



## Memorandum

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FROM: Glenn D. Haake, Esq.

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RE: Competitive Entry Exemption to Buyer Side Mitigation

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### 1. Introduction

Pursuant to the NYISO's request at its December 3, 2012 Installed Capacity Working Group (ICAPWG) meeting, the New York Power Authority (NYPA) offers the following comments concerning NYISO's proposal to implement a Competitive Entry Exemption (CEE) to its Buyer Side Mitigation (BSM) rules. At the outset, NYPA applauds the NYISO's effort to improve the efficiency and effectiveness of the process for obtaining relief from the BSM rules as reflected in NYISO's recognition of the need for an exemption for what effectively are purely merchant projects from the BSM bid floor rule. This recognition is consistent with the recommendation contained in the Draft Capacity Market Report that NYISO should "exempt resources not associated with or under contract to an entity possessing buyer-side market power from the application of buyer-side offer price mitigation."<sup>1</sup>

However, NYPA believes that the categorical exclusion of Public Authorities from the list of entities eligible to qualify for the CEE under any circumstances is inappropriate, unduly discriminatory and will impede NYPA from pursuing legitimate competitive projects. Moreover, the reasons cited by NYISO for its position regarding Public Authorities are incorrect and unsupported, as explained below. Finally, even if NYISO revises the CEE to address the concerns set forth herein, it is critical that NYISO promptly establish a waiver process to exempt from application of the BSM bid floor projects undertaken pursuant to legitimate public policy goals.

NYISO should begin immediate discussions in its governance process to address this need. Failure to accommodate within the BSM rules these important projects will impede, if not render impossible, the achievement of important public policy objectives and satisfaction of applicable

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<sup>1</sup> Evaluation of the New York ISO Capacity Market: Summary of Draft Report – Preliminary Draft (Draft Capacity Market Report), prepared by Scott M. Harvey, William W. Hogan and Susan L. Pope, November 7, 2012, p. 65.

reliability requirements, including those associated with proceedings recently initiated by the New York Public Service Commission (PSC)<sup>2</sup> as directed by Governor Cuomo's New York Energy Highway Blueprint (the Blueprint).<sup>3</sup>

## 2. Competitive Entry Exemption

The CEE is intended to enable competitive entrants to pursue projects without the application of the BSM bid floor when they meet certain criteria discussed below. The NYISO explains that this exemption is needed because the current BSM mitigation rules are "formulaic and not dynamic" and impede competitive entrants with a different view of future market conditions from advancing legitimate, competitive projects based on their forecasts when those forecasts differ from the set of assumptions that prescribe the existing BSM waiver tests.

By way of example, NYISO notes that the existing BSM waiver tests "do not reflect potential future retirements when estimating the level at which the Demand Curve will clear."<sup>4</sup> The CEE would be available to any project "that is not receiving support outside of competitive markets, thus allowing such entrants to enter at their own risk and based on their own business outlook."<sup>5</sup> Thus, a project that is shown to NYISO's satisfaction not to be supported by out-of-market subsidies would be entitled to the CEE.

More specifically, the NYISO explains that the CEE "would be granted if the project has no contracts (direct or indirect) with any NY distribution company, Municipal Utility, or any governmental entity including but not limited to Public Authorities. (emphasis added)"<sup>6</sup> In addition, the CEE expressly provides that "Public Authorities cannot get the exemption if they build a unit themselves."<sup>7</sup>

The NYISO should reconsider its unconditional prohibition on allowing a Public Authority to qualify under the CEE. The two main reasons NYISO has cited for its decision to exclude Public Authorities are incorrect and unsupported. First, NYISO argued that NYPA's status as a provider of last resort (POLR) imbues it with an incentive to exercise buyer-side market power. However, NYPA does not have a franchise area within which it is responsible as a POLR.

Second, NYISO has argued that NYPA would have the ability to cross-subsidize an uneconomic unit brought on to depress clearing prices by virtue of its portfolio of other generation resources. Leaving aside the absence of an economic incentive for NYPA to do so, the NYISO position ignores the fact that other entities for which NYISO has deemed the CEE appropriate are in the same position.

For example, NYISO's CEE Proposal would permit a project developer to sign a power purchase agreement with a competitive load serving entity (LSE) such as an energy services company (ESCO) and still qualify for the CEE. A competitive ESCO owned by an entity that

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<sup>2</sup> See Case 12 –T-0502 – Proceeding on Motion to Examine Alternating Current Transmission Upgrades, Order Instituting Proceeding, Issued November 30, 2012 (the AC Upgrades Proceeding) and Case 12-E-0503 – Proceeding on Motion of the Commission to Review Generation Retirement Contingency Plan, Order Instituting Proceeding and Soliciting Indian Point Contingency Plan, issued November 30, 2012 (the Retirement Contingency Plan Proceeding).

<sup>3</sup> See, New York Energy Highway Taskforce, New York Energy Highway Blueprint (2012)

<sup>4</sup> CEE Proposal, p.3

<sup>5</sup> Id.

<sup>6</sup> Id at p.6.

<sup>7</sup> Id.

also owns a generation affiliate could have an incentive to exercise buyer-side market power depending on the supply/load balance of the two affiliates, yet the CEE evidently would be available in such circumstances. In addition, it is commonplace for affiliate projects to be required to obtain a parent company guarantee in order to secure financing. This is effectively an arrangement whereby the profits from other projects owned by the parent company are available to “cross-subsidize” a potentially uneconomic addition.

NYPA is a unique entity that has no incentive to exercise oligopsony or monopsony market power across the New York Control Area or within New York City to depress ICAP clearing prices, which is the perceived threat the BSM rules were designed to address. . Moreover, the vast majority of its incumbent customers are served at contracted rates from dedicated NYPA resources. The portion of its load that is procured in the NYISO-administered wholesale markets is relatively small. In fact, NYPA also owns uncommitted generation which is sold into the NYISO markets and would benefit from higher capacity clearing prices.

In addition, in evaluating whether an entity has an incentive to exercise buyer-side market power, one must evaluate the relevant segment(s) of the market. For example, depending on the geographic boundaries of the new lower Hudson Valley (LHV) zone, it is entirely possible that NYPA will not be deemed a pivotal supplier within the LHV zone. If, following the outcome of the PSC’s Retirement Contingency Plan Proceeding, the PSC determines that a generation resource should be added in the LHV to compensate for the retirement of Indian Point, NYPA should not automatically be foreclosed from obtaining a CEE if it builds or contracts for the construction and operation of a new, competitive resource to fill that need.

Coincidentally, the PJM RTO recently filed with FERC revisions to its version of the BSM bid floor rule (known there as the Minimum Offer Price Rule (MOPR)) and has reinstated an exemption for self-supply under conditions in which the proposed new entrant is neither materially short of supply nor long in generation.<sup>8</sup> PJM’s self-supply exemption (SSE), which is available to investor owned utilities (IOUs), Public Authorities and municipal utilities, among others, garnered support from both the supply and demand side of the market, which is no small feat.<sup>9</sup>

While NYPA does not suggest the SSE can or should simply be imported from PJM into the NYISO markets without modification, the fact that both load and supply parties found this type of exemption appropriate is evidence that an unconditional prohibition on exemptions for IOUs and Public Authorities is not required in order to safeguard the competitive markets against the abuse of buyer-side market power.

Moreover, in supporting the SSE, the December 2012 MOPR Filing (citing a report of the Brattle Group) explains that in the absence of such an exemption the “MOPR rules “will inadvertently interfere with self-supply offers from generating resources that are competitive and do not involve manipulation;” and “will lead to over-mitigation that will undermine bilateral markets and RPM participation by entities, such as public power companies, that meet their customers’ needs primarily through long-term contracts or other self-supply options.””<sup>10</sup> Thus, in addition to being unnecessary to safeguard competitive markets from buyer-side market power abuse, a categorical CEE prohibition against Public Authorities can lead to over-mitigation and other

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<sup>8</sup> See, PJM December 7, 2012 filing in FERC Docket No. ER13-535-000 (the December 2012 MOPR Filing)

<sup>9</sup> See, For Self-Suppliers in ISOs, Capacity Market Mitigation is a Key Topic, and a Moving Target, Electric Utility Week, December 17, 2012, p. 12.

<sup>10</sup> December 2012 MOPR Filing at p.7.

harms to the market. Therefore, NYPA requests that NYISO convene discussions in its stakeholder process to further evaluate this issue and fine tune the proposed CEE exemption.

### 3. Need for a Public Policy Exemption

As mentioned above, the PSC has instituted two proceedings pursuant to the Blueprint to pursue important public policy objectives, including the public policy of ensuring the State's electric system can continue to satisfy applicable reliability requirements in the event of significant, foreseeable retirements. Achievement of these objectives may be thwarted by application of the current BSM rules. As a result, the NYISO must commence discussions to develop a public policy exemption (PPE) to the BSM bid floor rule.

In the AC Upgrades Proceeding, the PSC is seeking transmission upgrades to, inter alia, increase transfer capacity from the western portion of the state to the load centers in the LHV and New York City. The public policy objectives behind this effort include making increased use of existing renewable resources, increasing the capability to develop and deliver incremental renewable resources, improving system reliability, and realizing environmental quality improvements through reduced reliance on older, more polluting resources located in the southeastern non-attainment area. While the BSM rules do not apply directly to transmission upgrades, they do apply to newly created unforced capacity deliverability rights (UDRs), and to the extent a transmission upgrade may be supported by revenues it would receive for creating UDRs into a constrained capacity zone, those UDRs should not automatically be subjected to a BSM bid floor.

The Retirement Contingency Plan Proceeding is aimed at ensuring continued electric system reliability in the face of retirements and contemplates that procuring one or more new generation or supply side resources may, in theory, be appropriate to address the reliability concerns that would be raised by closure of the Indian Point facility, particularly if the Danskammer units in the LHV also are retired. If the PSC determines that maintaining electric system reliability is best served by constructing a new supply resource in the LHV, the BSM bid floor rule could thwart the potential for such a resource to be developed.<sup>11</sup>

Accordingly, NYPA believes it is critical that NYISO commence discussions to develop a PPE. A properly structured PPE could accommodate needed public policy projects in a manner that minimizes adverse impacts to competitive markets; it also could address transmission projects that include UDRs that are found to be needed as part of a Public Policy Requirement (PPR) under FERC Order 1000<sup>12</sup> or to maintain system reliability.

Moreover, although it found inadequate record basis to establish a generic exemption, FERC did express support for the concept of a Public Policy Exemption to the BSM bid floor rule, when it approved NYISO's compliance filing establishing the current paradigm for the BSM bid floor:

the Commission recognizes that the NYPSC may conclude that the procurement of new capacity, even at times when the market-clearing price indicates entry of

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<sup>11</sup> One could argue this suggests the need for another category of exemption related to reliability projects. For the purpose of these comments we will assume that reliability-based projects would fit within the public policy objective of ensuring electric system reliability.

<sup>12</sup> Order 10001000 – *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000 136 FERC ¶ 61,051 (2011).

new capacity is not needed, will further specific legitimate policy goals, such as renewable portfolio standards. We agree that it may be appropriate to exempt such new resources from the price floor proposed by NYISO, but the NYPSC has not provided sufficient specificity to allow us to mandate an appropriately narrow exemption at this time. The NYPSC may make a filing under section 206 of the FPA to justify a mitigation exemption for entry of new capacity that is required by a state-mandated requirement that furthers a specific legitimate state objective. At that time, we will evaluate the merits of the proposed exemption, but at this time, the NYPSC has provided inadequate justification either for a general exemption or for a finding that the appropriate mechanism for supporting its goals is, in fact, an exemption from the price floor for new capacity.<sup>13</sup>

In light of the dictates of the Governor's Blueprint and the advent of Order 1000's PPR policies, NYPA recommends that NYISO develop a mechanism to address public policy projects. NYPA looks forward to working with NYISO and other Market Participants to fashion an appropriate PPE.

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<sup>13</sup> See, Order on Rehearing and Further Order on Compliance Tariff Sheets, Docket Nos. EL07-39-002, ER08-695-000, and ER08-695-001, issued September 30, 2008, paragraphs 37 and 38, pp. 12-13.