UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator, Inc., *et al.*)	**Docket Nos.**	**ER00-1969-000, ER00-1969-002, ER00-1969-003, ER00-1969-004, ER00-1969-011, EL00-57-000, EL00-57-002, EL00-60-000, EL00-60-002, EL00-63-000, EL00-63-002, EL00-64-000, and EL00-64-002.**

MOTION OF THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC. FOR LEAVE TO SUBMIT A RESPONSE AND RESPONSE TO ANSWERS AND PROTESTS

Pursuant to Rules 212 and 213 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212 and 385.213, the New York Independent System Operator, Inc. ("NYISO"), by counsel, respectfully requests leave to submit a response, and submits this response, to the answers and protests (collectively, the "Answers"), filed in response to NYISO's Motion to Reopen the Record and for Disposition on Remand ("NYISO's Motion"). Answers were submitted in the above dockets by Long Island Power Authority and LIPA (together "LIPA"), Keyspan-Ravenswood, LLC ("Keyspan"), NRG Companies ("NRG"), Orion Power New York GP, Inc. ("Orion"), Indeck Energy Services, Inc., Indeck-Olean, L.P., Indeck Oswego, L.P., Indeck-Yerkes, L.P. (collectively "Indeck") (collectively "Answering Parties"), and the Transmission Owner Intervenors ("Transmission Owners").

REQUEST FOR LEAVE TO SUBMIT RESPONSE

The NYISO recognizes that the Commission generally discourages responses to answers. The Commission has, however, allowed such responses when they help to clarify complex issues, provide additional information that will assist the Commission, correct inaccurate statements, or are otherwise helpful in the development of the record in a proceeding.[1] The NYISO's response meets this standard. The NYISO's response does not introduce new arguments, but instead is submitted for the limited purpose of clarifying certain factual matters and correcting inaccurate or misleading statements in the Answers, thereby assisting the Commission in its review and consideration of the complex issues presented in this proceeding. The NYISO therefore respectfully requests that the Commission exercise its discretion and accept the NYISO's response.

RESPONSE

I. The Commission Previously Found that the Absence of Operating Reserves from B-G Constituted a Market Design Flaw, and that Finding was not Appealed

A "Market Design Flaw" is defined by the NYISO Tariff, as in effect during the Relevant Period, as "a market structure, market design or implementation flaw giving rise to situations in which market conditions or the application of ISO procedures would result in inefficient markets

[1] *See, e.g., Morgan Stanley Capital Group, Inc. v. New York Independent System Operator, Inc.*, 93 FERC ¶ 61,017 at 61,036 (2000) (accepting an answer that was "helpful in the development of the record . . . ."); *New York Independent System Operator, Inc.*, 91 FERC ¶ 61,218 at 61,797 (2000) ("Initial Order") (allowing "the NYISO's Answer of April 27, 2000, [because it was deemed] useful in addressing the issues arising in these proceedings . . . ."); *Central Hudson Gas & Electric Corp.*, 88 FERC ¶ 61,138 at 61,381 (1999) (accepting prohibited pleadings because they helped to clarify the issues and because of the complex nature of the proceeding).

or prices that would not be produced in a workably competitive market."[2] The Commission found in its prior orders that the NYISO's modeling and software relating to the Blenheim-Gilboa pumped storage generation facility ("B-G") constituted a Market Design Flaw, and those findings were not challenged on appeal by any of the Answering Parties. In its Initial Order, the Commission found that

> the New York ISO has already admitted that it has not modeled into its software the possibility that the Blenheim-Gilboa pumped storage facility could provide 10 minute spinning or non-spinning reserves. . . . The New York ISO has in its answers committed to getting this pumped storage facility modeled in the software so that it can be bid into the market as 10 minute reserves.[3]

Likewise, in it Order on Rehearing ("First Rehearing Order"),[4] the Commission stated that:

> The May 31 Order stated that the Blenheim-Gilboa pumped storage facility was not available to supply operating reserves due to NYISO's software flaws. . . . NYISO was directed to add the Blenheim-Gilboa pumped storage facility to its software for spinning and non-spinning reserves as quickly as possible and to address this issue in a September 1 Report.[5]

The Commission also found that the availability of NSR from B-G was a critical assumption in approving market-based rates for operating reserves. The Commission stated in its Initial Order that its approval of market-based rates for Non-Spinning Reserves ("NSR") had been based on, among other things, "the assumption that the Blenheim-Gilboa pumped storage

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[2] *See, e.g.*, *New York Independent System Operator, Inc*., Answer to the NYISO's Motion to Reopen Record and for Disposition on Remand of the NRG Companies, Docket Nos. ER00-1969 *et al.*, at 6 n.21 (July 16, 2004) ("NRG Answer") (citing Attachment E to NYISO's Service Tariff, Original Sheet No. 221, effective February 17, 2000).

[3] Initial Order at 61,800.

[4] 97 FERC ¶ 61,155 (November 8, 2001).

[5] First Rehearing Order at 61,681.

facility could place bids to supply non-spinning reserves . . . ."[6],[7] Thus, the assumed design of the NSR market for which the Commission approved market-based rates "is inconsistent with the actual practice of excluding this supplier from the market."[8]

None of these findings and holdings were challenged on appeal by any of the Answering Parties. Indeed, none of the Answering Parties lodged an appeal from the Commission's orders in these dockets. Thus, those findings and holdings are final, and not subject to being revisited in this limited remand proceeding.

II. The Absence of Operating Reserves from B-G Constituted a Market Design Flaw

Even if the Commission's conclusions that the absence of NSR from B-G constituted a Market Design Flaw were now open to question, the contracts and other documents attached to the Answers in voluminous exhibits, and the discussion of these documents in the Answers, are irrelevant to answering this question. As shown by the tariff language set forth above, nothing in the definition of a Market Design Flaw turns on assigning responsibility for a purported flaw, or requires parsing the history of a flaw to divine the precise reasons why a flaw came about. Instead, the relevant inquiry is whether the structure, design or implementation of the New York markets resulted in inefficient or non-competitive prices. During the period from January 29, 2000, to March 27, 2000 ("Relevant Period"), this test was met by the absence of NSR from B-G and the resulting non-competitive prices for NSR.

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[6] Unless otherwise specified, capitalized terms have the meanings specified in the NYISO's Market Administration and Control Area Services Tariff.

[7] Initial Order at 61,799 n.13.

[8] *Id.*

As the NYISO stated in its Answer to the Complaint of RG&E in EL00-64-000, after discussing how the B-G modeling decisions came about,

> [n]evertheless, the NYISO recognizes that its software prevents Blenheim-Gilboa from providing operating reserves at the levels that RG&E asserts it could provide. To the extent that the NYISO software could be changed to recognize significant operating reserves from Blenheim-Gilboa, the NYISO does not disagree that this situation could be characterized as a Market Design Flaw.[9]

Similarly, the NYISO stated in its Preliminary Compliance Filing and Limited Request for Clarification, submitted on June 30, 2000, in this Docket , that:

> In early June, the NYISO completed modeling changes that permit the Blenheim-Gilboa facility to be utilized as four separate units. These four units may now bid separately into both the 10-minute spinning and/or non-spinning reserves markets when Blenheim-Gilboa is in its generating or 'standstill' mode. The NYISO is currently implementing modeling and software changes to permit the four units to make separate bids into the 10-minute spinning and non-spinning reserves markets when Blenheim-Gilboa is in 'pumping' mode.[10]

The NYISO's September 1, 2000, Combined Compliance Filing and Report in Docket No. ER00-3591-000 further stated that:

> [T]he NYISO's original software modeled the entire Blenheim-Gilboa complex as a single unit and scheduled it either for generation or pumping, but not both. The NYISO was thus prevented from taking full advantage of Blenheim-Gilboa's capabilities as a reserves supplier. . . . The NYISO is pleased to report that it recently finished the programming work on software modifications that will enable the Blenheim-Gilboa units to bid into all three reserves markets when in pumping mode.[11]

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[9] *Rochester Gas and Electric Corp. v. New York Independent System Operator, Inc.*, Answer of NYISO to Complaint, Motion to Consolidate and Request for Fast Track Complaint Procedures of Rochester Gas and Electric Corp., at 6 (April 20, 2000).

[10] *New York Independent System Operator, Inc.*, NYISO's Preliminary Compliance Filing and Limited Request for Clarification, Docket No. ER00-1969, at 4-5 (June 30, 2000).

[11] *New York Independent System Operator, Inc.*, NYISO's Combined Compliance Filing and Report, Docket No. ER00-3591-000, at 13 (September 1, 2000).

As shown in § I above, it was these modeling and software deficiencies that the Commission identified as a Market Design Flaw. Consequently, the Answers are fatally deficient in that none show that the NYISO's software was capable of, or did, recognize NSR from B-G. Nothing in the Answers or their exhibits changes the fact that the NSR market had a critical flaw as compared to the market model anticipated by the Commission in approving market-based rates for NSR.

The Answers in effect acknowledge that the parties entitled to most of the output of B-G (the "B-G Contractors") wanted to change the bidding of B-G in order to participate in NSR markets.[12] But the Answers fail to acknowledge that the B-G Contractors could not bid B-G into the NSR market until the modeling of B-G had been changed in the NYISO's software, and fail to acknowledge that the Commission found in the earlier proceedings in these dockets that these modeling and software configurations were a Market Design Flaw that resulted in defective operation of the NSR market.

In sum, the Answers ignore the fact that modeling and software changes were necessary to recognize the full range of Operating Reserves that could be supplied by B-G. Moreover, after NSR became available from B-G, the resulting NSR prices have been substantially below the level of the NSR bid cap, indicating that the availability of NSR from B-G has had a significant and positive effect on the NSR market, and that the absence of NSR from B-G contributed to conditions that resulted in NSR market outcomes that were not consistent with the results to be

[12] *New York Independent System Operator, Inc.*, Answer of Keyspan Ravenswood, LLC to Motion to Reopen the Record and for Disposition on Remand; Request for Disposition; Alternatively, Request for Hearing, Including Discovery Procedures, Docket Nos. ER00-1969 *et al.*, at 4 (July 16, 2004)("Keyspan Answer") (claiming that: "Market prices signaled the parties to the B-G contracts that their decisions to self-schedule B-G for energy were not the best use of B-G, so the B-G parties changed their contracts and scheduling agreements."); *see also* Keyspan Answer at 16.

expected in conditions of workable competition. Thus, the Answers do not show that the absence of NSR from B-G did not constitute a Market Design Flaw.

III. The NYISO's NSR Refund Proposal is Analytically Sound

Complaints that Dr. Savitt's analysis is based on assumptions about units that were not bid or scheduled for NSR during the Relevant Period beg the question of the purpose of the refund calculation.[13] The whole point of the refund calculation is to correct for a Market Design Flaw that resulted in an important unit not being included in the NSR market.

The Answers assert that Dr. Savitt's analysis improperly assumes that B-G's bids during the proxy periods (the first quarters of 2001-2004) were comparable to what its bids would have been in the Relevant Period.[14] In fact, Dr. Savitt does not base his analysis on assumed bids from B-G or any other unit, but on the levels of NSR *prices*, once the NYISO software and modeling recognized NSR from B-G.[15]

The Answers complain that Dr. Savitt included western NSR prices in his analysis.[16] The Answers do not acknowledge that, because of the locational reliability requirements applicable to NSR, only minimal quantities of western operating reserves, if any, can be used. The NYISO

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[13] *See* NRG Answer at 17-18; *New York Independent System Operator, Inc.*, Answer of Long Island Power Authority and LIPA to Motion of NYISO, and Motion of Long Island Power Authority and LIPA to Establish Procedures, Docket Nos. ER00-1969 *et al.*, at 11 (July 16, 2004) ("LIPA Answer").

[14] *See, e.g., New York Independent System Operator, Inc*., Response of Orion Power New York GP, Inc. to Motion of the NYISO to Reopen Record and for Disposition on Remand, Docket Nos. ER00-1969 *et al.*, at 12 (July 16, 2004) ("Orion Answer").

[15] *See* NYISO's Motion, Attachment C, Savitt Affidavit ¶ 3.

[16] *See, e.g.,* NRG Answer at 21-22.

can thus confirm that as a result, exclusion of western suppliers would not change the weighted average price figure on which Dr. Savitt's refund calculation is based.

The Answers complain about the proxy periods (first quarters of 2001 through 2004) used by Dr. Savitt to determine a price level for NSR refunds,[17] but do not show that weather or other conditions in the Relevant Period dictate using a particular proxy period. Conversely, the Answers fail to acknowledge that, as Dr. Savitt states in his Affidavit, using a average of the four available winter quarters as a proxy ensures that possibly anomalous conditions during a particular proxy period do not distort the determination of proxy prices.

Keyspan challenges the validity of Dr. Savitt's proxy price calculation because of the implementation after the Relevant Period of lost opportunity cost payments for NSR, along with virtual bidding, automated mitigation, revised procedures for 30 minute reserves, and the modeling of certain load pockets in the dispatch programs.[18] While these features have been added to various NYISO markets, they do not affect Dr. Savitt's NSR calculations. Virtual bidding and automated bidding only apply to energy bids, the product at issue here is 10-minute NSR and not 30 minute reserves, and the modeling of certain load pockets would not change NSR requirements or bidding procedures. Accordingly, the only one of the market changes listed by Keyspan that even ostensibly relates to NSR is the advent of lost opportunity cost (LOC) payments for NSR.

The recognition of LOC for NSR does not, however, undermine the Savitt analysis. Keyspan fails to note that during the Relevant Period, which was of course during the winter, energy prices—which are available to all Market Participants on the NYISO's website—were on

[17] *See, e.g.,* LIPA Answer at 15-16; Keyspan Answer 31-32; and NRG Answer 16-18.

[18] *See* Keyspan Answer at 32.

average only slightly above, or were significantly below, $40/MWh,[19] and thus were well below the costs to provide energy of the combustion turbine units typically providing NSR. If the prevailing prices in the energy market were too low for NSR units to supply energy, then those units would not have any LOC. In addition, NSR prices throughout most of the Relevant Period were above $40/MWh.[20] This plainly indicates that NSR bids during the Relevant Period were not based on opportunity costs, since those costs are by definition limited to the level of energy prices less the energy generation cost of a given unit. Rather, NSR prices during the Relevant Period reflect other strategic bidding objectives. In short, Keyspan does not show that any of its listed market improvements would significantly distort the proxy prices determined by Dr. Savitt, nor does Keyspan propose a superior methodology for determining proxy prices.

Contrary to Orion's assertion, the NYISO's NSR refund proposal does not assume that B-G would have always been bidding and supplying 600 MW of NSR.[21] Dr. Savitt's calculation simply determines what NSR prices have been once B-G was modeled in a way that made all of its capabilities, including NSR, available to the NYISO, and then applies those prices to the NSR MW that were actually supplied during the Relevant Period. The refund would compensate the suppliers of the NSR MW used in the Relevant Period at the lower proxy price determined by Dr. Savitt. B-G as such would not pay or receive any of the refund.

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[19] *See* New York Market Advisor Annual Report on the New York Electric Markets for Calendar Year 2000 (April 2001) ("2000 Market Advisor Report"), at 5 Figure 2 (showing Monthly Average Day-Ahead Prices in New York) (filed with the Commission; *available at* http://potomaceconomics.com/NYISO/2000%20Annual%20Report-Full%20Text.pdf).

[20] *See* NYISO's Motion, Attachments A and B (graphs of NSR prices during the Relevant Period).

[21] Orion Answer at 4, 14.

Orion also asserts that if "Blenheim-Gilboa were bidding and supplying 600 MW into the reserves market, there would be up to 600 MW less energy in the market than there actually was. The NYISO cannot double-count Blenheim-Gilboa's capacity."[22] Orion offers no support for its implicit and implausible assertion that B-G as a pumped storage unit would have been operating at or near its capacity during low demand winter months, and thus would have had to back down energy output in order to supply NSR. Orion also ignores the fact that, as discussed above, the NYISO's refund calculation does not assume that all, or even most, of its NSR requirements would come from B-G. Rather, it turns on the disciplining effect on NSR prices evident from the level of those prices once it was possible for B-G to participate in the NSR market. Finally, Orion's assertion ignores the relatively low energy prices—consistent with winter operations—during the Relevant Period (see above). The prevailing prices in the Relevant Period mean that that the NY energy market would have been operating on the flat part of its supply curve, where even a few hundred MW would not significantly affect market clearing prices.[23]

IV. The NYISO's SR Refund Proposal is Analytically Sound

Mr. Hickey's analysis does not assume a particular level of SR or NSR from B-G, as claimed by Keyspan,[24] or that all of the NYISO's NSR would have come from B-G, as claimed

[22] Orion Answer at 14; *see also* LIPA Answer at 15.

[23] *See* 2000 Market Advisor Report at 7-11, Figure 4 and 7 (showing Supply Curve for Day-Ahead Energy, and stating that: "The supply curve shown in Figure 4 shows that a substantial amount of supply is available at very similar bid prices under most load conditions (i.e., the supply curve is flat). The practical implication of this is that, absent transmission constraints, prices will be relatively insensitive to changes in load or supply, including physical and economic withholding.")

[24] Keyspan Answer at 29

by LIPA.[25] Rather, his analysis is based on the fact that once the software and modeling for B-G was corrected, so that NSR was available from B-G as well as other sources, the NYISO would not have needed to meet its total reserves requirements (including both 10 minute and 30 minute reserves) by taking high-priced SR in excess of the 600 MW SR minimum.[26] The NYISO would not have needed to acquire "all" of its NSR from B-G, but only enough to offset any need for higher-priced SR in excess of 600 MW. On the days when this occurred in the Relevant Period, the NYISO can confirm that the additional purchases did not exceed 112 MW, and were often significantly less. The NYISO can also confirm that Mr. Hickey's analysis examined the B-G energy schedules during the Relevant Period, which was not a peak load period, and determined that at least one unit would have been available to provide NSR during the hours in which the NYISO procured more than 600 MW of SR. One B-G unit would have provided more than enough NSR to offset any excess purchases of SR during the Relevant Period.

It is simply not correct that, as Keyspan asserts, the NYISO proposal "destroys the clearing price method for the NSR and SR products . . . ."[27] To the contrary, the NYISO proposal is based on the use of SR market clearing prices, which it redetermines based on the bids for SR at the level of the 600th MW as received each day during the Relevant Period.[28] To calculate the SR refund on the basis of clearing prices above 600 MW would be to import the NSR Market Design Flaw into correction of the tariff violation remanded to the Commission,

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[25] LIPA Answer at 15.

[26] From time to time, in off-peak hours the NYISO may purchase more than 600 MW of SR, but only because SR is being offered at lower prices than 30 minute reserves, with reserves markets clearing in the range of $0.18.

[27] Keyspan Answer at 31.

[28] NYISO's Motion, Attachment B, Hickey Affidavit ¶¶ 4-6.

since correction of the Market Design Flaw would obviate the need to take more than 600 MW of SR. On these facts, it would be arbitrary to assume that the availability of NSR from B-G would have had no effect on the level of the NYISO's procurement of SR. To the extent the refund calculation pays for any SR schedule above 600 MW at the bid for those MW, as explained in Mr. Hickey's affidavit this ensures that the units that actually supplied SR receive compensation that is at least at the level of their bids.[29]

V. The SR Refund Should Not Exclude LI Units from Setting the Clearing Price

The Answer and Limited Protest of Transmission Owner Intervenors asserts that the setting of SR clearing prices by units on Long Island ("LI") that were dispatched for local reliability was a Market Design Flaw that should now be corrected by a TEP.[30] The Commission's Initial Order, which addressed this issue, did not identify the role of LI units scheduled for local reliability in setting SR clearing prices as a Market Design Flaw.[31] Instead, the Initial Order "accept[ed] the New York ISO's response [on the LI units] as a reasonable approach to this issue . . . ."[32]

Thereafter, the Transmission Owners twice waived their right to assert here that the setting of SR clearing prices by LI units dispatched for local reliability was a market design flaw. First, the rehearing requests of the Transmission Owners did not specify that the setting of SR

[29] *Id.*

[30] *See New York Independent System Operator, Inc.*, Answer and Limited Protest of Transmission Owner Intervenors, Docket Nos. ER00-1969 *et al*., at 7-8 (July 16, 2004) (hereinafter "Transmission Owners' Answer").

[31] *New York Independent System Operator, Inc.*, 91 FERC ¶ 61,218 at 61,807 (2000).

[32] *Id.*

market clearing prices by LI units was an error the Commission needed to address.[33] Instead, their only reference to this issue merely describes the role of LI units in setting SR prices: "Under the NYISO's procedures, bids for operating reserves in this sub-market [Long Island] of the NYCA can and do set the price for all sales of operating reserves in the NYCA."[34] The rehearing request does not characterize this fact as a Market Design Flaw, or explicitly request the Commission to make such a determination. Second, the Commission's determination that the NYISO's treatment of LI units was "reasonable" was not challenged by the Transmission Owners on appeal as an erroneous failure to find a Market Design Flaw. As a result, nowhere in its opinion does the D.C. Circuit hold that the Commission erred in not finding that the setting of SR prices by LI units was a Market Design Flaw.[35]

Under Section 313(b) of the Federal Power Act, "[n]o objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure to do so."[36] In interpreting this same provision under the Natural Gas Act, the D.C. Circuit stated that its purpose is to ensure both that, before the court intervenes, the Commission "has an

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[33] *See New York Independent System Operator, Inc.*, Application for Rehearing of LSE Intervenors, Docket Nos. ER00-1969 *et al*. (June 30, 2000); *and New York Independent System Operator, Inc.*, Request for Rehearing of Rochester Gas and Electric Corporation and Niagara Mohawk Power Corporation, Docket Nos. ER00-1969 *et al*. (June 30, 2000) (This rehearing request incorporated by reference the Application for Rehearing of LSE Intervenors).

[34] *New York Independent System Operator, Inc.*, Application for Rehearing of LSE Intervenors, Docket Nos. ER00-1969 *et al*., at 16 (June 30, 2000).

[35] *See Consolidated Edison Co. v. FERC*, 347 F.3d 964 (D.C. Cir. 2004).

[36] 16 U.S.C. § 825l(b).

opportunity to deal with any difficulties presented by its action" and that the Commission takes "a 'hard look' at the salient problems."[37] The court, however, also found that:

> The agency cannot reasonably be expected to take a hard look unless the parties participate in the task of identifying the hard problems, and of bringing to light pertinent information and analysis bearing on their resolution. The agency's obligation presupposes a burden on the part of interested parties to draw attention to the consequences of proposed action that adversely affects their interests.[38]

The Transmission Owners' decision not to explicitly raise the role of LI units in setting SR clearing prices as a Market Design Flaw in the specification of errors in their rehearing requests,[39] but rather to make a short, factual statement buried among other arguments, does not meet their statutory burden. Moreover, their statement about LI units was made in a section of the Transmission Owners' rehearing request that described purported tariff violations, not Market Design Flaws, and that focused on the quantity requirements for LI reserves. The D.C. Circuit's opinion makes clear that "tariff violation" and "Market Design Flaw" assertions are separate and distinct grounds for review of the Commission's actions in the Operating Reserves orders.[40] Ultimately, the Transmission Owners' failure to include this issue in their arguments to

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[37] *Rhode Island Consumers' Council & Division of Pub. Utils. & Carriers v. FPC*, 504 F.2d 203, 212 (D.C. Cir. 1974) (citations omitted).

[38] *Id.*; *Villages of Chatham & Riverton v. FERC*, 662 F.2d 23, 30 (D.C. Cir. 1981) ("This court . . . has stated that any argument brought clearly to the attention of the Commission by the party's petition for rehearing has been preserved for review in a court of appeals.") (emphasis added), *cited in Consolidated Edison*, 347 F.3d at 973.

[39] *See New York Independent System Operator, Inc.*, Application for Rehearing of LSE Intervenors, Docket Nos. ER00-1969 *et al*., at 4-5 (June 30, 2000); *and New York Independent System Operator, Inc.*, Request for Rehearing of Rochester Gas and Electric Corporation and Niagara Mohawk Power Corporation, Docket Nos. ER00-1969 *et al*., at 2 (June 30, 2000).

[40] *See Consolidated Edison*, 347 F.3d at 974 (holding that the LSE's claim that a tariff violation arose from the NYISO's refusal to accept bids of cheaper reserves from western suppliers of operating reserves was waived because the LSE's did not adequately raise the issue as a tariff violation, but rather as a market design flaw).

the D.C. Circuit, and the resulting lack of any holding by the D.C. Circuit that the Commission erred in its treatment of the SR pricing role of LI units, leaves standing the Commission's determination in its Initial Order. Any assertion that the role of LI units in SR pricing was a Market Design Flaw has been waived and cannot be asserted on this remand.

VI. The Commission Should not Order Refunds Predicated on Operating Reserves from Western Suppliers

The Transmission Owners claim that the NYISO should "recogniz[e] operating reserves from western suppliers in its refund methodology and calculation."[41] As shown in the NYISO's Motion, obtaining operating reserves only from eastern suppliers was not a Market Design Flaw,[42] but an element of the New York market design, because "the optimal mix of resources supplying energy and operating reserves favored the use of Central-East for energy rather than reserves."[43]

The Transmission Owners do not controvert the support for this conclusion in the NYISO's Motion, but rather claim that "both the Commission and the Court, in fact, found that the NYISO's failure to accept bids from western suppliers was a Market Design Flaw."[44] In support of this assertion the Transmission Owners include a lengthy quote from the D.C. Circuit's opinion, but this quote acknowledges the NYISO's contention that "the nature of NYISO's market design prevented it from accepting bids from western suppliers."[45] As shown in

[41] Transmission Owners' Answer at 10.

[42] NYISO's Motion at 10-13.

[43] NYISO's Motion at 13.

[44] Transmission Owners Answer at 9.

[45] *Id*.; *Consolidated Edison*, 347 F.3d at 971-72.

the NYISO's Motion, a range of "operational, reliability and other practical considerations make it clear that limitations on the use of operating reserves from western suppliers was part of the New York market design, and not a Market Design Flaw."[46] Moreover, the Commission's orders did not find conclusively that operating reserves should have been obtained from western suppliers. The Initial Order only stated that "it is not clear why the NYISO should not be able to rely on western suppliers when there is no congestion present."[47] Similarly, the First Rehearing Order found that the NYISO's September 1, 2000, Compliance Filing and Report "showed that there was no immediate solution that would allow transmission capacity across the Central-East constraint to be used to move western operating reserves to the east."[48] Thus, there is nothing in the prior proceedings that precludes the Commission from making a determination now on the underlying question of a Market Design Flaw. The NYISO's Motion makes clear why the NYISO did not rely on western supplies of operating reserves during the Relevant Period, and why this was the appropriate choice during the Relevant Period for the NYISO markets.

Equally important, the Transmission Owners do not provide any basis for making refund calculations based on an assumption that operating reserves could have been obtained from western suppliers. They fail to show that reserves from western suppliers would have met reliability requirements. They also fail to show that the NYISO improperly ignored bids to supply reserves from any qualified western supplier. Absent such showings, there is no rationale for calculating lower Operating Reserves prices during the Relevant Period on the basis of using western suppliers.

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[46] NYISO's Motion at 12.

[47] Initial Order at 61,799-80.

[48] First Rehearing Order at 61,677.

VII. Keyspan's Request for an Evidentiary Hearing, Including Discovery Procedures, Should be Denied

No trial-type evidentiary hearing is necessary in this proceeding because the material issues of fact were resolved in the prior proceedings in these dockets, and the NYISO's Motion raises no disputable issues of fact.[49] The calculations in the Hickey and Savitt affidavits are built on, respectively, the SR bids submitted during the Relevant Period, and the prices for NSR during the winter proxy periods. In both instances, this is data derived directly from the NYISO's databases, and would not be elucidated by cross-examination or other evidentiary procedures. It is what it is. The issue properly before the Commission in this remand is the appropriate methodology for calculating refunds, and the SR and NSR refund methodologies proposed by the NYISO are fully described in the Hickey and Savitt affidavits. Both Mr. Hickey and Dr. Savitt explained the straight-forward mathematical calculations they performed on the bid or price data to determine the SR and NSR refund amounts. Both included exhibits demonstrating the derivation of the refund amounts. Contrary to NRG's suggestion that Mr. Hickey's affidavit is "wholly insufficient" because it provides only two hours of data,[50] the two hours of data presented in Mr. Hickey's affidavit exemplify the determinations that were made

[49] *See Transwestern Pipeline Co.*, 72 FERC ¶ 61,085 at 61,452, 61,457-58, 61,460-61, 61,463-64 (1995) (finding that: "An evidentiary trial-type hearing is necessary only where material issues of fact are in dispute that cannot be resolved on the basis of the written record. . . . By accepting the pleadings discussed above, the Commission has achieved a complete record and given all parties an adequate opportunity to be heard") (citations omitted); *and Texas Gas Transmission Corp.*, 70 FERC ¶ 61,108 at 61,287 (1995) (denying a request for an evidentiary hearing, finding that "there are no material issues of fact in dispute which require holding such a[n evidentiary] hearing in this proceeding, since all material issues are capable of being resolved on the basis of the existing record").

[50] *See* NRG Answer at 25.

on exactly the same basis in every other hour.[51] As far as the underlying methodology goes, including more hours would just be showing more of the same. The discovery and evidentiary hearing requested by Keyspan would therefore serve no useful purpose, and would only result in unnecessary delay. Keyspan's request should thus be denied.[52]

VIII. Refunds Are Equitable and Appropriate Under the Circumstances of this Proceeding

The NYISO and the Answering Parties appear to agree that the Commission has broad remedial power to order refunds.[53] All the parties recognize that in determining whether refunds are appropriate, the courts have held that the Commission must "explore and give due weight to considerations of equity,"[54] and that the court has also held that "[c]ustomer refunds are a form of equitable relief, akin to restitution," and therefore are appropriate when "'money was obtained in such circumstances that the possessor will give offense to equity and good conscience if permitted to retain it.'"[55]

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[51] NYISO's Motion, Attachment B, Hickey Affidavit ¶ 9 ("Exhibit A uses two selected hours to demonstrate the determination of the proxy, hourly market clearing price when the Long Island constraint was binding, and when the Long Island constraint was not binding.").

[52] Keyspan Answer; *see also* LIPA Answer; *New York Independent System Operator, Inc.*, Motion to Intervene and Answer of Indeck Energy Services, Inc., Indeck-Olean, L.P., Indeck Oswego, L.P., and Indeck-Yerkes, L.P., Docket Nos. ER00-1969 *et al*. (July 16, 2004).

[53] *See Towns of Concord, Norwood, & Wellseley v. FERC*, 955 F.2d 67, 73 (D.C. Cir. 1992) ("The Federal Power Act does not explicitly deprive the Commission of remedial discretion with respect to refunds; in fact the Act quite clearly confers it.").

[54] *Gillring Oil Co. v. FERC*, 566 F.2d 1323, 1325-26 (5th Cir. 1978), *cert. denied*, 439 U.S. 823 (1978); *Koch Gateway Pipeline Co. v. FERC*, 136 F.3d 810, 816 (D.C. Cir. 1998) (explaining that the Commission must "establish that its decision represents a 'reasonable accommodation of the relevant factors' and the refund is 'equitable in the circumstances'") (citation omitted).

[55] *Concord*, 955 F.2d at 75 (quoting *Atlantic Coast R.R. v. Florida*, 295 U.S. 301, 309 (1935)).

Answering Parties Orion, LIPA and Keyspan assert that they should not be subject to refunds under this standard, but can do so only by ignoring the key findings of both the Commission and the D.C. Circuit about NSR and SR pricing during the Relevant Period.[56] The generators will not be "punished" for tariff violations that they assertedly were not responsible for. Rather, they would be required to disgorge the windfall returns they were able to realize from the non-competitive NSR market during the Relevant Period, and from SR prices that the D.C. Circuit found were set at higher levels than permitted by the tariff. As the D.C. Circuit has held, while the Commission has "considerable discretion in fashioning remedies," a decision not to order refunds would be inequitable when windfall profits result from the collection of an unjustified rate.[57] The Commission has recognized the particular importance of this principle in situations in which ostensibly competitive market-clearing prices did not in fact result from a workably competitive market, holding that

> it is fair that all those who benefit[] from [the] market also bear responsibility for remedying any potential unlawful transactions that might have occurred in the market. Consequently, if the price for a specific sale is found to be unjust and unreasonable, then all sellers who obtained that price received an unjust and unreasonable rate. To the extent the Commission determines refunds are an appropriate remedy for that sale, consumers can only be made whole by refunds from all sellers who received the excessive price.[58]

Here, the D.C. Circuit determined that Commission had "found that NYISO had 'presented sufficient evidence to call into question continued reliance on market-based pricing

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[56] Orion Answer at 8-9; LIPA Answer at 12-14; Keyspan Answer at 22-28.

[57] *P.U.C. of California v. FERC*, 143 F.3d 610, 617-18 (D.C. Cir. 1998).

[58] *Enron Power Marketing, Inc. & Enron Energy Servs. Inc.*, 103 FERC ¶ 61,346 at P 14 (2003).

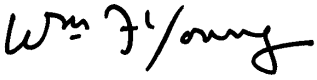
for non-spinning reserves.'"[59] The Commission accordingly approved a prospective bid cap on NSR, a decision that was not challenged by any party on appeal.[60] The evidence on which the Commission acted in approving the bid cap, however, was that NSR prices were not the result of a workably competitive market during the Relevant Period. Thus, that same evidence shows that certain generators earned unjustifiably high returns from sales of NSR during the Relevant Period. The evidence also shows that certain generators received SR prices that benefited from a floor NSR price that the Court held was not authorized by the tariff. Since the record in this proceeding therefore shows that the generators received unjust and unreasonable NSR and SR rates during the Relevant Period because the rates were not the result of a workably competitive market, or were not the result of the market design or tariff previously approved by FERC, refunds are appropriate to bring NSR and SR rates during the Relevant Period to just and reasonable levels.

[59] *Consolidated Edison Co.*, 347 F.3d at 968 (quoting Initial Order at 61,798).

[60] *Id.* at 966 (holding that the issue before the court was "what remedies, particularly monetary ones with retroactive effect, are available for electric service providers and ultimately electric consumers who experience substantial price increases when a deregulated energy market fails to operate properly.").

Respectfully submitted,

NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.



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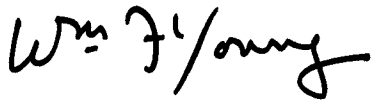
CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service lists compiled by the Secretary in these proceedings in accordance with the requirements of Rule 2010 of the Rules of Practice and Procedure, 18 C.F.R. § 385.2010 (2003).

Dated at Washington, DC this 2nd day of August, 2004.



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