

NYISO BOARD OF DIRECTORS
DECISION ON APPEAL
OF
MANAGEMENT COMMITTEE DECISIONS DATED
FEBRUARY 4, 2004 AND MARCH 2, 2004

INTRODUCTION

These are appeals by the Independent Power Producers of New York, Inc. (“IPPNY”)¹ from two Management Committee (“MC”) votes concerning the manner in which Demand Response Providers (“DRPs”) and Distributed Generators (“DGs”) participate in stakeholder governance.² In both appeals, IPPNY argues that stakeholder voting on key issues tends to be split between suppliers and load and that fair stakeholder governance depends on maintaining the existing balance between supplier and load votes. IPPNY also argues that the changes approved by the MC would skew that balance towards load and disadvantage generators. For the reasons set forth below and in the accompanying Appendix A, the NYISO Board of Directors denies both appeals.

DISCUSSION

On February 4, 2004, the MC approved amendments to its bylaws and the *ISO Agreement* to include DRPs and DGs in the Other Suppliers sector of NYISO’s stakeholder governance. On March 2, 2004, the MC declined to create a new subsector in the Public Power and Environment sector for DRPs and DGs. IPPNY appealed both votes. Several parties filed Motions in Opposition; no party filed a Motion in Support. The Board’s Governance Committee consolidated the appeals and held oral argument on April 19, 2004. All parties, including IPPNY, agree that DRPs and DGs should participate and vote in NYISO governance.

The threshold concern raised by these appeals is to ensure that the governing processes of the NYISO support the continued competitiveness of the New York markets, without coming under the domination of any sector, group of sectors or economic interest. In this appeal, IPPNY has expressed the view that the MC proposal will skew the balance of votes in stakeholder governance towards the loads, making shared governance untenable. We are not aware of any substantial evidence that the proposal approved by the MC would negatively interfere with the continued competitiveness of NYISO’s markets or unreasonably reduce any market participant’s opportunity to continue to participate effectively in the NYISO decision-making process. Neither do we believe that the MC proposal would permit any sector or economic interest to have

¹ IPPNY is an organization representing 19 generation owners in New York State.

² Market Participants who have signed the *ISO Agreement* and paid the prescribed membership fee may vote in all three of the NYISO’s principle governance committees. Votes are apportioned by sector to avoid the dominance of any particular groups of Market Participants. MC actions require a 58% approval vote for passage.

dominant voting weight such that coalitions would no longer be necessary to achieve or block MC approval.

That is not to say that evidence of ineffective or biased governance may not appear in the future, whether due to the addition of DRPs or DGs, or for other reasons. The Board will continue to monitor the stakeholder governance structure for indications that it is losing its fairness, effectiveness or ability to support workable competition, and it will closely examine any evidence presented for the appearance of bias or ineffectiveness. This Board responsibility is further discussed in our *2004-2008 Strategic Plan*. The Board has formalized this monitoring process and has instructed staff to report periodically to the Governance Committee and not less than annually to the Board on the effectiveness and fairness of our shared governance structure and to propose changes as necessary. Should it appear to the Board that improvements in the governance structure are needed, the Board will expeditiously present them to the market participants for further action and pursue appropriate filings at FERC, as necessary.

We further note that the Federal Energy Regulatory Commission (“FERC”) has expressed the necessity of assuring that DRPs and DGs, as an important and emerging presence in the markets, are well represented in ISO or RTO governance. We believe that the actions of the MC in this regard are consistent with that policy.

Based on all of the evidence, as further described in Appendix A, which we incorporate by reference, we find both appeals to be without merit. We, therefore, direct NYISO staff and counsel to file amendments to the *ISO Agreement*, as approved by the MC on February 04, 2004, with FERC pursuant to Sections 205 and 206 of the Federal Power Act.³

The two IPPNY appeals are denied.

NYISO Board of Directors
May 18, 2004

³ Pursuant to Article 19 of the *ISO Agreement*, the MC-approved changes to Section 7.04 of the *ISO Agreement* must be filed with FERC pursuant to Section 206 of the Federal Power Act. The other approved changes can be filed pursuant to Section 205.

APPENDIX A
ADDITIONAL ANALYSIS

The Other Suppliers Sector: IPPNY argues, in its February 19 and March 16, 2004 Notices of Appeal, that DRPs and DGs should be included in stakeholder governance but not in the Other Suppliers sector. IPPNY states that DRPs and DGs were neither contemplated nor discussed, even as a concept, during the 1998 - 1999 negotiations that led to the NYISO's formation. Thus, IPPNY believes that these new entrants should be accommodated through the creation of a new subsector, with voting rights contributed equally from all sectors, in order to avoid unfairly skewing the existing balance between load and supply in the MC.⁴

Appellees counter that DRPs and DGs, if not specifically envisioned during NYISO governance negotiations, were contemplated when the broad eligibility criteria for membership in the Other Suppliers sector were drafted. They assert that the Other Suppliers sector was intended to include many disparate economic interests.

It is reasonably clear that the Other Suppliers sector embraces the types of participants at issue here. While the precise services offered by DRPs and DGs may not have been actually contemplated in 1998, appellees are correct in concluding that load reduction was contemplated as a service in the electricity market in 1998. Moreover, the original intent in establishing the Other Suppliers sector is of marginal relevance at best, since the terms that define eligible participants in the Other Suppliers sector are generic and adequately include DRPs and DGs within their scope. The *ISO Agreement*, states that a party is eligible to join the Other Suppliers sector if it is a:

[S]eller, buyer, broker, aggregator, Power Exchange, ESCO or transmitter of capacity or energy in, from or through the New York Control Area. . . .⁵

The term "ESCO" or "Energy Service Company" is defined as:

A Load Serving Entity . . . , a retail load aggregator or a provider of comprehensive energy services, serving customers in New York State.⁶

Since the MC proposal is to amend the *ISO Agreement*, we need not determine whether the DRPs and DGs fit the literal definition of eligible participants in the existing

⁴ IPPNY proposed housing this new subsector in the Public Power and Environment sector but was amenable to creating the new subsector in any agreed-upon sector provided that the newly created voting rights were the result of equal contributions from all sectors.

⁵ *ISO Agreement*, Section 1.96.

⁶ *ISO Agreement*, Section 1.33

Other Suppliers sector, although we note that they probably do. Moreover, we agree with appellees that DRPs and DGs appear to fulfill similar functions in NYISO's markets (*i.e.*, they supply energy or capacity to load, and/or modify the terms or conditions under which energy is supplied) as existing members of that sector. As noted below, we need not decide, for these appeals, whether to form a new subsector for DGs and DRPs as IPPNY has requested.

Load versus Supply: IPPNY argues that Market Participants ("MPs") tend to vote as blocks of either load or supply -- particularly with regard to matters that are likely to affect substantially their economic or voting interests. IPPNY also argues that DRPs and DGs will tend to represent the interests of load since they depend on agreements with such consumers to deliver their products. By adding these new load-favoring entities to an existing sector, IPPNY argues, the MC-approved proposal will tip the existing balance between load and supply to the disadvantage of suppliers. Therefore, the MC approved proposal will: (i) confer an improper advantage upon the load side of the existing block voting; (ii) unfairly skew the balance of interests intended to exist between suppliers and loads when the governance structure was developed; and (iii) render shared governance untenable.

The appellees deny that market participants regularly or predictably vote as load or supply. They point to load's support for significant supplier initiatives, like elimination of the bid cap on 30 minute reserves, the ICAP demand curve and scarcity pricing, as specific evidence that IPPNY's assertion is wrong. Appellees also refute, as baseless, IPPNY's prediction that DRPs and DGs will vote as load. Many appellees argue that these new entrants are more likely to vote with suppliers since the appellees believe that their economic interest is in higher prices.

It is axiomatic that participants are likely to vote in their own economic interests. However, even similarly situated market participants may view their own economic interests differently and the evidence in this case does not support a conclusion that members of the MC always vote as blocks of either load or supply. Moreover, we are unable to determine whether the interests of DRPs or DGs would likely cause them to vote as load or as supply. Only experience will provide the answer.

Based on all the evidence and arguments presented, we cannot find that the MC-approved proposal would confer an unfair advantage upon loads or unreasonably skew future governance votes because a conclusion that the interests of DRPs or DGs would likely cause them to vote as load would be speculative at this time. We are thus not persuaded to substitute our judgment for that of the MC on this point.

Nonetheless, the Board is committed to maintaining a balanced and workable voting structure. We would be concerned if evidence in the future indicated that the voting balance in stakeholder governance was trending in favor of load or supply. Such a trend could jeopardize the continued competitiveness of the NYISO markets. Therefore, the Board is directing its staff to monitor future MC votes for evidence of skewing in either direction. If IPPNY's prediction is correct, and significant numbers of DRPs and

DGs join the MC and regularly vote with load-interests such that legitimate and necessary supplier-supported efforts are thwarted, NYISO's monitoring of the governance structure will uncover such unfair outcomes. We will propose necessary remedies at that time. On the other hand, if IPPNY's prediction is incorrect, and these new participants vote as supply, neither IPPNY nor the markets are harmed. Indeed, if these new participants vote as supply, IPPNY may gain additional support in the governance process under the voting clarifications approved by the MC. We also note that the Board's appellate review process and its ability and willingness to take independent action will continue to serve as an immediate check on MC bias, should such bias arise.

IPPNY's Proposal: IPPNY urges that DRPs and DGs be incorporated into stakeholder governance by adding a new subsector to which all sectors would contribute an equal voting percentage. Under the IPPNY proposal, the existing sectors and subsectors would "contribute" a pro rata portion of their existing voting weight in order to create a new subsector with a 2% voting weight. IPPNY argues that only this approach will avoid taking voting rights solely from the suppliers' side of the market and they urge us to remand this issue for further work in that direction. Appellees counter that a new subsector is unreasonable since these new participants "clearly fit" the definition of Others Suppliers. They also complain that the IPPNY proposal disproportionately draws voting weight away from loads to support the new subsector.

We understand that the proposal approved by the MC was itself the product of a series of MP discussions. While the proposal IPPNY puts forth in their second appeal is not irrational on its face, we need not reach the merits of IPPNY's second appeal because we find no flaw in the MC proposal sufficient to justify its reversal. The Board is hesitant to reverse Management Committee actions when, as with this appeal, we find insufficient evidence to support the appellant's claims of harm, wrongdoing or danger to the markets. In the absence of a clear demonstration of error, and in light of our conclusions that the MC proposal is reasonable, we see no reason to second guess the decisions already made. We thus decline to remand this issue for further work.