UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator, Inc.) Docket No. _____

REPORT OF TARIFF IMPLEMENTATION ERRORS
REQUEST FOR APPROVAL OF PROPOSED COMPENSATION METHODOLOGY
AND REQUEST FOR LIMITED TARIFF WAIVERS OF
THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.

The New York Independent System Operator, Inc. ("NYISO") submits this filing:

(i) to report on its implementation of an erroneous Day-Ahead guarantee payment impact test, called the guarantee payment 2 ("GP2") test. The GP2 test was used to test guarantee payment impact under the NYISO's conduct and impact mitigation framework from May 1, 2004 to January 31, 2005. The NYISO determined that the GP2 test did not appropriately test guarantee payment impact in accordance with the requirements of Section 3.2.1(2) of its Market Mitigation Measures ("MMM")[1] in mid/late January of 2005 and ceased applying the test on February 1, 2005;

(ii) to request the Federal Energy Regulatory Commission's ("Commission's") approval of the NYISO's proposed methodology of ensuring that generators that were erroneously mitigated by the GP2 test are not harmed by the GP2-based mitigation; and

[1] The NYISO's MMM are set forth in Attachment H to its Market Administration and Control Area Services Tariff ("Services Tariff").

(iii) to request such limited tariff waivers as may be necessary to preclude any obligation to retroactively restate market clearing prices on days when generators were mitigated solely by the GP2 test and subsequently committed.

The NYISO asks that the Commission act on this filing by April 10, 2006, in order to provide the NYISO with adequate time to process customer bills that will be impacted hereby.

Background Information

The NYISO implemented its Day-Ahead GP2 guarantee payment impact test as part of a package of improvements to its mitigation software. GP2 was one of two tests that were implemented by the NYISO on May 1, 2004 to permit the NYISO to automatically test for guarantee payment impact in its Day-Ahead Market ("DAM").[2] As the NYISO explained on page 31 of its November 26, 2003 filing in docket No. ER04-230-000, the guarantee payment 1 ("GP1") and GP2 automated guarantee payment impact tests were put in place to satisfy the NYISO's longstanding commitment to automate the testing of guarantee payment impacts.[3]

There is a conceptual flaw in the GP2 test that caused the NYISO to disable that test on February 1, 2005, shortly after the flaw was discovered. The purpose of the NYISO's guarantee payment impact test is to identify a generator that has submitted bids that, unless mitigated, would enable the generator to increase its guarantee payment revenues beyond certain percentage thresholds that are set forth in Section 3.2.1(2) of the MMM. However, generators that do not

[2] Unless otherwise specified, capitalized terms used in this filing have the meanings specified in the NYISO's Services Tariff.

[3] *See* the NYISO's March 20, 2002 compliance filing in Docket Nos. ER01-3155, ER01-1385 and EL01-45 at 31 ("In connection with the development of the necessary software, the NYISO anticipates that at least initially the AMP may not be able to assess the impact of bidding on guarantee payments.").

receive a Day-Ahead schedule are not eligible to receive guarantee payments, and thus cannot have a guarantee payment impact. The GP2 test was overbroad in its application because it tested and, if impact was identified, led to the mitigation of generators that would not, but for the GP2 mitigation, have received a Day-Ahead schedule in the first place.

Generators that would not have been committed but for the GP2 mitigation, and that were mitigated solely because they failed the GP2 impact test (i.e., generators that did not also fail either the GP1 or the LBMP impact tests), should not have been mitigated for guarantee payment impact because, absent the GP2-based mitigation, this subset of generators would not have received a Day-Ahead schedule and thus would not have been eligible to receive any guarantee payments at all.

When the NYISO eliminated the GP2 test on February 1, 2005, it addressed all going-forward GP2-related tariff compliance issues. The NYISO continues to use its GP1 test to test bids for guarantee payment impact in its DAM, so there is no "hole" in the NYISO's Day-Ahead mitigation scheme that needs to be addressed. This filing does not request any changes to the NYISO's tariffs, and does not propose any retroactive changes to market clearing prices. To the contrary, in this filing the NYISO seeks approval of a proposed method for ensuring that no GP2 mitigated generator is harmed by the GP2 mitigation and asks the Commission to confirm the application to the reported matters of its policy in favor of price certainty and against retroactive changes in market clearing prices by the application of market mitigation measures. The Day-Ahead mitigation issues addressed in this filing are not related to the Real-Time mitigation issues that the NYISO brought to the Commission's attention in its November 8, 2005 filing in Docket No. ER06-185-000.

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II. List of Issues

This filing presents the issues whether the Commission should, under the facts and circumstances described below:

(1) Accept the NYISO's proposal to compensate or hold harmless GP2 mitigated generators. Generators that actually started in Real-Time will have their unmitigated DAM bids restored and will receive guarantee payments consistent with those bids. Generators that did not actually start in real-time will be held harmless by voiding their DAM and real-time schedules, including any balancing obligations.

Authorities on which the NYISO relies include *New York Independent System Operator, Inc*., 110 FERC ¶ 61,227 (2005); *New York Independent System Operator, Inc*., 109 FERC ¶ 61,163 (2004); and *New York Independent System Operator, Inc*., 95 FERC ¶ 61,471 (2001), as well as authorities confirming that the Commission's discretionary authority is at its "zenith" when fashioning remedies. *See, e.g.*, *New York Independent System Operator, Inc.* 113 FERC

¶ 61,155 at P 47 (2005) (*citing Connecticut Valley Electric Co. v. FERC*, 208 F.3d 1037, 1043 (D.C. Cir. 2000), *Niagara Mohawk Serv. Corp. v. FPC*, 379 F.2d 153, 159 (D.C. Cir. 1967), *Louisiana Public Service Commission v. FERC*, 174 F.3d 218, 225 (D.C. Cir. 1999)). The NYISO further relies on the analysis of these authorities set forth in Section IV of this filing.

(2) Confirm the application of § 4.2.2(d) of the MMM, and the Commission's policy in favor of price certainty and against retroactive application of market mitigation measures to change market clearing prices, to bar any redetermination of LBMPs in connection with the GP2 mitigation that occurred from May 1, 2004 to January 31, 2005; and

(3) Waive any other provisions of the Services Tariff if and to the extent they could be interpreted to require retroactive mitigation of LBMPs or would otherwise be inconsistent with any action requested in this filing.

Authorities upon which the NYISO relies in support of its position on issues (2) and (3) include: *New York Independent System Operator, Inc., et al*., 90 FERC ¶ 61,317 (2000); *New York Independent System Operator, Inc.*, 93 FERC ¶ 61,187 (2000) (Commission policy against retroactive mitigation); as well as, for the Commission's tariff waiver authority, *Wisvest-Connecticut*, 101 FERC ¶ 61,372 at 62,551 (2002) (observing that error was "an inadvertent mishap"); *Great Lakes Gas Transmission Limited Partnership*, 102 FERC ¶ 61,331 (2003); *TransColorado Gas Transmission Co.*, 102 FERC ¶ 61,330 (2003); and *Northern Border Pipeline Co.*, 76 FERC ¶ 61,141 (1996). The NYISO further relies on the analysis of these authorities set forth in Sections IV.D and VI of this filing.

III. Explanation of Mitigation Error Associated with Implementation of GP2 Guarantee Payment Impact Test

On May 1, 2004 the NYISO implemented two Day-Ahead automated guarantee payment impact tests: the GP1 test, which the NYISO continues to use to test for guarantee payment impact in its DAM, and the GP2 test, which the NYISO ceased applying on February 1, 2005. Below the NYISO explains how the GP1 and GP2 tests work, the differences between the GP1 and GP2 tests, and why the GP2 was later determined not to be necessary and not to conform to the requirements of Section 3.2.1(2) of the NYISO's MMM. The issues addressed below are not related to the real-time mitigation issues that the NYISO brought to the Commission's attention in its November 8, 2005 filing in Docket No. ER06-185-000.

A. Explanation of How and Why the NYISO Tests for Guarantee Payment Impact

The NYISO tests bids for guarantee payment impact to prevent Market Participants from increasing their guarantee payments by submitting incremental Energy, Minimum Generation or "Mingen" and/or Start-Up Bids that are not disciplined by competitive forces. The test ensures that a generator's guarantee payment, calculated over the course of a 24-hour day, does not exceed the guarantee payment that the generator would be able to receive under competitive conditions by more than a margin that is set forth in Section 3.2.1(2) of the MMM.

Once an appropriate Automated Mitigation Procedure ("AMP") arming threshold has been satisfied,[4] generators that have been economically committed in the DAM are GP1 tested for guarantee payment impact by comparing the guarantee payment that a generator would receive over the course of a 24 hour day using unmitigated bids to the guarantee payment that a

[4] AMP arms when LBMPs exceed $150/MWh or when there is congestion in-City. *See* MMM §§ 3.2.1(b)(1), 3.2.2(d).

generator would receive over the course of the same day substituting reference levels for any/all of the three bid parameters (Start-up, Mingen, or Energy) that failed the conduct test. During the time period at issue in this filing, if the use of unmitigated bids increased guarantee payments by 200% or more in unconstrained areas,[5] or increased guarantee payments by 50% in New York City (the "City") over the course of the day, then the NYISO replaced the conduct-failing portion(s) of the bids with reference levels based on its determination that the bid in question had GP1 impact.

B. Explanation of the GP2 Impact Test and How it was Flawed

The GP1 impact test only applies to generators that have been economically committed in the NYISO's Day-Ahead Security Constrained Unit Commitment ("SCUC") software's first bid pass ("Bid Pass 1"). The GP2 test was very similar to the GP1 test, but the GP2 test's scope was not limited to generators that were economically committed in Bid Pass 1. GP2 tested the set of generators that SCUC committed after replacing the conduct-failing components of their bids with reference prices in the first AMP pass ("AMP Pass 1") of the NYISO's SCUC software.[6] Unlike the GP1 test, the GP2 tested both generators that would have and generators that would not have been economically committed by SCUC, absent mitigation. The GP2 test

[5] At the time the GP2 test was active, from May 1, 2004 to January 31, 2005, the NYISO was authorized by the Commission to mitigate generators in unconstrained areas (outside New York City) in accordance with its then applicable MMM. The NYISO is not presently authorized to utilize fully automated mitigation outside the City. However, the NYISO is authorized to use its automated tools to assist in performing mitigation outside the City once the NYISO has consulted with the affected Market Participant. *See New York Independent System Operator, Inc.*, 112 FERC ¶ 61,284 *mimeo* at PP. 17-20 (2005).

[6] The AMP Pass 1 of SCUC is the pass that the NYISO uses to test bids for potential LBMP impact. The fact that a reference price has been substituted in SCUC's AMP Pass 1 does not necessarily mean the unit in question will ultimately be mitigated.

(1) determined the guarantee payment that the generator would have received over the course of a 24 hour day if the generator had been committed at its SCUC AMP Pass 1 schedule and compensated in accordance with its original bids, and (2) compared that amount to the guarantee payment that the generator would have received over the course of the entire day if the generator had been committed at its SCUC AMP Pass 1 schedule, but the conduct-failing components of the generator's bids were replaced with reference prices. If the use of unmitigated bids increased guarantee payments for the unit by 200% or more in unconstrained areas, or by 50% or more in New York City, over the course of the day, then the NYISO replaced the conduct-failing portion(s) of the bids with reference levels. The problem with the GP2 test was, as explained in greater detail below, that it was premised on circular logic and based its determination of guarantee payment impact on the assumption that the generators being tested would be mitigated and then committed.

Generators that were economically committed in the DAM from May 1, 2004 to January 31, 2005 were, with few exceptions,[7] subject to guarantee payment impact testing using both the GP1 and GP2 impact tests. The only difference between the GP1 and GP2 tests was the schedules and LBMPs that were used to test for impact. The GP1 test is based on SCUC's Bid Pass 1 schedule and LBMPs, while the GP2 test relied on SCUC's AMP Pass 1 schedule and LBMPs. The same original offers and mitigated bids are used in each of the two tests. The

[7] GP1 tests generators that would have received a Day-Ahead schedule in the absence of any mitigation. GP2 tested generators that would have received a Day-Ahead schedule if the NYISO mitigated all of the conduct-failing components of the bids it received. The vast majority of generators that receive schedules in SCUC's Bid Pass 1 also receive schedules in SCUC's AMP Pass 1. However, generators that were marginally economic in the bid pass can be displaced in the AMP pass by generators that become more economic because reference prices are substituted for the conduct failing components of each generator's bids in AMP Pass 1.

difference in the schedules used to perform the test was only rarely of consequence. Thus, generators committed in Bid Pass 1 that should have been mitigated for guarantee payment impact were mitigated based on GP1 impact. In addition to GP1 mitigation, generators that had a significant impact on LBMPs were mitigated based on the separate LBMP impact test that is set forth in sections 3.2.1(1) (for unconstrained areas) and 3.2.1(3) (for Constrained Areas that are experiencing constraints) of the MMM.

Thus, the generators that were purely GP2 mitigated were generators (1) that submitted uneconomic bids (generators that were not committed in Bid Pass 1), (2) that did not have an LBMP impact that warranted mitigation, and (3) which, absent mitigation, would not have received a Day-Ahead commitment. As explained previously, the GP2 test is a guarantee payment impact test. Generators that are not committed and that do not receive a schedule are not eligible to receive a guarantee payment.[8] If the bids submitted by the generators that were mitigated based on GP2 impact had been left undisturbed, the bids would not have been economic, the generators would not have received Day-Ahead schedules and there would have been no guarantee payment owed to those generators, so there would not have been any need for GP2 mitigation.

The flaw in the GP2 logic was first identified by a Market Participant in mid/late January, 2005. Once the flaw was confirmed by the NYISO and its Market Advisor, and after the NYISO determined that disabling the GP2 test would not leave its markets open to manipulation, the NYISO acted quickly to correct the problem and notify its Market Participants. The NYISO fixed the GP2 problem by leaving the Day-Ahead GP1 and LBMP impact tests in place to

[8] *See* Attachment C to the NYISO's Services Tariff.

protect its markets, while eliminating the GP2 impact test. The GP2 test was disabled on February 1, 2005.

C. The NYISO's Guarantee Payment Test Implementation Process

Both the GP1 and GP2 tests were implemented after consultation with the NYISO's Market Participants. Over a period of several months the NYISO discussed and received comments on proposed revisions to the software rules implementing its mitigation measures from participants in the Business Issues Committee's "AMP ICM Task Force." Participation in the Task Force was open to all Market Participants and the documents that were discussed were all publicly posted on the NYISO's web site. As part of the review process the NYISO's Market Participants were provided multiple iterations of the NYISO's "Automated Mitigation Concept of Operations" ("ConOp") that specifically described the NYISO's proposed guarantee payment tests. A copy of the pages of the ConOp that discuss the GP1 and GP2 tests are included in Attachment A hereto. The attached excerpts from the ConOp accurately described how both the GP1 and GP2 tests would operate. The GP2 test is set forth on page 10 of the ConOp as follows:

$$\frac{GP_3}{GP_4} \geq TGP$$

The ConOp explains that GP_3 and GP_4[9] are the guarantee payments based on "pass 1B" (referred to herein as AMP Pass 1) prices and schedules and that TGP is the "[g]uarantee payment

[9] GP_3 is guarantee payment that the generator being tested would have received over the course of a 24 hour day if the generator had been committed at its SCUC AMP Pass 1 schedule and compensated in accordance with its original bids. GP_4 is guarantee payment that the generator would have received over the course of the entire day if the generator had been committed at its SCUC AMP Pass 1 schedule, but the conduct-failing components of the generator's bids were replaced with reference prices.

threshold." The ConOp was provided to members of the AMP ICM Task Force and was publicly available for Market Participant review. The NYISO is not aware of any comments that Market Participants submitted questioning the proposed GP2 test that was described in the ConOp. At the time the GP2 test was implemented, neither the NYISO nor its Market Participants recognized that the application of the GP2 test could result in an erroneous determination of impact. Instead, the test was seen by the NYISO and its Market Participants as a legitimate method of preventing the exercise of market power and ensuring that generators committed in the AMP pass were tested for guarantee payment impact in accordance with the MMM.

As explained above, the GP1 test that the NYISO continues to use to test Day-Ahead bids for guarantee payment impact does not suffer the same flaw in logic as the GP2 test. It applies only to economically committed generators and continues to be used to automatically test in-City generators for guarantee payment impact at the end of each dispatch day. The NYISO intends to begin discussing possible improvements to the GP1 test with its Market Participants later this year.

IV. Proposed Method of Ensuring that GP2 Mitigated Generators are Not Harmed

A. The Commission Must Balance the Interests of Impacted Generators and Loads

The NYISO's implementation of the GP2 impact test was an error that the NYSO made with the intent of ensuring full compliance with the tariff requirements for mitigating abuses of market power, after consulting with its Market Participants (including but not limited to the affected generators). The entities that have been harmed by the erroneous implementation of GP2 are the GP2 mitigated generators. The monies the NYISO proposes to use to compensate

the GP2 mitigated generators would be charged to NYISO loads as uplift under the NYISO's Rate Schedule 1.

The Commission is responsible for ensuring that the solution it approves to resolve the GP2 error is just and reasonable and does not unduly prejudice any affected party.[10] The NYISO accordingly proposes a fair and balanced compensation methodology that will ensure that (a) no GP2 mitigated generator is financially harmed by the GP2 mitigation, (b) GP2 mitigated generators that ran in Real-Time to meet the schedules that resulted from GP2 mitigation are compensated based on their unmitigated bids, (c) loads only provide compensation for services that were actually provided by the affected generators, and (d) settled expectations are not disrupted and unquantifiable consequences are not caused by restating market clearing prices. The NYISO's proposed compensation methodology strikes an appropriate balance among all affected entities and is consistent with prior Commission decisions that address compensation for erroneous mitigation, for the reasons explained below.

B. NYISO Proposed Compensation Methodology

The NYISO's tariffs do not instruct the NYISO on how to compensate generators that were mitigated and scheduled due to an improper determination that the generator's bid had a guarantee payment impact.[11] The NYISO proposes to compensate generators that were

[10] *See* Federal Power Act §§ 205 and 206, 16 U.S.C. §§ 824d and e.

[11] Section 4.2.2(c) of the NYISO's MMM addresses circumstances where the NYISO mitigated based on an incorrect reference level. Section 4.2.2(c) of theMMM is not applicable to the issues raised in this pleading because the NYISO applied the correct reference levels to the GP2 mitigated bids.

mitigated and scheduled in the DAM based solely[12] on a determination that the generator had GP2 impact as follows:

(1) All GP2 mitigated generators that actually started in Real-Time[13] will receive guarantee payments consistent with their unmitigated DAM bids;

(2) Generators that did not actually start in real-time will be held harmless by voiding their DAM and real-time schedules, including any balancing obligations.[14]

The NYISO's proposed methodology is appropriate because it provides compensation to generators that ran to satisfy their schedules in Real-Time and ensures that generators that did not run in Real-Time are placed in the same financial position they would have been in if they had not been mitigated and committed Day-Ahead. The NYISO's proposal appropriately balances the interests of affected generators and loads and is consistent with the Commission's decisions addressing compensation to erroneously mitigated Market Participants.

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[12] The mitigated bids of generators that had GP2 impact, but that also had GP1 or LBMP impact, would not be corrected. This is appropriate because the GP1 and LBMP impact tests each present independent, Tariff-compliant bases for determining impact under the MMM.

[13] The generators that started in Real-Time ran in good faith to satisfy the Real-Time schedules that resulted from each generator's GP2 mitigated Day-Ahead schedule. Had that not been the case, the NYISO might have modified its proposed compensation methodology.

[14] Over the period when GP2 was in effect there were a total of ten instances in which generating units did not operate in Real-Time to satisfy their Day-Ahead schedules that resulted from GP2 mitigation. In three of these instances, the generators called in a full derate to the NYISO. Two of the remaining instances involved in-City GTs that were mitigated for both LBMP and GP2 impact (mixed mitigation). These units likely would have received Day-Ahead schedules even absent the GP2 mitigation. As explained in this filing, the NYISO is only proposing to eliminate the portions of these generators Day-Ahead and resulting Real-Time schedules that were the result of GP2 mitigation. The remaining five instances all involved in-City units that received GP2 schedules of 2 hours or less duration. The mitigated DAM bids of these units were not economic in Real-Time, so these units were not dispatched in Real-Time.

C. The NYISO's Proposed Compensation Methodology Comports With Commission Precedent

In its first order accepting the NYISO's proposed AMP, the Commission announced "if the NYISO subsequently determines that the bid [that was erroneously mitigated] was not an attempt to assert market power, the generator will be paid its full bid."[15] The Commission has subsequently discussed its "full bid" compensation methodology in a pair of orders,[16] the most recent of which accepted for filing proposed tariff revisions containing provisions that address how generators that are mitigated using incorrect reference prices are to be compensated.[17] This most recent order was issued on March 4, 2005 in Docket No. EL03-26-004 (the "2005 Order"). In its 2005 Order the Commission explained:

> Erroneous mitigation may force a supplier to provide more energy than if the erroneous mitigation had not occurred. The erroneous mitigation would harm the supplier to the extent that its additional costs for supplying this additional energy exceed the additional market revenues that it received. 2005 Order at P 18.
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> . . .
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> [C]ompensating a supplier as if the mitigated megawatts had set the market price would, in effect create a separate LBMP for this supplier only that exceeds the actual LBMP and would amount to a windfall payment to the supplier at the expense of New York electricity customers. [Footnote omitted.] Moreover, such a remedy would be unfair to all the other suppliers who did not receive this *artificial* LBMP. [Emphasis in original.] 2005 Order at P 20.

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[15] *New York Independent System Operator, Inc*., 95 FERC ¶ 61,471 *mimeo* at n. 9 (2001).

[16] *New York Independent System Operator, Inc*., 110 FERC ¶ 61,227 (2005); *New York Independent System Operator, Inc*., 109 FERC ¶ 61,163 (2004).

[17] The GP2 error did not involve an error in computing the affected generators' reference prices. Instead it involved an incorrect determination that a particular conduct-failing bid had guarantee payment impact. The tariff provisions addressing the compensation to be paid when the NYISO mitigates based on an inaccurate reference price are not directly applicable to this proceeding.

The 2005 Order sets forth two controlling principles applicable to the compensation of the GP2 mitigated generators. First, the compensation methodology must ensure that GP2 mitigated generators are not required to incur costs for supplying Energy that exceed the revenues that the generators receive; that is, the generators must be held harmless from additional net operating costs caused by the mitigation. Second, the compensation methodology should not result in a windfall payment to GP2 mitigated suppliers at the expense of New York electricity customers. Application of these principles fulfills the Commission's obligation under Federal Power Act Sections 205 and 206 to ensure that rates are just and reasonable and are not unduly preferential or prejudicial.

The NYISO's proposed methodology implements the principles set forth in the Commission's "full bid" orders. Under the NYISO's methodology, GP2 mitigated generators that ran in real-time and incurred operating costs to satisfy obligations that resulted from their Day-Ahead commitment will be compensated at the greater of the Day-Ahead market price or the unit's unmitigated DAM bid(s). Any Real-Time commitments undertaken by a generator in excess of its GP2 DAM schedule will be compensated at the appropriate Real-Time price, in accordance with normal expectations.

The NYISO's DAM is a financial market. Cost incurred by GP2 mitigated generators that did not run in Real-Time to satisfy Real-Time schedules that resulted from their Day-Ahead GP2 commitment are limited to purchasing replacement Energy, meeting other balancing obligations and possibly covering undergeneration penalties. The NYISO's proposal would "zero out" the Day-Ahead schedules of generators that did not run in Real-Time, ensuring that these generators would not incur any such costs due to their GP2 mitigation and commitment. Instead, the generators would be placed in the same position that they would have been in if the

GP2 test had not resulted in the mitigation of their bids and DAM commitment. This provision of the NYISO's proposal also ensures that GP2 mitigated generators that did not operate will not receive a guarantee payment windfall at the expense of New York electricity customers.

The Commission should accept the NYISO's proposed compensation methodology because it complies with prior Commission directives addressing erroneous mitigation and appropriately balances the interests of all affected parties.

D. The Commission Should not Require Day-Ahead Market-Clearing Prices to be Restated

Certain of the NYISO's Market Participants have argued that the NYISO should be required to re-run its DAM for the days on which GP2 related mitigation affected market prices. The NYISO disagrees with this suggestion for several reasons.

First, the Commission has explained that it does not intend that mitigation entail any retroactive recalculation of market clearing prices.

> The market mitigation plan is designed to target specific behavior by specific entities believed to have engaged in anti-competitive behavior and any mitigation measures taken against an entity are specific to the entity. Moreover, the Commission, in approving the NYISO's market mitigation plan stated that it did not intend for mitigation to entail any retroactive recalculation of market-clearing prices.[18]

If the NYISO erroneously fails to mitigate a generator that it should have mitigated under its Commission-accepted MMM, the NYISO may not go back and revise market prices to reflect the missed mitigation. Sections 4.2.2(c) and 4.3.3(d) of the NYISO's MMM implement the

[18] *New York Independent System Operator, Inc.*, 93 FERC ¶ 61,187 *mimeo* at 6 (2000); *citing New York Independent System Operator, Inc., et al*., 90 FERC ¶ 61,317 *mimeo* at 7 (2000) ("We require the ISO to file a further revised mitigation plan to clarify that mitigation for market power is prospective only. We do not intend for mitigation to entail any retroactive recalculation of market-clearing prices.").

Commission's directive. Section 4.2.2(d) of the MMM states "The ISO shall not use a default bid to determine revised market clearing prices for periods prior to the imposition of the default bid, except as may be specifically authorized by the Commission." Because the NYISO is not authorized to restate market clearing prices when it erroneously fails to mitigate a generator that it should have mitigated (when it errs in the generator's favor), the NYISO believes that it would be similarly inappropriate to retroactively restate market clearing prices if the NYISO erroneously mitigates a generator that it should not have mitigated (when it errs in the loads' favor). The NYISO has not restated DAM clearing prices to address past mitigation concerns.

Second, a given set of DAM prices corresponds to a specific DAM schedule in which resources are committed to satisfy expected loads based on the bids that are submitted to the market (after accounting for appropriate mitigation). In the NYISO's discussions with its Market Participants, the vast majority of the Market Participants that favored re-running the DAM were proposing that the NYISO re-run the DAM without GP2 mitigation to come up with revised prices.[19] The revised prices derived from re-running the DAM would then be paid to the generators that were committed in the original (not revised) DAM based on their original (not

[19] Alternatively, some Market Participants may argue that the NYISO should re-run its DAM and use both the revised prices and the revised schedules that result. While this proposal would result in consistent Day-Ahead prices and schedules, it could produce dramatic inconsistencies between Day-Ahead and Real-Time schedules and prices because the Real-Time Market cannot be re-run (it is based on actual Real-Time operation). Inconsistencies between Day-Ahead and Real-Time prices and schedules could have significant inequitable consequences. For example, generators that are scheduled in the revised DAM at a level in excess of their original DAM schedule would be required to buy out of all or a portion of their new or additional DAM obligation at (potentially unfavorable) Real-Time prices because it is no longer possible for these generators to run in Real-Time to satisfy their obligation (they would become *de facto* virtual suppliers). Price capped load bids that were accepted in the original DAM but that are not accepted in the revised DAM due to higher Day-Ahead prices would lose the opportunity to contract in the bilateral market to hedge their Real-Time exposure.

revised) schedules. Paying suppliers that were accepted in the DAM, as originally run, based on the restated Day-Ahead prices would create obvious inconsistencies between prices and schedules, and would likely have other inappropriate consequences, including mismatches between:

(a) Day-Ahead schedules and resulting Real-Time obligations;

(b) virtual load/supply bids and schedules (virtual load/supply could be scheduled at a price that is not consistent with its bid); and

(c) price-capped load bids and schedules (price-capped load could be scheduled at a price that exceeds its bid).

As the Commission has implicitly recognized in its policies against retroactively restating market-clearing prices, it is far from evident that re-running the markets in the manner proposed would produce results that were fair or equitable to all Market Participants (some Market Participants would be better off, others would be worse off). The NYISO proposes to avoid disrupting settled expectations and other potentially inequitable consequences of restating the markets by limiting remedial actions to holding harmless inappropriately mitigated generators in the manner proposed herein.

The NYISO recognizes that its proposal to compensate generators with GP2 mitigated bids instead of re-running the DAM impacts which Market Participants must bear a portion of the cost of the GP2 mitigation error. The NYISO is not aware of any method of addressing the GP2 mitigation error that will satisfy all of its Market Participants. For the above reasons, the NYISO believes that its proposal to ensure that no generator that had a bid mitigated based on the GP2 impact test is harmed by the GP2 mitigation is a better choice than disrupting settled market expectations by requiring the NYISO to re-run its DAM and re-state Day-Ahead prices for all 82 days in which mitigation of bids based on GP2 impact occurred.

V. Financial Impact of GP2 Mitigation

Under the NYISO's proposed compensation methodology, uplift payments of approximately $1,001,000 will be made to compensate GP2 mitigated generators for the period May 1, 2004 to January 31, 2005. Approximately $356,000 in uplift will be paid to in-City generators, while the remaining $645,000 will be paid to generators located outside New York City. In addition the NYISO will reclaim slightly more than **$**50,000 (net) in balancing payments/charges when it eliminates the Day-Ahead and Real-Time schedules and balancing obligations of generators that did not run in Real-Time to satisfy the schedules that resulted from their Day-Ahead GP2 mitigation.[20]

Because GP2 was used to mitigate bids outside New York City on five days in January of 2005,[21] the LBMP impact of mitigation on units located outside the City was not constrained by the tight in-City LBMP mitigation thresholds on those days. Although the LBMP impact of GP2 mitigation outside New York City averaged only -$0.84/MWh, a -$30.55/MWh LBMP impact was identified on Long Island for hour beginning ("HB") 12 on January 27th. The next largest hourly LBMP impact identified was -$15.91/MWh at Millwood in HB 09 on January 24th. The -$0.84/MWh average LBMP impact makes clear that the -$30.55/MWh and -$15.91/MWh single hour, single zone, impacts were statistical outliers. The NYISO estimates that the total change in LBMP revenues paid to generators over the five affected days was approximately -$1,617,040.

[20] The NYISO has provided the days and hours on which generators were mitigated based on a determination of GP2 impact to the appropriate Market Participants.

[21] January 17, 22, 24, 25 and 27, 2005.

This represents a decrease in generator revenues of less than 1% over the relevant days due to GP2 mitigation.[22]

VI. Tariff Waivers

Under the Services Tariff, generators submit three-part bids into the Real-Time Market, that is, bids for Energy, Mingen, and Start-up. The marginal Energy bid sets the market-clearing price (LBMP) for Energy. All three bids are used to commit units and determine whether they should receive a guarantee payment for a given operating day. A guarantee payment is made if a unit's total as-bid costs are greater than its revenues over the course of a 24-hour operating day. While LBMP prices are established by the market clearing price for a given geographic market area, guarantee payments are necessarily determined on a unit-by-unit basis. As a result, guarantee payments are ultimately determined in the billing and settlement process for each unit, and only affect that unit. By contrast, Energy clearing prices, or LBMPs, are paid to all units selected for Energy, and once determined cannot be changed without disrupting the settled expectations of all entities participating in the Energy market. The Commission has determined that, as specified in § 4.2.2(d) of the MMM: "The ISO shall not use a default bid to determine revised market clearing prices for periods prior to the imposition of the default bid, except as may be specifically authorized by the Commission."[23]

In January of 2005 the NYISO learned that its GP2 guarantee payment impact test did not conform to applicable tariff requirements. In this filing, the NYISO proposes a method of either

[22] Estimated LBMP impacts are provided for informational purposes only. The NYISO is not proposing to retroactively revise market prices to address the LBMP impact of GP2-related mitigation.

[23] MMM § 4.2.2(d).

compensating or cancelling the Day-Ahead, Real-Time and balancing obligations of GP2 mitigated generators which, if accepted by the Commission, will, prior to the final billing settlements with the affected units, ensure that all affected generators are held harmless in the manner proposed in Section IV.B, above. The NYISO's proposal is a reasonable remedy for an inadvertent error that falls well within the Commission's broad remedial discretion.[24]

In addition, however, the mitigation of DAM bids based on findings of GP2 impact also affected Day-Ahead LBMPs in certain instances. Although the precise effects would be difficult to quantify because of the difficulties and uncertainties inherent in attempting to redetermine market-clearing prices retroactively, for the reasons discussed in Sections IV.D and V of this pleading, the NYISO believes any effects would be relatively small and would not warrant departure from the Commission's policy against the retroactive application of market mitigation measures to change market clearing prices. Accordingly, the NYISO requests that the Commission confirm the application of § 4.2.2(d) of the MMM to the situations described in this filing, and otherwise waive the application of any contrary requirements of the Services Tariff during the specified periods so as not to require any retroactive changes to market clearing prices.

The Commission's evaluation of whether it should permit tariff waivers in order to help alleviate the effects on an error has focused on several key points, including whether: (1) the underlying error was made in good faith; (2) the waiver is of a limited scope; (3) a concrete

[24] It is well established that the Commission's discretionary authority is at its "zenith" when fashioning remedies. *See, e.g.*, *New York Independent System Operator, Inc.* 113 FERC ¶ 61,155 at P 47 (2005) (*citing Connecticut Valley Electric Co. v. FERC*, 208 F.3d 1037, 1043 (D.C. Cir. 2000), *Niagara Mohawk Serv. Corp. v. FPC*, 379 F.2d 153, 159 (D.C. Cir. 1967), *Louisiana Public Service Commission v. FERC*, 174 F.3d 218, 225 (D.C. Cir. 1999)).

problem needs to be remedied; and (4) the waiver will not have undesirable consequences, such as harming third parties.[25]

All of these factors are present in this case. As explained above, the underlying errors are related to difficulties in developing and implementing complex software, and brought no pecuniary or other benefit to the NYISO. Moreover, once the NYISO discovered the errors, it remedied the problems in an expeditious manner, after timely informing the Commission Staff of the issue. The NYISO also informed the stakeholders of the problems and their potential effects in a series of committee and working group discussions. Further, the waiver requested herein is of a limited scope. The NYISO is seeking a one-time waiver of the tariff provisions described above, since the underlying issue has already been resolved. Assuming the NYISO's proposed compensation methodology is accepted and the Commission determines that LBMPs should not be restated, the NYISO will be in compliance with its tariffs. Third, as discussed above, concrete problems exist and need to be remedied. Finally, the requested waiver is consistent with the Commission's policy against retroactive changes in market clearing prices as the result of the application of market mitigation measures.[26] The requested waivers will prevent harm to Market Participants by preventing the disruption of settled expectations about historic market clearing prices. The negative effects of retroactively changing market clearing prices may well outweigh any benefits of the corrections.

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[25] *See, e.g.*, *Wisvest-Connecticut*, 101 FERC at 62,551 (observing that error was "an inadvertent mishap"); *Great Lakes Gas Transmission Limited Partnership*, 102 FERC ¶ 61,331 (2003); *TransColorado Gas Transmission Co.*, 102 FERC ¶ 61,330 (2003); *Northern Border Pipeline Co.*, 76 FERC ¶ 61,141 (1996).

[26] *See* Section IV.D of this pleading.

VII. Service

The NYISO is electronically serving a copy of this filing on the official representative of each of its customers, on each participant in its stakeholder committees, on the New York State Public Service Commission, and on the electric utility regulatory agencies of New Jersey and Pennsylvania. In addition, the complete filing has been posted on the NYISO's website at www.nyiso.com. The NYISO will also make a paper copy available to any interested party that requests one.

VIII. Conclusion

WHEREFORE, for the foregoing reasons, the New York Independent System Operator, Inc., respectfully requests that the Commission:

(a) accept the method of compensating or otherwise holding harmless generators whose bids were mitigated due to a determination of GP2 impact that is proposed in Section IV.B of this filing;

(b) confirm the application of § 4.2.2(d) of the MMM to bar any redetermination of LBMPs in connection with the NYISO's erroneous implementation of the GP2 guarantee payment impact test for the period May 1, 2004 to January 31, 2005, and waive any other provisions of the Services Tariff that could be interpreted to require retroactive redetermination of LBMPs in the situations described above;

(c) act on this filing by April 10, 2006, in order to provide the NYISO with adequate time to process customer bills that will be impacted hereby[27]; and

[27] As explained above, the GP2 mitigation that this filing addresses occurred from May 1, 2004 to January 31, 2005. The NYISO's submission of this filing has been delayed, in part, due to deliberations with its Market Participants and internal deliberations regarding the appropriate (continued…)

(d) grant the NYISO any and all other relief to which it is entitled.

Respectfully submitted,

Alex M. Schnell
New York Independent System Operator, Inc.

February 8, 2006

cc: Shelton M. Cannon
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Dean Wight

method to use to ensure that GP2 mitigated generators are not harmed by the mitigation that occurred; an issue that is addressed in detail in Section IV of this filing. In addition, administrative changes to the NYISO and its MMP impacted the timing of the NYISO's submission of this filing.

Attachment A

Redlined Excerpt From:

Second Draft

Dated July 31, 2003

Automated Mitigation

Concept of Operations (ConOp)

$CTMG_2$	$100.00

6 Impact

6.1 Price Impact

The impact test compares prices (or local congestion) determined with two sets of offers: (i) an original set called the Base-Set and (ii) a set resulting from the mitigation of offers tripping the conduct test (subject to the arming criteria), called the Ref-Set. The price impact test is evaluated at each time interval. The test will trip for an interval if the difference in energy price (or local congestion) is significant. Ultimately a one-hour granularity, aligned with the one-hour offer periods, shall be used and the price impact shall trip for an entire hour if it trips for any interval during the hour.

6.1.1 NYCA Energy Price Impact

The same energy impact threshold is applied to NYCA super-zones DA and RT. The energy impact threshold is currently $100. Currently the DA-AMP measures impacts on price of each zone in a super-zone. Zonal price is a weighted average of prices and the generators within a zone. The energy price impact test in RT-AMP is done at each generator in the super-zone and trips if the threshold is exceeded at any generator. The impact by super-zone is:

- West (zones A-E): If the change in LBMP at the location of any energy supplier in zones A-E exceeds the threshold for a 15-minute RTC interval then all energy resources in zones A-K are subject to mitigation for the hour containing the interval.
- East (zones F-I): If the change in LBMP at the location of any energy supplier in zones F-I exceeds the threshold for a 15-minute RTC interval then all energy resources in zones F-K are subject to mitigation for the hour containing the interval.
- NYC (zone J): If the change in LBMP at the location of any energy supplier in zone J exceeds the threshold for a 15-minute RTC interval then all energy resources in zone J are subject to mitigation for the hour containing the interval.
- LI (zone K): If the change in LBMP at the location of any energy supplier in zone K exceeds the threshold for a 15-minute RTC interval then all energy resources in zone K are subject to mitigation for the hour containing the interval.

6.1.2 Load Pocket Energy Price Impact

The load pocket impact test trips if the change in LBMP at the location of any energy supplier in a load pocket exceeds the threshold for that load pocket. In RT a load pocket is considered to have tripped the impact for the entire hour if it trips for any 15-minute interval in the hour. ~~Separate load pocket thresholds are maintained for DA and RT.~~While the in-City DA-AMP and RT-AMP load pockets are calculated in the same manner, and should be quite close to each other, they probably will not be identical; the average price and the frequency of congestion, two components of the LPT formula, will differ as between DA and RT.

6.2 Guarantee Payment Impact

The Plan requires mitigation of offers for start-up cost, minimum generation cost, and incremental energy cost in the event that there is substantial impact on guarantee payments to the generator, even in the absence of an energy price impact. The guarantee payment is the difference between a supplier's cost and market revenue. However, the guarantee payment can be no less than zero. The DA-AMP accumulates guarantee payments for the full day to determined impact. The guarantee payment test for RT-AMP ~~has no guarantee payment impact test~~will take place after the end of the operating day.

The impact test compares the guarantee payments associated with start-up, minimum generation, and energy ("guarantee payments") with two sets of offers and two sets of schedules. These are:

- An original set of offers, called the Base-Set
- A mitigated set of offers, called the Ref-Set
- The schedules and prices derived from Base-Set

- The schedules and prices derived from Ref-Set

		Offer	
		Base	Ref
Schedule & Price	From Base	GP_1	GP_2
	From Ref	GP_3	GP_4

Guarantee payments shall be determined using original (base-set) and mitigated (ref-set) offers with schedules and prices from pass 1A (base-set results) and pass 1B (ref-set results). Referring to the table above, the four calculated guarantee payments use offer, price, and schedule as shown below:

Guarantee Payment	**Offer**	**Price (LBMP)**	**Schedule**
GP_1	Base	From Base	From Base
GP_2	Ref	From Base	From Base
GP_3	Base	From Ref	From Ref
GP_4	Ref	From Ref	From Ref

Where total cost of an energy resource includes it start-up cost, minimum generation cost, and incremental energy cost. Revenue for the resource is its schedule times the clearing price for energy plus lost opportunity payments, if any. The guarantee payment impact for a generator is the ratio of the two guarantee payments for the time period. The impact test is said to have tripped for an hour, or remainder of an hour, if the ratio of guarantee payments exceeds the Plan's threshold. That is, the test trips if:

$$\frac{GP_1}{GP_2} \geq TGP \text{ , or}$$

$$\frac{GP_3}{GP_4} \geq TGP$$

Where:

Term	**Description**
TGP	Guarantee payment threshold

Provided that either GP_1 is greater than zero, or GP_3 is greater than zero, or both are greater than zero. The test trips if either GP_2 or GP_4 (or both) are equal to zero (that is, with mitigation there would be no guarantee payment).

7 Portfolio Exclusion

The portfolio exclusion of the DA-AMP (aka 50 MW exclusion) shall be modified to recognize the use of SU and/or MG to economically withhold resources. The entire capacity of a generating unit is considered withheld if the conduct test for SU is tripped or if the conduct test for MG is tripped. Otherwise, only the portion of the generating unit that trips the conduct test for incremental energy is considered withheld. Energy offers from generating units subject to the DA-AMP shall not be mitigated if the economic withholding of each organization that may influence that generating unit's offer is less than or equal to a predefined value, designated MW_{limit}. The value of MW_{limit} is currently 50 MW.

The RT-AMP has no portfolio exclusion.