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June 24, 2004

VIA HAND DELIVERY

Mr. John W. Boston
Chairman of the Board
c/o Mr. William J. Museler
President and Chief Executive Officer
New York Independent System Operator, Inc.
3890 Carman Road
Schenectady, New York 12303

Re: Appeal of Management Committee Decision Concerning
Rate Schedule 1 Cost Allocations
Motion In Opposition

Dear Chairman Boston:

Pursuant to the New York Independent System Operator, Inc.'s ("NYISO") "Procedural Rules for Appeals to the ISO Board," AES-NY, LLC, Mirant Corporation, Reliant Energy, Inc. and Sithe Energies, Inc. (collectively, "Movants") hereby file this motion in opposition to the June 17, 2004 Appeal filed by Entergy Nuclear Indian Point 2, LLC, Entergy Nuclear Indian Point 3, LLC and Entergy Nuclear Fitzpatrick, LLC ("Entergy") and the June 18, 2004 Appeal filed by some New York municipal electric utilities ("NY Municipals") (collectively, "Appeals"). The Appeals concern the Management Committee's decision, by a 87.63% vote, to revise the cost allocations that currently are applied to the NYISO operating budget component of Rate Schedule 1.

MOTION IN OPPOSITION TO MUNICIPAL APPEAL AND ENTERGY APPEAL

Pursuant to the New York Independent System Operator, Inc.'s ("NYISO") "Procedural Rules for Appeals to the ISO Board," AES-NY, LLC, Mirant Corporation, Reliant Energy, Inc. and Sithe Energies, Inc. (collectively, "Movants") hereby file this Motion In Opposition to the June 17, 2004 Appeal filed by Entergy Nuclear Indian Point 2, LLC, Entergy Nuclear Indian Point 3, LLC and Entergy Nuclear Fitzpatrick, LLC ("Entergy") and the June 18, 2004 Appeal filed by some of the New York municipal electric utilities who are members of the Management Committee ("NY Municipals") (individually, "Entergy Appeal" and "Municipal Appeal" and, collectively "Appeals"). At its June 4, 2004 meeting, the NYISO Management Committee determined that a straight percentage cost allocation approach should continue to be used to allocate the NYISO operating budget component of Rate Schedule 1 between loads and suppliers but that the percentage should be adjusted, effective beginning January 1, 2005, from the currently applicable levels of 85% load and 15% supply to 80% load and 20% supply ("RS 1 Cost Allocations"). The NYISO Management Committee further determined that the RS 1 Cost Allocations should remain in place for a minimum of five years.

In their Appeals, Entergy and the NY Municipals each seek to overturn the Management Committee's June 4, 2004 motion approving the RS 1 Cost Allocations ("RS 1 Motion"). Specifically, Entergy and the NY Municipals argue that entities that are parties to bilateral contracts should be assigned lower cost allocations.[1] In addition, the NY

[1] Upon information and belief, both Entergy and the NY Municipals are parties to bilateral contracts.

Municipals alone challenge the Management Committee's decision to maintain the RS 1 Cost Allocations for a period of at least five years.

During numerous, widely attended meetings held over a six-month period, the Budget, Standards and Performance Subcommittee ("BSP Subcommittee"), with the aid of an independent consultant retained by the NYISO, RJ Rudden Associates ("Rudden"), identified and reviewed a number of potential Rate Schedule 1 cost allocation changes, including the unbundled, bilateral contract exemption approach proposed by Entergy and the NY Municipals. After extensive review and consideration, the BSP Subcommittee recommended the RS 1 Cost Allocations to be applied for a minimum of five years. This recommendation, endorsed by both Rudden and the NYISO Staff, garnered an 87.63% Management Committee vote.

The Appeals should be denied on the grounds that the Management Committee acted reasonably in continuing to base the RS 1 Cost Allocations upon a straight percentage cost allocation approach and in approving this mechanism for a minimum of five years. Thus, the NYISO Board should issue a decision upholding the RS 1 Motion and should direct its Staff to submit a tariff filing to the Federal Energy Regulatory Commission ("FERC") under Federal Power Act ("FPA") Section 205 to implement the RS 1 Cost Allocations to be effective beginning January 1, 2005 for a minimum five-year period.

I. THE MANAGEMENT COMMITTEE ACTED REASONABLY IN RETAINING A STRAIGHT PERCENTAGE COST ALLOCATION APPROACH

Citing to a series of FERC orders issued in 1999, 2000 and 2001, the NY Municipals allege in their Appeal that the Management Committee's decision to adopt the

RS 1 Cost Allocations was contrary to FERC directives. (See Municipal Appeal at 2-3.) The NY Municipals further allege that the Management Committee's decision to continue to base the RS 1 Cost Allocations upon a straight percentage cost allocation approach contravened the intent of the December 2002 Business Issues Committee ("BIC") motion that led to the completion of the Rudden study. (Id. at 3.) By acting at its June 4, 2004 meeting, Entergy asserts that the Management Committee "discontinued efforts to develop an unbundled Rate Schedule 1 charge" and, as a result, erroneously and disproportionately allocated costs to parties that have bilateral contracts. (See Entergy Appeal at 1-2.) Entergy further asserts that a similar "bilateral bias issue" previously was addressed by the NYISO. (Id. at 3.) However, these claims are belied by orders issued by FERC, the terms of the December, 2002 BIC motion, Rudden's findings concerning the unbundling issues and the extensive review conducted by the BSP Subcommittee. Accordingly, the Management Committee's decision to retain a straight percentage cost allocation approach should be upheld.

A. The Management Committee's Decision Is Not Contrary to Prior FERC Decisions

On May 31, 2002, the NYISO submitted a tariff filing under FPA Section 205 in Docket No. ER02-1961-000, New York Independent System Operator, Inc. ("RS 1 Docket"), to implement the currently applicable straight percentage cost allocation approach, which is assigned 85% to loads and 15% to suppliers ("NYISO RS 1 Filing").[2] On June 21,

[2] See FERC Docket No. ER02-1961-000, New York Independent System Operator, Inc., Recovery of Charges Assessed Under Rate Schedule 1 of Its Open-Access Transmission Tariff and Market Administration and Control Area Services Tariff (dated May 31, 2002).

2002, the Municipal Electric Utilities Association of New York State ("MEUA")[3] submitted a Motion To Intervene and Protest to the NYISO RS 1 Filing[4] in which it, inter alia, relied upon the same string of FERC decisions as set forth in the Municipal Appeal, sought consolidation of dockets and made the same argument to oppose that filing – namely, that the NYISO RS 1 Filing failed to implement a structure that separated transmission-related functions from the energy market functions and allocate costs accordingly. (See MEUA Protest at 2-4.)

In its Order issued on September 25, 2002 in the RS 1 Docket,[5] the FERC rejected MEUA's proposal to consolidate that proceeding with the 1999 proceedings, holding, "We further reject MEUA's contention that these proceedings should be consolidated…As MEUA states, that proceeding addresses issues related to separation of NYISO's transmission costs from its costs for non-transmission services, rather than the allocation among market participants of NYISO's fixed budget for operating costs involved here." (See RS 1 Order at 5.) MEUA neither sought rehearing nor clarification of the RS 1 Order.

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[3] Upon information and belief, the three municipal utilities that filed the Municipal Appeal are members of MEUA.

[4] See FERC Docket No. ER02-1961-000, supra, "Motion To Intervene and Protest of the Municipal Electric Utilities Association of New York State" (dated June 21, 2002) ("MEUA Protest").

[5] See FERC Docket No. ER02-1961-000, supra, "Order on Revised Tariff Sheets," 100 FERC 61,315 (2002) ("RS 1 Order").

B. The Management Committee's Decision Is Consistent With the December, 2002 BIC Motion

The NY Municipals' claim concerning the alleged failure to satisfy the intent of the December, 2002 BIC motion is equally unavailing. The Management Committee motion that led to the NYISO RS 1 Filing included a provision requiring a working group to be appointed to determine whether an alternative allocation should be considered.[6] In its RS 1 Order, the FERC pointed to this aspect of the Management Committee motion and encouraged the NYISO to complete its examination of whether the 85 load/15 supply split was an appropriate long-term allocation. (See RS 1 Order at 4-5.) This, in turn, led to the December, 2002 BIC motion.

As the NY Municipals themselves acknowledge in their Appeal, the December, 2002 BIC motion requested that the NYISO Staff, or a retained outside consulting firm, identify the NYISO customers that use or benefit from specific Rate Schedule 1 functions "to assess if Rate Schedule 1 should be allocated to NYISO customers by component or grouping of components (i.e., similar to PJM methodology) according to the benefits received." (See December, 2002 BIC motion at 1; emphasis supplied.) However, the NY Municipals then make the quantum leap in their Appeal that the Management Committee's failure to adopt an unbundled approach was contrary to "the intent of the motion requesting the Rudden study." (See Municipal Appeal at 3.)

In so doing, the NY Municipals effectively presume what the outcome of the Rudden study should have been -- an outcome that, as demonstrated below, ultimately was

[6] See NYISO Management Committee, December 5, 2001 Meeting Minutes and Summary of Motions, Motion #2.

not justified by the findings of the Rudden study itself. While the NY Municipals may have business reasons to dislike the end result, the Rudden study did, in fact, consider and address the issue identified by the BIC in its December 2002 motion. Upon a full review, the answer was no.

C. The BSP Subcommittee Gave Extensive Consideration To The Issues Specific To Bilateral Contracts

Nor are claims that the BSP Subcommittee failed to adequately address the issues specific to bilateral contracts compelling. The BSP Subcommittee held two meetings beginning in December, 2003 to provide Rudden representatives with input to conduct its study. On March 19, 2004 and, again, on April 16, 2004, the BSP Subcommittee met to review Rudden's preliminary findings. In these early meetings, Rudden initially proposed to treat parties that held bilateral contracts differently than parties that participated in the NYISO's spot market.

However, the discussions that ensued during those meetings demonstrated that the Rudden representatives were unaware that bilateral transactions must be scheduled through the NYISO market and the NYISO must utilize its personnel and software systems, including its scheduling and billing functions, to accommodate both parties with bilateral contracts as well as parties with spot market transactions. Moreover, a number of parties raised concerns that providing any exemption to parties with bilateral contracts would force parties to move from currently existing financial contract for differences arrangements to physical bilateral contract arrangements. This, in turn, adversely would affect NYISO operations. In addition, timing, NYISO resource allocation, software, cost and implementation concerns also were raised. Based upon this input, as evidenced from the lists attached hereto, Rudden took action items during these two meetings to further consider these issues.

Following extensive discussion and consideration of the bilateral contract issues and unbundling issues, Rudden recommended to the BIC and, subsequently, to the Management Committee to continue to use the straight percentage cost allocation approach applicable to all parties.[7] The NYISO Staff concurred. It was upon this extensive record that the Management Committee approved the RS 1 Cost Allocations by a vote of 87.63% with support coming from all five sectors. Thus, the NY Municipals and Entergy's claims notwithstanding, the bilateral contract issues were fully considered and ultimately were rejected by the Management Committee.

D. The NYISO's Tariff Provisions Concerning Its Credit Policy Do Not Compel Reversing the Management Committee's Decision

In its Appeal, Entergy argues that the NYISO previously has recognized that parties to bilateral contracts should be exempt from the bad debt loss and working capital aspects of the NYISO credit policy because they cover their own credit risks, and therefore, this same approach should be carried over for purposes of the allocation of the NYISO's operating budget. (See Entergy Appeal at 3.) However, Entergy's reliance on the NYISO's action concerning its credit policy is also without merit.

[7] As established by Rudden in its presentations to both the BIC and the Management Committee, its recommendation to retain the straight percentage cost allocation approach "results in an identical cost allocation to MP groups as the unbundled rates." See RJ Rudden Associates, "Schedule 1 Evaluation Project Business Issues Committee Presentation" (dated May 19, 2004) at 19; see also RJ Rudden Associates, "Schedule 1 Evaluation Project" (dated June 4, 2004) at 19.

In addressing an appeal to the Management Committee's decision approving the NYISO's credit policy,[8] the NYISO Board stated that it had spent much time considering the assertion that a bilateral contract exemption would cause Market Participants to shift from financially-based contract-for-differences arrangements to physical bilateral transactions in order to avoid absorbing bad debt losses. (See NYISO Board Decision at 4.) At that time, the NYISO Board found that the concern was based on the assumption that Market Participants would react to the fear alone of potentially incurring an unquantifiable bad debt loss at some unknown time in the future. (Id.) Thus, the NYISO Board declined to reverse the Management Committee's decision to include the bilateral contract exemption on the grounds that the concerns raised under those circumstances were "largely theoretical." (Id.)

Such is clearly not the case in this instance. If approved by FERC, the RS 1 Cost Allocations will be applied to Market Participants immediately upon the effective date, proposed to be January 1, 2005. Thus, there is nothing theoretical about whether, and the degree to which, these charges would be incurred.

II. THE MANAGEMENT COMMITTEE APPROPRIATELY APPROVED AN EFFECTIVE PERIOD FOR THE RS 1 COST ALLOCATIONS OF AT LEAST FIVE YEARS

The RS 1 Motion expressly provides that the proposed allocation between loads and suppliers shall remain in place for at least the next five years to be reviewed at the end of the fourth year only if "significant market changes merit its review." (See RS 1

[8] See NYISO Board of Directors, "NYISO Board of Directors Decision on Working Capital and Bad Debt Losses Allocation Appeal" (dated June 17, 2003) ("NYISO Board Decision").

Motion at 2.) Only the NY Municipals challenge this provision. However, as demonstrated, infra, this aspect of the NY Municipals' appeal also is without merit, and therefore, it, too, should be denied.

During the discussions that took place at the BSP Subcommittee meetings, many parties from different sectors emphasized the need to set a known Rate Schedule 1 cost allocation structure for a defined period of time to eliminate uncertainty and foster longer term forward contracting in New York. As evidenced by the RS 1 Motion, based on its analysis, inter alia, of the Rudden Study and the New York markets, the BSP Subcommittee reached consensus that a minimum of a five-year period was needed. This aspect of the RS 1 Motion was a critical component that led Movants to either support or register an abstention on it.

Indeed, eliminating this aspect of the RS 1 Motion substantially would undercut the significant efforts that have been undertaken by Market Participants to date to better quantify their Rate Schedule 1 exposure. At its July 24, 2003 meeting, the Management Committee unanimously approved Budget Development and Project Monitoring Guidelines developed by the BSP Subcommittee ("Budget Guidelines") by a show of hands with only 4 abstentions.[9] While prior to this motion the budget information provided to Market Participants on an annual basis had been limited to a detailed budget for the next year, the Budget Guidelines now require the NYISO to couple this information with a 5-year budget target to allow Market Participants to better define their cost exposure going

[9] See NYISO Management Committee July 24, 2003 Meeting Minutes and Summary of Motions, Motion #1.

forward. The NYISO Management Committee discussed and acted on its first budget target motion at its November 12, 2003 meeting.

Acting through these two motions, the Management Committee has ensured that critical information will be provided to the market that will bolster the ability of parties to enter into longer term contracts. Stripping away the defined cost allocation structure for a known period significantly would limit the value of the budget target information. Thus, the Management Committee's decision to implement a minimum five-year term for the RS 1 Cost Allocations also should be upheld.

VI. CONCLUSION

For the foregoing reasons, Movants respectfully request that the NYISO Board issue a decision denying the Municipal Appeal and the Entergy Appeal and submit a tariff filing to the FERC under FPA Section 205 effectuating the Management Committee's decision.

Dated: June 24, 2004
Albany, New York

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Should any party request oral argument or the Governance Committee elect to schedule oral argument on its own motion, Movants hereby request the opportunity to be heard. Movants respectfully request that the NYISO post this document on its website and serve a copy via e-mail to all members of the Management Committee. Thank you for your courtesies in this regard.

Very truly yours,

COUCH WHITE, LLP

Doreen Unis Saia
Counsel for the Movants

DUS/ama
Enclosure
cc: Robert Fernandez, Esq. (via hand delivery & e-mail; w/encl.)
Mr. Charles King (via hand delivery & e-mail; w/encl.)
Ms. Kristen Kranz (via hand delivery & e-mail; w/encl.)

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RJ Rudden

BSP Subcommittee
Schedule 1 Evaluation Project Status Report
Action Items from 3/19/04 Meeting

The following items provide a summary of the requests made by BSP Subcommittee members during the 3/19/04 presentation on the status of the Schedule 1 Evaluation project. Rudden consultants intend to evaluate each request and provide a response at the next scheduled BSP meeting.

1. Compare the Rudden recommendations for assigning activities to the Service Categories, with the assignments for similar activities used in the prior NYISO study that lead to the existing rate design allocating 85% of the costs to load and 15% to supply. In particular, analyze the causes for the change in the overall effect from 85/15 to 70/30.

2. Compare the overall effect of the Rudden recommendations for Schedule 1 on Load vs. Supply, to the other ISOs.

3. Consider the allocation of some of the departments in the Management Services Type 1 costs (e.g. the Human Resources Department) based on labor dollars versus total dollars.

4. Review the possibility of moving external legal services, auditing and market monitoring to Management Services Type 2. Consider whether the full Management Services Type 2 category should be allocated 50% to load and 50% to supply.

5. Provide a list of "A" Projects, and a list of billing projects, and how they were allocated in the Rudden recommendations.

6. Review the reasoning and potential market impacts resulting from the recommendation to exclude bilateral contracts, and to include the virtual load and virtual supply, in recovering costs for the Energy and Ancillary Services Markets Service Category.

7. The NYISO Vice Presidents should review Rudden's recommendations for the Schedule 1 allocations, in particular the impact of the recommendations for bilaterals and virtual trading.

8. Review the possibility of using MW to allocate the System Reliability Service Category rather than MWh.

9. Review the recommendations for a) collecting Capacity Market Service Category costs through a surcharge on the ICAP market transactions, b) excluding Spot Auction Excess Transactions and c) excluding self-supplied ICAP from the charges.

10. Review the proposed treatment of combining the Transmission Congestion Contracts (TCC) Market with the Real Time Operations Service Category. Consider combining the TCC Services Category with Energy and Ancillary Services Markets Service Category, reflecting the view that these contracts provide financial hedges for transactions in the energy markets. In addition, consider the possibility that the TCC costs may grow with the potential influx of merchant generation, and the impact this would have on the proposed rate design.

11. In the analysis of present charges, correct the treatment of the FERC fees to reflect the allocation method used in the existing rate design. Consider an alternative allocation that reflects the view that FERC activities govern, and the FERC fee is caused by and benefits, both load and supply.

12. Develop a recommendation on how to treat the actual net costs, after any financing, versus the gross costs, prior to financing, that are currently used in the analysis.

RJ·Rudden ASSOCIATES

BSP Subcommittee
Schedule 1 Evaluation Project Status Report
Action Items from 4/16/04 Meeting

The following items provide a summary of the requests made by the BSP Subcommittee members during the 4/16/04 presentation on the status of the Schedule 1 Evaluation project. Rudden consultants intend to evaluate each request and provide a response at the next scheduled BSP meeting.

Rudden Action Items

1. Prepare a comparison of the service categories presented in the old NYISO study that was used as the basis for the current 85/15 split. Show the relative percentages in each category and discuss the changes and the reasons for the split. Include a review of the current recommendation to allocate 100% of the market monitoring costs to supply and why this changed from the prior study.

2. Create a third customer category for Transmission Owners (TO) and determine how much of the costs should be allocated to the TOs.

3. Perform further evaluation of the currently proposed exclusion of the bilaterals from the EASM billing units, particularly the potential of the increased costs driving Market Participants (MPs) to the bilateral markets and discouraging participation in the NYISO market.

4. Perform further evaluation of the currently proposed exclusion of the self-supply from the Capacity Markets Services category billing units.

5. Review the requirements of SMD and how it affects:

    a. The 50/50 split of SMD costs between the Real-Time Operations and Energy and Ancillary Services Markets (EASM) service categories, and
    b. The split of EASM portion of the costs 60% to Load and 40% to Supply.

6. Present a more typical amount of Capacity Markets costs by eliminating the cost of ICAP auction automation projects.

7. Apply the $45 million net new financing to reduce SMD project costs and other project costs, instead of to reduce rates proportionately across the board.

8. Create a one-page summary of the current recommendations.

9. Deliver a draft recommendation to Mary McGarvey by April 23, 2004 for review by David Patton. The draft may not have addressed each of the items above but will include a list of issues still under review.

NYISO & Rudden Action items

10. Research the available data on the New York Power Pool (NYPP) costs. Based on the data availability, NYISO will determine whether Rudden should evaluate and compare the NYPP costs to the proposed NYISO cost allocations.

11. Review the currently proposed allocations of the Capacity and TCC market costs with the applicable NYISO personnel.

12. Estimate the NYISO IT costs and needed timeframe associated with modifying the current 85/15 percentage allocations with all other billing processes remaining unchanged.

13. The NYISO legal group will determine the tariff issues associated with Rudden's proposed treatment of eliminating the bilaterals from the Energy & Ancillary Services (EASM) billing units (presented in item 4, Section III of the 4/16/04 Project Status Report to the BSP).

14. The NYISO legal group will identify which NYISO presentations that FERC relied on for its September 25, 2002 Order approving the 85/15 split.

15. NYISO will evaluate and recommend an approach to address the debt repayment for prior year debt that was incurred with the current 85/15 allocations.