In-City Capacity Rules Applicable to Divested Generation Owners

Agenda #6

Issues Related to ISO/Keyspan Proposal to

- Eliminate the Bilateral Prohibition
- Apply the $105 Revenue Cap Annually

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1-09-03 MC Meeting

Bilateral Prohibition

Mitigated capacity must be sold into ISO Auctions

- Ensures that revenue caps are not circumvented
  - If capacity prices exceed revenue cap, DGOs would have a financial incentive to package mitigated capacity sales with above market energy sales.
- Precludes preferential sales to retail affiliates
  - Sales of mitigated capacity to retail affiliates of DGOs would give them a competitive advantage over other in-City LSEs
  - DGOs could circumvent the revenue cap by selling a retail contract with the capacity component priced at non-mitigated levels.

Application of the $105 Revenue Cap

Problems Applying Annual Cap in a Monthly Market:

- Discourages in-City capacity hedges
  - "Uplift" from true-ups payments to DGOs undermines effectiveness of hedges (e.g. bilateral contracts with non-mitigated units or CFDs with mitigated units)
- Creates financial uncertainty for LSEs
  - Would not know actual capacity costs until year-end
- Is complex to administer and somewhat arbitrary
  - ISO conducts up to 8 different auctions for the same calendar month of supply
  - DGO settlement would depend on their individual auction strategies.
- Creates new and potentially inefficient incentives for DGOs
  - Past under-collection creates financial incentives to withold capacity
  - Past over-collection reduces incentives to maximize future revenues