the traditional physical reservation-based model that the Commission had in mind when we adopted our pro forma OASIS standards. It states that the Commission has

[42] Order No. 2000 at 31,141.

previously granted the NYISO waivers from certain OASIS requirements.[43] It does not believe that these waivers, which are necessitated by the NYISO's Commission-approved market design, should affect its compliance with Order No. 2000's OASIS requirement. NYISO independently computes ATC and TTC values at Level 3 using a methodology specified in its OATT,[44] and that it is currently working on enhancing its ability to post ATC and TTC. In response to Order 2000's requirement that RTOs must coordinate ATC values with neighboring regions and develop procedures to validate its own ATC values,[45] NYISO states that it computes transfer capability through the performance of its Security Constrained Unit Commitment (SCUC)[46] and BME. It states that because these programs consider transmission constraints and desired net interchange, NYISO is already largely coordinated with neighboring control areas, and that it will continue to work with its neighbors to more closely coordinate interregional OASIS operations.

2. Intervenors' Comments

Williams believes that the NYISO's RTO proposal is acceptable. It states that it especially likes the NYISO's practice of independently calculating ATC & TTC values. Further, Williams states that the NYISO's efforts to coordinate interregional OASIS operations have merit, but that such

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[43] In Central Hudson Gas & Electric Corp., et al., 88 FERC ¶ 61,253 (1999), the Commission granted NYISO waiver of the OASIS requirements of subsections 37.6 (c)(1), 37.6 (c)(3), 37.6 (c)(4), 37.6 (c)(5), 37.6 (d)(1), 37.6 (d)(3), 37.6 (d)(5), and 37.6 (e)(1). Additionally, in New York Independent System Operator, Inc., 94 FERC ¶ 61,215 (2001), the Commission granted NYISO waiver of certain provisions of Version 1.4 of the Commission's Standards and Communications Protocols Document and sections 4 and 5 of the Commission's Uniform Business Practice Standards.

[44] NYISO calculates ATC according to Attachment C of its OATT. Attachment C provides that NYISO calculations of ATC will be performed by NYISO through its Security Constrained Unit Commitment, Security Constrained Dispatch, and BME computer algorithms. These scheduling algorithms consider, among other things, load forecasts, market-based bids for ancillary services, bilateral transactions, and energy sales, in determining ATC.

[45] Order No. 2000 at 31,145.

[46] SCUC is a computer algorithm that simultaneously minimizes the bid production cost of: (1) supplying power to satisfy all accepted purchaser's bids to buy energy from the day ahead market; (2) providing sufficient ancillary services to support energy purchased from the day-ahead market; (3) committing sufficient capacity to meet the ISO's load forecast and provide associated ancillary services; and (4) meeting all transmission schedules submitted day-ahead.

interregional OASIS coordination efforts could easily be avoided with the establishment of a single Northeast RTO.

Calpine claims that NYISO does not meet Order 2000's requirements with regard to Function No. 5. It notes that under NYISO's LBMP system, no reservation of transmission capacity is required and ATC is used only as an instantaneous indication of the existence of uncongested transmission paths, not to determine whether additional requests for transmission service can be satisfied. Calpine states that instead of ATC, market participants seek access to more real-time flow of information in a clear and useful format. Calpine argues that such access will foster better understanding of market conditions to determine whether inter-control area transactions are feasible.

Calpine states that the NYISO's assertion that it is working on its ability to post ATC and TTC is unacceptable. Calpine argues that the Commission should set firm milestones by which the NYISO will post ATC and TTC to conform to 18 C.F.R. § 37.6 (2000), as the Commission has required, and facilitate a transmission system with a high level of transparency and freedom from unnecessarily encumbering ambiguities. Calpine states that these milestones should also require the NYISO to address issues related to ramping scheduling and examination of interchange transactions.

3. NYISO's Response

NYISO responds that Calpine has misleadingly minimized both NYISO's efforts to improve its information disclosure practices and the distinctive features of NYISO's market model that have led the Commission to grant the NYISO a temporary waiver of certain OASIS requirements. NYISO also reiterates that it has included the need for the Northeastern ISOs to adopt a common method of performing ATC and TTC calculations in its "Best Practices" proposal.

4. Discussion

We find that NYISO's RTO proposal satisfies our requirements with regard to the OASIS, ATC, and TTC function. NYISO administers the single OASIS site for the transmission facilities under its control and calculates ATC and TTC at Level 3. Calpine takes issue with the way in which ATC and TTC information is calculated and posted by NYISO. Nonetheless, NYISO's calculation and posting of ATC and TTC is consistent with the waivers we have previously granted it. We reaffirm, however, that the waivers were for Phase IA requirements on an interim basis, and not for any of the communications protocols and standards for business practices which we may adopt in Phase II of the OASIS implementation. We expect that intervenors' other concerns will be addressed within the process of establishing a single RTO in the Northeast and that compliance with respect to this Function will be improved by that RTO's larger scope.

RTO Function No. 6: Market Monitoring: To ensure that the RTO provides reliable, efficient and not unduly discriminatory transmission service, the RTO must provide for objective

monitoring of markets it operates or administers to identify market design flaws, market power abuses and opportunities for efficiency improvements, and propose appropriate actions

1. NYISO's Proposal

NYISO argues that its Commission-approved Market Monitoring Plan (MMP)[47] satisfies this requirement. NYISO states that MMP provides for a market monitoring unit (MMU) that monitors the competitive performance of the markets for evidence of potentially abusive behavior and for an outside consultant who functions as an Independent Market Advisor (IMA). Pursuant to the MMP, NYISO is authorized to take prospective corrective action upon detection of abusive conduct.

The MMP also empowers NYISO to monitor markets that it does not administer. In particular, NYISO monitors schedules submitted to it for bilateral or other transactions, as well as conditions and events outside of the NYCA affecting New York energy markets.

Also, NYISO state that its MMP commits it to file annual reports on the competitive structure and performance of New York energy markets. Pursuant to the MMP, NYISO's MMU and IMA are also required to submit reports upon request.

2. Intervenors' Comments

Aquila contends that NYISO's proposed MMP does not meet the Order 2000 requirement, because it does not subject the ISO staff and NYISO's transmission planning and expansion activities to the review of an outside, independent monitor. Accordingly, Aquila urges the Commission to require that an independent market monitoring unit be established to monitor NYISO's activities and to assess the competitive effects of any transmission plan. Aquila states that an independent monitor will also perform interregional market monitoring functions. In Aquila's opinion, the Joint Markets Committee (JMC) formed pursuant to the agreement between the NYISO and NE-ISO Boards to coordinate monitoring efforts of the two ISOs is not sufficient.

Morgan Stanley and NRG also support the establishment of a regional independent market monitor that will assess the markets in the entire Northeast region. Sithe also proposes to establish an independent market monitoring unit that could be integrated with neighboring regions to promote the development of large seamless markets. Sithe reasons that for a market monitor to identify and resolve market flaws objectively and efficiently, it must monitor broad regional markets. Enron suggests that the MMU functions should be transferred to a larger organization comprising three ISOs in the Northeast region.

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[47] See New York Independent System Operator, Inc., et al., 89 FERC ¶ 61,196 (1999) and New York Independent System Operator, Inc., et al., 90 FERC ¶ 61,317 (2000).

Member Systems, on the other hand, oppose as premature the establishment of a regional independent monitoring unit. They believe that this issue should be addressed later as part of the resolution of seams issues.

Calpine and EPSA argue that the MMU should not be used as a substitute for a properly structured RTO and must be independent of the entities deciding market policy, as well as those implementing recommended market improvements. Morgan Stanley and NRG are also concerned about the degree of independence of the MMU under NYISO's MMP. Sithe asserts that although the NYISO-proposed MMP is beneficial in a number of aspects, it fails to provide for an independent market monitoring unit governed by its own independent board of directors. Also, Enron states that NYISO's MMU lacks independence from NYISO and thus cannot be expected to assess objectively activities of the latter.

In their reply comments, Member Systems urge the Commission to reject the requests for an independent market monitoring unit. They argue that because, an RTO is, by its nature, independent, there is no need to ensure its independence by separating its market monitoring function from other market administering functions.

EPSA and Calpine contend that NYISO's MMP should be modified to limit the MMU's authority to observing and investigating the market and making recommendations to NYISO. They express concern about the MMU's ability to unilaterally impose market rules changes and to adjust market clearing price after the fact. Calpine asserts that MMU's artificial interference with market signals that prices send to suppliers and users will cause reliability problems. Williams is also concerned with the MMU's authority to review and change bid prices in an attempt to address an alleged anti-competitive behavior. Williams argues that such remedial action should be vested with this Commission or the Department of Justice. Also, Morgan Stanley, like Calpine and EPSA, proposes to limit the MMU's authority to the market examination and reporting function and to leave the market mitigation function and market rules changes within the purview of the RTO.

Member Systems, on the other hand, argue that requests to remove MMU's remedial authority should be rejected. They state that NYISO's Commission-approved MMP provides for specific objective mitigation criteria that have been made public, which satisfies the Order 2000 requirement. They also state that there is no allegation that NYISO has misused or abused its mitigation authority.

The New York Commission also opposes a limited role for the MMU. It believes that the MMU must have mitigation authority, at least during the transition period, when the need for mitigation remains due to market design and software flaws.

Additionally, Williams and EPSA request that the Commission adopt a standard definition of "market power." Specifically, EPSA proposes a test for assessing market power to be employed by the Commission.

3. NYISO's Answer

NYISO contends that the Commission should not limit MMU's mitigation authority, which is based on objective, pre-approved standards. NYISO believes that its market mitigation authority is essential to the competitiveness of the NYISO- administered markets that are highly concentrated and vulnerable to the exercise of market power.

NYISO opposes the proposal to establish a regional market monitoring unit that will be independent from participating ISOs and will have no mitigation authority. It notes that ISOs are already independent from their market participants and thus there is no reason for a market monitoring unit to be independent from ISOs. NYISO asserts that separating market monitoring from ISO staff will substantially undermine its effectiveness. NYISO further explains that an effective market monitor must have close ties to an ISO's operational staff and full access to ISO market information in order to fully understand ISO practices and procedures.

Also, NYISO states that creating a regional independent market monitoring unit will divert resources from other more important efforts to enhance the Northeastern market. In NYISO's opinion, such diversion will be totally unjustified given the lack of benefits from a proposed monitoring unit. NYISO notes that the Joint Markets Committee established under the recent agreements between the NYISO and ISO-NE Boards will already coordinate the two ISOs' market monitoring efforts.

4. Discussion

Order No. 2000 requires that the RTO proposal contain a market monitoring plan designed to identify market design flaws, market power abuses and opportunities for efficiency improvement, and to propose appropriate actions. In particular, market monitoring must include: (1) evaluating the behavior of market participants in the RTO-administered markets, including transmission owners, to identify adverse effects of their conduct on the RTO's ability to provide reliable, efficient, and nondiscriminatory service; (2) periodically assessing whether behavior in markets in the RTO's region that are operated by others affects the RTO operations; and (3) filing with the Commission and other affected regulatory bodies reports on market design flaws, market power abuses in the RTO-operated markets, and on opportunities for enhancement of the market efficiency.[48]

We find that NYISO's proposal complies with these requirements. NYISO's MMU monitors for market power abuses and market design flaws, and is authorized to take corrective actions. NYISO's MMU also surveys markets operated by others, such as bilateral and other transactions and transactions taking place outside the NYCA that affect New York energy markets. Finally, the MMP requires NYISO to file with the Commission annual reports on the competitive conditions and

[48] Order No. 2000 at 31,156.

economic efficiency of New York energy markets. Under the MMP, the MMU and IMA also have an obligation to submit other reports required by various regulatory agencies.

Certain intervenors argue that NYISO's MMP does not comply with the Order No. 2000 requirements because it fails to provide for a market monitoring unit that will be completely independent of the RTO. Order No. 2000 permits, but does not require, the market monitor to be outside of the RTO.[49] NYISO's MMU and IMA, which report directly to NYISO's Chief Executive Officer satisfy the criteria of Order No. 2000. The Commission has the statutory responsibility to ensure that public utilities selling in competitive bulk power markets do not engage in market power abuse and also to ensure that markets within the Commission's jurisdiction are free of design flaws and market power abuse. To that end, the Commission will expect to receive the reports and analyses of an RTO's market monitor at the same time they are submitted to the RTO.[50] The Commission intends to work with the market monitor to ensure that markets are functional and free of abuse or design flaws.

Some commenters propose to eliminate the MMU's authority to mitigate market power abuses. Order No. 2000 permits market mitigation plans to impose sanctions and penalties for certain types of behavior, as long as the plans clearly identify such remedial actions and the specific conduct to which they would be applied, provide the rationale for imposition of sanctions and penalties, and explain how they would be implemented.[51] We find that in this respect, NYISO's MMP complies with Order 2000. The MMP identifies the conduct warranting mitigation, describes mitigation measures and sets forth the criteria for their application.

In response to the intervenors' request to establish a regional market monitor, we will not prescribe specific parameters for market monitoring at this time in light of our finding with regard to the scope and regional configuration of this proposal.

We reject the requests that the Commission adopt a standard definition of "market power." Such requests are beyond the scope of this proceeding.

In the future, the Commission will re-assess the need for and the degree of market monitoring , and we reserve our authority to issue a supplemental order regarding market monitoring.[52]

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[49] Order No. 2000 at 31,155.

[50] California Independent System Operator Corporation, 86 FERC ¶ 61,059 (1999).

[51] Order No. 2000 at 31,156.

[52] Order No. 2000 at 31,157.

RTO Function No. 7: Planning and Expansion: The RTO must be responsible for planning and for directing or arranging necessary transmission expansions, additions and upgrades that will enable it to provide efficient, reliable and non-discriminatory transmission service and coordinate such efforts with the appropriate state authorities. If the RTO is unable to satisfy this requirement when it commences operations, it must file with the Commission a plan with specified milestones that will ensure that it meets this requirement no later than three years after initial operation

1. NYISO's Proposal

NYISO states that it is proposing certain revisions to its tariffs and enabling agreements that will establish a comprehensive program for the coordination of transmission planning and expansion activities, thereby ensuring compliance with Order 2000. It states that it proposes to create a new Transmission Planning Committee (TPC) as a permanent joint subcommittee of both the Business Issues Committee (BIC) and the Operating Committee (OC) with responsibility for considering and coordinating all transmission expansion proposals in the NYCA and for developing a Consolidated Transmission Plan (CTP) that will include transmission facilities necessary to ensure the continued reliability of the New York transmission system.[53]

The TPC's responsibilities will include, among others: (a) development of a CTP that will specify transmission facilities needed to maintain minimum system reliability after considering and including existing facilities, planned system expansions, proposed generation interconnections, demand-side response mechanisms and other alternatives, where appropriate; (b) the assessment of generation and transmission expansion activities; (c) working closely with neighboring RTOs and state regulatory agencies; (d) facilitating the development of rules, procedures and cost allocation methodologies for transmission expansions and generator interconnections; (e) the development of a review process for reliability-based transmission projects; (f) all transmission planning-related functions: (g) determination of whether economic-based transmission projects can be integrated reliably into the CTP; (h) consideration of appropriate incentives for the construction of reliability-based transmission facilities identified in the CTP; (i) oversight of the development of, and approval responsibility for, reliability-related analyses and reports; and (j) development of any market-based mechanisms to foster

[53] The TPC will have the same membership rules and voting structure as the BIC and OC. The TPC will generally report to both the BIC and OC. The TPC will submit a draft CTP, including any reliability projects, and associated cost allocations, to the BIC and OC and to NYISO staff for review and comment. After any revisions to the CTP, the TPC will submit the CTP to the BIC and OC for action and then to the Management Committee. Ultimately, the CTP will be submitted to the NYISO Board for final action.

economic-based transmission expansion projects. The NYISO staff, in cooperation with the TPC, will perform the required planning studies and analyses.

The transmission owners will construct reliability projects included in the board-approved CTP, subject to: (a) the transmission owner being assured by the appropriate regulatory authorities full recovery of its reasonably incurred costs, which include adequate returns on investment and appropriate amortization periods; (b) the approval of cost recovery mechanisms for a transmission owner constructing a transmission project and for a non-constructing transmission owner allocated project costs; (c) the receipt of all federal, state and local approvals; (d) the securing of any necessary real property rights; (e) the receipt of board of trustees or directors' approvals, as applicable; and (f) the receipt of adequate financing.

2. Intervenors' Comments

Calpine argues that NYISO's proposal limits the consideration of transmission upgrades or expansions, and its consolidated transmission plan does not cover local transmission facilities. Calpine states that the best way to satisfy Order No. 2000's requirements for the prevention of discrimination and operational efficiency is to have a standard interconnection agreement governing transmission upgrades in the NYISO area.

Calpine and EPSA take issue with NYISO's proposal that transmission plans be updated every two years, rather than twice a year. They recommend that NYISO consider adopting the rules that PJM uses to manage transmission upgrades and expansion on a regional basis. EPSA calls the two year updates unacceptable, noting that the growth in demand today is not only higher in the aggregate, but is also subject to regional shifts.

EPSA contends that NYISO does not possess exclusive authority over interconnecting new generators, planning and expansion requirements. It notes that the CTP will not be developed by NYISO staff, but by the new stakeholder committee. EPSA argues that since the only parties to the TPC with the information and technical expertise to establish a transmission plan are the transmission owners, it can be expected that the CTP will in fact be prepared by the transmission owners. Furthermore, EPSA argues that the limited authority of the NYISO Board is exemplified by the proposal itself. EPSA notes that if the NYISO Board determines that modifications to the CTP are necessary, the Board is limited to remanding the CTP to the Management Committee, with an explanation of the Board's reasons for the proposed modifications. EPSA argues that the Board, in other words, can only "propose" modifications to the CTP.

EPSA contends that the CTP will only address transmission projects required to meet reliability requirements, which cannot be expected to be met by new supply resources -- thus, transmission upgrades or expansions that would be required: (1) only if new generation supply projects were not built or (2) to serve new generation supply, will not be included in the CTP. EPSA claims that it is not clear what transmission facilities will even be considered by the TPC in its CTP because they will only

relate to the "bulk power" system, an undefined and potentially limited category of transmission facilities.

EPSA states that the transmission owners appear to want the TPC to approve "incentives" for the construction of reliability-based transmission facilities. EPSA argues that it is inappropriate for the TPC to consider such incentives in connection with the construction of reliability-related upgrades and expansions because considering incentives poses a serious conflict of interest for this stakeholder group. EPSA raises concerns about the TPC's requirements, such as "appropriate amortization periods," the receipt of the transmission owners' board's approval and the receipt of adequate financing prior to construction. EPSA believes that these requirements are likely to present barriers to construction of transmission upgrades and expansions.

Williams requests that the Commission require NYISO to develop a fully compliant transmission and expansion proposal, and grant approval only after an opportunity for full review by interested parties.

AF&PA takes issue with two aspects of the CTP: (1) a transmission owner's obligation to construct such facilities will be subject to the owner being assured by the appropriate regulatory authorities full recovery of its reasonably incurred costs; and (2) reasonably incurred costs will include the recovery costs with a rate of return and amortization period that reflect the risk inherent in the construction of transmission projects in a restructured electric industry. AF&PA protests these provisions as an attempt by the NYISO to establish, on a generic basis, a standard for rates of return and amortization periods applicable to the collection of costs incurred in building new transmission facilities. AF&PA claims that such a risk might justify a particular return rate or amortization period, the transmission owner should be required to make a showing of such risks as related to a particular project before being permitted to reflect that risk in enhanced rates of return or amortization periods.

Morgan Stanley opposes NYISO's proposed two-tiered approach to transmission expansion, thereby "economic" expansion and "reliability-related" expansion are addressed under separate methodologies. Morgan Stanley claims that NYISO's proposal establishes a double standard for transmission expansion, separating reliability and economic projects. Morgan Stanley states that the separation of reliability projects is an unfair way of allocating the costs of projects to market participants that do not benefit from the proposed expansions. Morgan Stanley argues that certain market players will be in a position to receive appropriate benefits that are not easily quantifiable, while distributing the associated costs to all other market participants. Morgan Stanley insists that market forces should determine when transmission expansion is required.

Transenergie supports NYISO's proposal, with several qualifications. It states that the proposal's merits include that the process will provide a forum for market participants representing all segments of the New York State electric market and the NYISO to play a role in the development of the CTP. Transenergie also agrees that the CTP should consist only of reliability projects. It claims

that the situations in which the market does not provide sufficient transmission should be limited to those cases in which transmission is needed for reliability purposes.

Transenergie notes that the proposal does not expressly address the Commission's requirement to develop market-based mechanisms to foster economic-based transmission expansion projects. Transenergie also states that the proposal should be conditioned so that such market-based mechanisms are consistent with the New York market design and do not favor any such specific transmission technology, congestion relief approach, including new generation or load management, or transmission provider. Transenergie argues that NYISO's RTO proposal suffers from one major limitation, i.e., it does not ensure that the most cost-effective solution to a reliability need -- whether that solution is generation, transmission built by traditional or non-traditional transmission companies, or load management programs -- is selected. Transenergie indicates that this limitation arises because according to the proposal, only incumbent transmission owners can construct reliability projects, and by implication, reliability projects are limited to only transmission projects which meet a reliability need that is identified in the CTP, but is not being met by the market. Transenergie suggests that this limitation might be remedied if the proposal were modified to allow for a competitive solicitation process.

Orion contends that NYISO should serve as a safety net for those times when the market fails to protect reliability, not as a central planning committee. It argues that NYISO should clarify what constitutes a "reliability-based transmission project" and modify its procedures to minimize its involvement in transmission expansion to those times when it is absolutely necessary to ensure reliability.

HQUS raises several concerns with the transmission expansion proposal. HQUS submits that the efforts to create the CTP should not divert attention from discrete projects for which there already is a demonstrated and urgent need, such as increasing transfer capability across Central East interface. HQUS also states that it is important that transmission expansion and planning be coordinated interregionally; since many of the transmission issues, such as the Central East constraint, have an impact outside, as well as inside that region. Finally, HQUS submits that NYISO should use its position as operator of the New York transmission system to foster the maximum use of interconnections, for example, by adopting flexible limits on transfer capability, thereby allowing for temporary relief from transfer limit restrictions until the implementation of a permanent solution.

Multiple Intervenors states that the transmission owner cost recovery provisions of the NYISO's RTO compliance filing should be rejected because the filing fails to include any justification as required by Order 2000. Multiple Intervenors point out that the Commission has found that an applicant must support any innovative rate proposal as just, reasonable, and not unduly discriminatory or preferential. It claims that the NYISO proposal conditions the transmission owners' commitment upon Commission approval of innovative transmission rate treatments, but fails to include any

demonstration of how those rates would help achieve the goals of RTOs, thereby failing to meet the requirements for the approval of innovative transmission rates.

EPRI does not directly address NYISO's transmission expansion proposal, but sets forth broader recommendations with regard to RTOs in general. EPRI urges the Commission to encourage RTOs to join EPRI and fund EPRI's Power Delivery Research and Development programs, including the relevant research targets and the reliability and digital society infrastructure initiatives it describes. For those RTOs that do join EPRI and fund such targets and initiatives, EPRI recommends that the Commission allow them recoup the associated costs in their transmission rates.

The New York Commission requests that the Commission should reject the provision that the New York Commission must pre-approve the costs of any transmission construction ahead of time. The New York Commission states that although it does approve major transmission line construction, it objects to the concept of a pre-approval process, which would undermine utility regulation in New York.

3. Responsive Pleadings and NYISO's Answer

The New York Commission argues that maintaining reliability must be the paramount goal of transmission planning. The New York Commission states that reliable operation of the transmission system is critically important to the economic well-being of New York and that the interests of market participants, primarily economic, may not always reflect the interests of the general public. Accordingly, the New York Commission states that the Commission should not adopt any proposal that would assign transmission expansion planning solely to the market and the NYISO committees.

In response to intervenors' arguments that there is a lack of market-driven incentives to invest in additional transmission facilities, Member Systems state that finding a mechanism to enable market-based transmission expansion has been explicitly included in the NYISO proposal as a task of the TPC. It states that the NYISO proposal also provides that any party may propose to build economic-based transmission facilities, and that the TPC is authorized to develop and recommend appropriate market-based mechanisms that foster economic-based transmission projects.

Member Systems also respond to intervenors' arguments that there should be no generic standard for rates of return and amortization periods applicable to the costs associated with building new transmission facilities. They state that the proposal does not provide for Commission approval in advance of any specific rate treatment. Member Systems claim that the filing only seeks assurance that new transmission facilities constructed for the purpose of assuring regional reliability will receive rate of return and amortization treatment appropriate in the restructured electricity market, which is consistent with the Commission's policy expressed in Order No. 2000.

NYISO states that because most of the challenges to the proposal involve rate issues or questions about legal responsibilities of the Member Systems, it defers to the Member Systems' answer on those matters.

4. Discussion

An RTO must have ultimate responsibility for both transmission planning and expansion within its region that will enable it to provide efficient, reliable and non-discriminatory service and coordinate such efforts with the appropriate state authorities. Specifically, we stated that an RTO must satisfy the requirements to: (1) encourage market-motivated operating and investment actions for preventing and relieving congestion; (2) accommodate efforts by state regulatory commissions to create multi-state agreements to review new transmission facilities, coordinated with programs of existing Regional Transmission Groups where necessary; and (3) file a plan with the Commission with specified milestones that will ensure that it meets the overall planning and expansion requirement no later than three years after initial operation, if the RTO is unable to satisfy this requirement when it commences operation.[54] In addition, we found that independent governance of the RTO is necessary for nondiscriminatory and efficient planning and expansion. We noted that while accurate price signals can signal the need for expansion, such expansion may not be achieved if an RTO operates under a faulty governance system (e.g., a governance system that allows market participants to block expansions that will harm their commercial interests).[55]

We note that NYISO has not filed a complete transmission expansion and planning proposal as part of its RTO compliance filing. Rather, it has submitted only the broad outline and principles of a plan based on its existing committee process. A detailed proposal should be consistent with our transmission planning principles, and should consider all market perspectives, identify expansions needed to support competition, and provide for input from all parties and for competitive solicitations for new projects.

As we noted above in an earlier section, we have concerns with the degree of independence that will be held by NYISO's proposed RTO. These concerns are equally applicable here. NYISO's plan will allow market participants to block expansions, as it appears to provide that ultimate decision-making authority to construct transmission expansions or upgrades will rest in the hands of the existing transmission owners. We agree with intervenors that the plan does not explicitly grant the RTO the ability to propose transmission upgrades, but only to review proposals by its committees, which are composed at least in part by transmission owners. We also agree with intervenors that the proposal's cost recovery principles raise concerns. These principles appear to condition transmission expansion upon the satisfaction of transmission owners with, among other things, an agreeable return on

[54] Order No. 2000 at 31,164.

[55] Order No. 2000 at 31,165.

investment. These cost recovery principles seem to give the transmission owner the ultimate decision-making ability to carry out transmission upgrades. In addition, we have concerns with other aspects of NYISO's proposal, including its 2-year interval between plan updates, its lack of a standard interconnection agreement, and its distinction between transmission planning for reliability and transmission planning for 'economic' facilities. Further, the RTO transmission protocols need to take appropriate account of local reliability standards. In sum, we find NYISO's proposal to be too vague, and we find that NYISO has not supported its cost recovery proposal, especially with regard to how it will facilitate transmission expansion. Thus, we cannot approve NYISO transmission and expansion proposal for RTO Function No. 7.

NYISO also has not complied with our requirement that an RTO must file a plan with specified milestones to ensure that it meets the overall requirements of RTO Function No. 7 within 3 years after the RTO's initial operation.

RTO Function No. 8: Interregional Coordination: The RTO must ensure the integration of reliability practices within an interconnection and market interface practices among regions

1. NYISO's Proposal

NYISO states that it actively participates in efforts to more closely integrate the reliability and market interface practices of the three Northeastern ISOs and the IMO. In particular, NYISO takes part in the ISO MOU process, which is a joint collaborating effort of the three Northeastern ISOs and the IMO to address seams issues and to make their markets more compatible.

NYISO also states that NYISO and ISO-NE reached agreement on specific initiatives to jointly address interregional market performance and market seams issues on an expedited basis. According to NYISO, the agreement is yet to be approved by NYISO and NE-ISO Boards. Under the agreement, NYISO and ISO-NE would share information relevant to preventing market power abuses across ISO boundaries. The agreement establishes the JMC comprised of Market Advisers to NYISO and NE-ISO Boards that will work cooperatively to address interregional market monitoring issues.

Furthermore, NYISO states that it, jointly with ISO-NE and the IMO, but not PJM, sponsors a study of the feasibility of creating an integrated Northeastern day-ahead energy market. On January 31, 2001, NYISO submitted a supplemental filing containing the joint feasibility study. According to the feasibility study, a combined day-ahead electricity market for the Northeast has a number of potential benefits. Among those are improved efficiency of energy, reserve and congestion management markets for the region as whole; reduction in ISO software costs and market participants' transaction and hedging costs; and enhanced regional reliability. On the other hand, the study states that there are a number of practical transition issues that need to be taken into account in assessing the feasibility of an integrated day-ahead market and in evaluating alternative structures for implementing

such a market. By NYISO's own account, it is not currently considering the creation of a regional real-time market, because the difficulties associated with such a project are likely to be greater than those involved in establishing a day-ahead market. However, NYISO states that the creation of a Northeastern real-time energy market may be possible in the future.

Also, NYISO states that it is engaged in the NPCC's efforts to integrate reliability and planning practices both within the NPCC area[56] and on a super-regional level, among the NPCC, MAAC and ECAR reliability councils. NYISO explains that its active participation in the NPCC initiatives assures that NYISO's reliability practices and assessment of expansion plans will be consistent with the broader international Northeast region.

Additionally, NYISO has entered into emergency energy transaction agreements with PJM and NE-ISO in order to ensure regional reliability. These agreements set forth the rates, terms, and conditions pursuant to which energy will be sold in emergency situations.

NYISO also proposes to voluntarily file reports with the Commission after it becomes an RTO. The reports will describe the progress of interregional coordination activities under the MOU and will provide timetables for the resolution of various issues.

2. Intervenors' Comments

Aquila and NRG propose to establish a formal well-organized collaborative process to develop an interregional independent market monitoring unit and to establish milestones and a decision-making process to converge New York's and New England's energy markets. They request that the proposed collaboration be undertaken under the auspices of the Commission's dispute resolution service. Industrial Consumers and Dynegy also urge the Commission to convene a collaborative process by establishing a technical conference to address interregional coordination issues.

EPSA argues that NYISO's compliance filing fails to meet the Order No. 2000 regional coordination requirement, because NYISO's proposals do not provide for definite implementation schedules with enforceable deadlines. Accordingly, EPSA requests that the Commission provide NYISO with guidance on the appropriate schedule for accomplishing the integration of the Northeastern market. HQUS urges the Commission to establish firm procedures and deadlines for cooperation. Also, Reliant requests the Commission's active intervention in the process and points out that the MOU has failed, as no results have been achieved and no decisions have been made since the MOU was executed.

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[56] NPCC is comprised of New York, New England, Ontario, Quebec and the Maritime Provinces.

Furthermore, NYSEG and RGE state that the MOU fails to address functional and structural integration of the ISOs; suffers from procedural lapses and a lack of serious priority; and creates the potential for new seams problems by failing to bring PJM into the process. Several Commenters request the Commission Alternative Dispute Resolution (ADR) unit's involvement in the MOU Working Groups meetings and the Commission Staff's oversight of the project implementation process. NYSEG and RGE propose a three-phase process to achieve functional and structural integration among the three Northeastern ISOs. The proposed integration process would comprise: (1) selecting best practices and implementing certain market improvements; (2) consolidating real-time and day-ahead market operations, settlement functions, and transmission scheduling and OASIS management and implementing a consistent congestion management system; (3) consolidating market monitoring units, ancillary services, and Installed Capacity and TCC auctions and improving coordination of planning and transmission expansion-related functions.

NY City argues that the Commission should not approve this RTO until NYISO demonstrates that its interregional coordination efforts create a regional market. Williams, NRG, and Enron find NYISO's proposed interregional coordination plan to be inadequate to satisfy the Order No. 2000 requirements. Williams believes that once a single Northeastern RTO is established, interregional coordination issues will be resolved.

The New York Commission addresses NYISO's proposal to voluntarily file with the Commission biannual status reports on the progress toward interregional coordination. It requests that the Commission require the three Northeastern ISOs to submit a detailed report describing the scope and progress of interregional coordination within 60 days of issuance of this order, regardless of the outcome. The New York Commission further argues that thereafter NYISO should be required to file every 90 days a status report until coordination issues are fully resolved. NYSEG and RGE propose a monthly reporting requirement.

HQUS contends that the emphasis should be given to strengthening the transfer capacity of the interconnections between Quebec and the United States in order to maximize the level of cross-border energy flows. Additionally, HQUS proposes to establish a TPC, the activities of which would be coordinated with the interregional expansion and planning guidelines developed pursuant to the ISO-MOU process.

Aquila, Morgan Stanley, NRG, Sithe, and Enron propose to establish a regional market monitoring unit to advance interregional coordination efforts. Dynegy suggests forming an Interregional Transmission System Coordinator to ensure that interregional coordination is timely, efficient, and beneficial for the entire Northeastern region.

Orion supports NYISO's efforts to develop a single day-ahead market with neighboring ISOs.

Williams requests that the Commission change the criteria applicable to an RTO filing by requiring the development of uniform reliability and market interface practices, instead of simply requiring compatibility of those practices.

3. Discussion

Most intervenors focus their comments on NYISO's interregional coordination efforts with ISO-NE and PJM through the MOU process. We are not satisfied with the parties' progress to date with respect to the MOU process and movement toward a single market for the Northeast. As we stated above, we believe that the scope of the proposed NYISO RTO is too small and the issues facing the Northeast would be better handled through an RTO that encompasses the entire Northeast region and in coordination with Canadian entities, rather than through the MOU process. We expect that intervenors' concerns with respect to many interregional coordination issues will be addressed with the creation of a single fully-integrated RTO in the Northeast.

We also reject Williams' request to require the uniformity of reliability and market interface practices. This request is a collateral attack on Order No. 2000.

V. Open Architecture: Any proposal to participate in an RTO must not contain any provisions that would limit the capability of the RTO to evolve in ways that would improve its efficiency, consistent with the required characteristics and required functions for an RTO

1. NYISO's Proposal

NYISO states that its tariffs and enabling agreements do not contain any such restriction, and that it is therefore in full compliance with the open architecture requirement. It also states that it appreciates its continuing responsibility to monitor NYISO operations and developments in other regions, and to propose structural changes to the NYISO, including possible functional or structural integration with other RTOs, and additional structural alternatives.

2. Intervenors' Comments

No substantive comments were filed regarding NYISO's proposal for this function.

3. Discussion

We find that NYISO's market structure, tariffs and supply of information to market participants meet our Open Architecture requirements.

The Commission orders:

NYISO's filing is hereby rejected as not minimally satisfying the requirements of Order No. 2000, as discussed in the body of this order.

By the Commission. Commissioners Massey and Wood concurred with separate statements attached.

( S E A L ) Commissioner Breathitt dissented in part with a

Appendix

separate statements attached.

David P. Boergers,
Secretary.

**Docket No. RT01-95-000 Interventions**

American Forest and Paper Association (AF&PA)*
Aquila Energy Marketing Corporation (Aquila)*
BP Energy Company (BP Energy)
Calpine Eastern (Calpine)*
City of New York (NY City)*
Connecticut Department of Public Utility Control (DPUC)**
Duke Energy North America, LLC (Duke)
Dynegy Inc.*
Edison Mission Energy, Edison Mission Marketing & Trading, Inc., and
Midwest Generation EME, LLC (collectively, EME)* **
Electric Power Research Institute (EPRI)
Electric Power Supply Association (EPSA)*
El Paso Merchant Energy, L.P. (El Paso Merchant)
Enron Power Marketing, Inc. (Enron)*
H.Q. Energy Services (U.S.), Inc. (HQUS)*
Indeck Companies (Indeck)
Industrial Consumers of New England (Industrial Consumers)
Keyspan-Ravenswood, Inc. (Keyspan-Ravenswood)
Long Island Power Authority and LIPA (collectively, LIPA)**
Mirant Americas Energy Marketing, LP (Mirant)
Morgan Stanley Capital Group Inc. (Morgan Stanley)*
Multiple Intervenors*
New York State Electric & Gas Corporation & Rochester Gas and Electric (NYSEG)* New York State Reliability Council (NYSRC)**
Niagara Mohawk Energy Marketing, Inc. (NMEM)
NRG Power Marketing Inc. (NRG)*
Ontario Independent Electricity Market Operator (IMO)**

Appendix

Orion Power New York GP, Inc. (Orion)*
PG&E National Energy Group, Inc. (PG&E)
PPL EnergyPlus, LLC (PPL)*
Public Service Commission of the State of New York (New York Commission)* Public
Service Enterprise Group (PSEG)
Reliant Energy Power Generation, Inc. (Reliant)*
Shell Energy Services Company, L.L.C. (Shell)*
Sithe Power Marketing, L.P. (Sithe)*

Tractebel Energy Marketing, Inc. and Tractebel Power, Inc. (collectively, Tractebel)
TransEnergie U.S. Ltd. (Transenergie)*
The Williams Companies (Williams)*

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* parties filing protests or comments

** interventions out-of-time

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator Docket No. RT01-95-000

Central Hudson Gas & Electric Corporation
Consolidated Edison Company of New York, Inc.
Niagara Mohawk Power Corporation
New York State Electric & Gas Corporation
Orange & Rockland Utilities, Inc.
Rochester Gas & Electric Corporation

(Issued July 12, 2001)

MASSEY, Commissioner, concurring:

In this order, the Commission expresses its intention to evaluate in the near future the importance of standardizing generation interconnection procedures. I've long advocated such standardization, so this is a big step in the right direction. But I would have been clearer and firmer in expressing our resolve to standardize interconnection procedures. For me, the time to evaluate whether to do so is past. It's time simply to do it.

Interconnection standardization is good for the market. Generators should make location decisions based on economics, not on the basis of a patchwork of idiosyncratic interconnection standards. Establishing uniform standards will be good for generation investment and good for consumers. And standardization would be an efficient use of the Commission's staff resources. It's no secret that the staff is laboring under a crushing work load. Processing a multitude of interconnection filings eats up staff time. Standardization will free staff for other important work.

Therefore, I concur with today's order.

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William L. Massey
Commissioner

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator, Inc. Docket No. RT01-95-000

Central Hudson Gas & Electric Corporation
Consolidated Edison Company of NewYork, Inc.
Niagara Mohawk Power Corporation
New York State Electric & Gas Corporation
Orange & Rockland Utilities, Inc.
Rochester Gas & Electric Corporation

(Issued July 12, 2001)

Breathitt, Commissioner, dissenting, in part:

Since the Commission began promoting RTOs as a means to remove barriers and impediments to wholesale electricity markets, I have been fully committed to the goal of implementing RTOs. However, I am dissenting, in part, to express my objections to specific language in this order and other RTO orders on today's agenda supporting the creation of four RTOs in the country. I agree with the majority's claim that the Commission has been attempting to facilitate the development of large RTOs reflecting natural markets since we issued Order No. 2000. That was our stated goal and one that I have actively pursued. However, today's orders go further by stating that the Commission "favors the development of one RTO for the Northeast, one RTO for the Midwest, one RTO for the Southeast, and one RTO for the West." I do not necessarily favor such development.

When the Commission deliberated over how to attain our mutual objective of RTO formation, we decided to adopt an open collaborative process that relied on voluntary regional participation. The intent was to design RTOs so that they could be tailored to the specific needs of each region. We specifically declined to propose fixed or specific regional boundaries under section 202(a) of the FPA. Instead, we concluded, as a matter of policy, that we would not attempt to draw boundaries, based upon our conviction that transmission owners, market participants, and regulators in a particular region have a better understanding of the dynamics of the transmission system in that region, and that they should propose the appropriate scope and regional configuration of an RTO. We did not specifically endorse one particular scheme of RTO configuration, but opted instead to establish appropriate guidelines to aid in RTO development. In fact, our regulation requires only that an appropriate region is one of sufficient scope and configuration to
permit an RTO to maintain reliability, effectively perform its required functions, and support efficient and non-discriminatory power markets.



Today's order represents a dramatic departure from the approach we pursued in Order No. 2000 to the extent that it directs the formation of four specific RTOs. Just as some commenters to our RTO rulemaking feared, the Magic Markers have come out, and the boundaries are being drawn with little regard to the status and timing of RTO formation efforts in various regions of the country. This was not my intent at the time we issued Order No. 2000; and the events since we issued Order No.

2000 do not compel me to embrace this policy shift. Parties have spent many hours and countless resources in negotiations, collaborations, and complicated business strategy sessions to develop reasonable RTO approaches. The impact of the majority's directive that these four RTOs be formed could be to render these efforts useless and force parties to begin the difficult and time-consuming process anew. For example, the Midwest ISO -Alliance settlement, which the Commission approved and which represented a tremendous effort by many parties, could unravel.

If the majority believes that the Commission should depart from the basic philosophies embodied in Order No. 2000, then I believe it would be only appropriate to initiate a formal notice-and-comment rulemaking proceeding so that we could make a reasoned decision informed by the views of the stakeholders in this process – state commissions, chief among others.

Finally, I do not adopt the majority's assertion that forming larger RTOs will result in lower wholesale electricity prices. This is a laudable goal, and as such, I embrace it. As a general proposition, Order No. 2000 encouraged the development of
large RTOs. However, the promise of lower wholesale electricity prices is one that I, as a federal official, am not willing to make to consumers at this time.

For these reasons, I respectfully dissent.

Linda K. Breathitt
Commissioner

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator, Inc. Docket No. RT01-95-000

Central Hudson Gas & Electric Corporation
Consolidated Edison Company of New York, Inc.
Niagara Mohawk Power Corporation
New York State Electric & Gas Corporation
Orange & Rockland Utilities, Inc.
Rochester Gas & Electric Corporation

(Issued July 12, 2001)

Wood, Commissioner, concurring:

In the discussion under RTO Function No. 8, Williams requested the Commission require the development of uniform reliability and market interface practices. The order dismisses this request as a collateral attack on Order No. 2000. I think this is incorrect. It is clear, especially following the helpful discussions at our recent "seams" conference, that such a project is long overdue, and in fact would buttress Order No. 2000, rather than attack it.

Although the order correctly concludes this item should not be addressed here, it does so on grounds I do not support.

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Pat Wood, III
Commissioner