

refraining from exercising its TEP authority to recalculate prices for a brief period in 2000 in connection with the exclusion of the Blenheim-Gilboa pumped storage facility and western suppliers in the reserves market. Additionally, we found that NYISO did not violate its tariff by modeling the Blenheim-Gilboa plant so that the output of that plant could not be offered into the reserves markets. We also found that NYISO's tariff violation with regard to the prices of spinning and non spinning reserves did not warrant price recalculation and refunds.

2. This case arises from price increases for non-spinning reserve (NSR) in the NYISO-administered operating reserves markets during the period from January 29 to March 27, 2000 (Relevant Period).² In administering the operating reserves markets, NYISO accepts offers from suppliers to procure reserves for the region. The highest-priced bid that NYISO accepts for spinning reserve (SR) and for NSR sets the clearing price that will be paid to all suppliers of each service. SR and NSR differ from each other in that SR can be synchronized to the system and be made almost immediately available to the system, while NSR is not available to the system as quickly. For this reason, SR is a more valuable product than NSR.

3. This order affirms the findings made in the March 4, 2005 Order. The Commission finds that, based on the TEP tariff provisions, NYISO did not act unreasonably in not invoking TEP in these circumstances. Neither the exclusion of the western suppliers nor the failure to dispatch Blenheim-Gilboa were market design flaws under TEP, since there were reasonable bases for NYISO's failure to include these generators in the reserve markets, and neither meets the TEP standard of "reasonable certainty" to qualify for retroactive rate adjustments.

4. With respect to the claim that the NYISO violated its tariff in the manner in which it dispatched NSR and SR, the Commission reaffirms its finding that refunds are not warranted for this technical tariff violation because the end result of the NYISO's actions was not unjust, unreasonable, or unreasonably discriminatory, its actions were consistent with the least cost pricing model of the NYISO's tariff that maintains system reliability, and its pricing of reserves was not the cause of the alleged market manipulation or market power. Similarly, the Commission finds no violation of the NYISO's tariff in its failure to model the Blenheim-Gilboa unit for NSR reserves, since the tariff permitted, but did not require, the unit to be modeled for reserves, and NYISO's modeling was consistent with the unit owner's instructions to model the unit to provide energy, not reserves.

² Under NYISO's Market Administration and Control Area Services Tariff (Tariff), NYISO maintains markets for different types of operating reserves.

I. Background

5. Before NYISO began operation, it filed an amendment to its open access tariff to include its TEP provision.³ The purpose of TEP is to enable NYISO to address unanticipated market design flaws and transitional abnormalities. The TEP provided that, in the event of a NYISO declaration of a market design flaw that would impair reliability or market prices, NYISO could take Extraordinary Corrective Actions (ECAs). ECAs include recalculating clearing prices to the level that would have been reached absent the market design flaw.⁴

6. This proceeding arose shortly after NYISO began operations. During the Relevant Period, prices spiked from averages of \$1.04 per megawatt hour (MWH) in December 1999 to an average of \$65.57 in February 2000, with a high of \$302 that month. Also at that time, the quantity of NSR that suppliers offered into the market decreased. Prior to January 29, 2000, an average of more than 1,400 megawatts (MW) was offered into the NSR market. On January 29 the quantity of NSR being offered dropped below 900 MW, and remained below the prior average levels for February and March.⁵

7. On March 27, 2000, NYISO made a filing with the Commission in which it proposed to address the NSR price spike. Also with regard to the NSR prices, the New York Transmission Owners (NYTOs) filed complaints with the Commission.⁶ The NYTOs requested that the Commission require NYISO to invoke its TEP authority to provide retroactive relief for increases in operating reserve prices for the Relevant Period by recalculating prices. The NYTOs argued that NYISO's market design was flawed because it excluded suppliers on the western side of an east-west constraint, and the output of the Blenheim-Gilboa pumped storage facility, from bidding into the reserves market. The NYTOs also requested that the Commission find that NYISO

³ *New York Independent System Operator, Inc.*, 88 FERC ¶ 61,228 (1999).

⁴ NYISO Tariff, Attachment E, at section C.

⁵ NYISO Request for Suspension of Market-Based Pricing for 10-Minute Reserve, March 27, 2000, at 6-7 (NYISO March 27 filing).

⁶ The NYTOs are Consolidated Edison Company of New York, Inc., Orange and Rockland Utilities, Inc., New York State Electric & Gas Corporation, Rochester Gas and Electric Corporation, and Niagara Mohawk Power Corporation. We note that in their complaints the NYTOs collectively refer to themselves as Load Serving Entities.

violated its Tariff in two ways: (1) by improperly excluding the Blenheim-Gilboa pumped storage facility from competing to supply SR and NSR, and (2) by allowing the price for NSR to control the price for SR.

8. In the Commission's May 31 Order,⁷ the Commission granted NYISO's proposed NSR bid cap. We also found that NYISO's practice of procuring SR and NSR from generators only located on the east side of an east-west constraint contributed to the price anomalies, and directed NYISO to develop procedures to maximize access to western suppliers of reserves. In addition, the Commission stated that one reason for the NSR price increases was NYISO's practice of allowing the highest bid for NSR to set the market clearing price for SR under certain circumstances. Last, the Commission stated in the May 31 Order that if NYISO had modeled its software to include the Blenheim-Gilboa storage facility, the market concentration levels would have been lowered. The Commission denied retroactive price relief and stated that changes should be prospective.

9. The Commission's November 8 Order⁸ denied requests for rehearing of the May 31 Order. The NYTOs argued that the Commission improperly denied retroactive relief and that the filed rate doctrine requires retroactive relief in instances of tariff violations. They argued that NYISO violated its Tariff by excluding Blenheim-Gilboa from competing to supply reserves and by allowing the price for NSR to control the price for SR.

10. The Commission's orders were appealed to the U.S. Court of Appeals for the D.C. Circuit.⁹ On remand, the court affirmed the Commission's determination not to grant retroactive refunds based on the filed rate doctrine and on the related rule against retroactive ratemaking. The court, however, returned the case to the Commission to further explain why TEP was inapplicable to remedy (1) NYISO's exclusion of Blenheim-Gilboa from bidding into the reserves market and (2) NYISO's failure to accept bids from western suppliers into the reserves market. The court also found that the Commission had not adequately explained why NYISO's actions had not violated its

⁷ *New York Independent System Operator, Inc.*, 91 FERC ¶ 61,218 (2000) (May 31 Order), *reh'g denied*, 97 FERC ¶ 61,155 (2001) (November 8 Order), *reh'g denied*, 99 FERC ¶ 61,125 (2002) (April 29 Order).

⁸ *New York Independent System Operator, Inc.*, 97 FERC ¶ 61,155 (2001).

⁹ *Consolidated Edison Co. of N.Y. v. FERC*, 347 F.3d 964 (D.C. Cir. 2003) (*Consolidated Edison*).

tariff with respect to NYISO's treatment of the pricing of SR and NSR and NYISO's failure to obtain operating reserves from Blenheim-Gilboa.

11. On remand, the Commission found that NYISO did not abuse its discretion by refraining from exercising its TEP authority to recalculate prices in connection with the exclusion of Blenheim-Gilboa and western suppliers. Additionally, we found that NYISO did not violate its tariff by permitting the modeling of the Blenheim-Gilboa plant so that the output of that plant could not be offered into the reserves markets. We also found that, although NYISO did violate its tariff with regard to the interdependent determination of the prices of SR and NSR, that violation did not warrant price recalculation and refunds.

II. Discussion

12. The court, on remand, found that under the filed rate and retroactive ratemaking doctrines, the Load Serving Entities (LSEs) were not entitled to retroactive rate adjustments for the period prior to the NYISO tariff filing during which the LSEs alleged market power had been exercised. The only issues remanded by the court were whether: the Commission should have invoked NYISO's TEP to remedy two alleged market flaws -- the exclusion of the Blenheim-Gilboa facility from bidding into the reserves market and the failure to accept bids from western suppliers; and whether refunds should be ordered for two alleged tariff violations -- pricing of spinning and non-spinning reserves and the exclusion of the Blenheim-Gilboa facility from the non-spinning reserves market. Throughout the rehearing requests, parties maintain that refunds are needed to rectify the alleged market power exercised prior to NYISO's section 205 filing.¹⁰ In resolving the issues on remand, the Commission limits its inquiry solely to the specific issues remanded by the court -- whether NYISO's TEP provisions should be applicable here and whether there were violations of NYISO tariff --and whether refunds are warranted for the violations on their own merits, without regard to the alleged abuses occurring prior to NYISO's tariff filing.¹¹

¹⁰ For example, the NYTOs argue that refunds are appropriate here because market power may have been exercised prior to NYISO's section 205 filing. NYTO Rehearing Request at 10.

¹¹ Issues relating to retroactive refunds for market power and market manipulation prior to NYISO's section 205 filing were decided by the court and relitigation of those issues is precluded by the law of the case. *See Laffey v. Northwest Airlines, Inc.*, 740 F.2d 1071 (D.C. Cir. 1984).

A. NYISO's Temporary Extraordinary Procedure Authority

13. NYISO's TEP provision allows for corrective action to address market design flaws. NYISO's TEP provision states

If the ISO determines that a Market Design Flaw or Transitional Abnormality exists, the ISO *may* take Extraordinary Corrective Action to correct a Market Design Flaw or to address a Transitional Abnormality. . . . Extraordinary Corrective Actions are to be effective and applied on an interim basis only, and are to be imposed only during the time needed to address a Transitional Abnormality or to develop a long-term solution to a Market Design Flaw on a non-emergency basis.¹²

The TEP provision allows NYISO to take corrective action as it considers appropriate, which would include recalculating market clearing prices, in the event of a finding that a market design flaw exists. A "Market Design Flaw" is defined 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 or prices that would not be produced in a workably competitive market.¹³

1. Court's Ruling

14. The court found that although the Commission acknowledged that TEP allows for retroactive recalculation, the Commission's determination that TEP applies only in circumstances of straightforward calculation errors is inaccurate. It went on to state that the Commission's past TEP orders do not justify the narrow view of TEP that the Commission applied to this case and remanded for the Commission to explain why TEP does not apply here.

2. The Commission's March 4 Order

15. In the March 4 Order, we agreed with the court that we did not initially limit TEP to certain technical miscalculations. However, we found that NYISO did not abuse its discretion when it refrained from invoking TEP to recalculate prices. This is because

¹² NYISO's Services Tariff, Attachment E, section C, emphasis added.

¹³*Id.*, section A.

TEP was drafted to enable NYISO to exercise its judgment as to whether and when TEP should be applied. We found that “NYISO made a reasonable determination that the problems in the market were primarily due to market power, not market design flaws.”¹⁴

16. With respect to the western suppliers, we agreed with NYISO that these suppliers should not be considered reliable reserves due to transmission constraints. With respect to Blenheim-Gilboa, we found that NYISO’s failure to model the plant for NSR reserves was reasonable since it reflected the owners’ choice to use the plant’s output for energy. We also found that price recalculation would not necessarily be appropriate, given that it was early in NYISO’s operation and “the NSR market had not yet begun to function competitively and NYISO would have had no clear basis on which to recalculate, with reasonable certainty” the prices for NSR had Blenheim-Gilboa been included.

3. Rehearing Request

17. The NYTOs request rehearing with respect to the Commission’s determination regarding TEP. They argue that the Commission’s finding that NYISO was not required to take Blenheim-Gilboa as an NSR resource and that NYISO’s decision was discretionary is contradicted by the Commission’s finding that TEP was added to the tariff in order to address situations such as this, where a lower cost supply of reserves is available but not being taken because of software problems. They state that the Commission found that the conditions in the NSR market resulted from the unintended exclusion of suppliers such as Blenheim-Gilboa as a resource from the NSR market and argue that both NYISO and the Commission had separate obligations to enforce the TEP provisions of the NYISO tariff to correct for the failure to include Blenheim-Gilboa.

18. Also regarding Blenheim-Gilboa’s exclusion, the NYTOs argue that the software flaw should not be uncoupled from market power since “the market power is a direct result of the market design/software flaw.”¹⁵ They further state that there is no indication that the owners acted as a barrier to the inclusion of Blenheim-Gilboa in the software modeling, nor that the contract was an obstacle.¹⁶

¹⁴ March 4 Order, 110 FERC ¶ 61,244 at P 56.

¹⁵ NYTOs April 4, 2005 Filing at 18.

¹⁶ *Id.*

19. The NYTOs argue that the Commission has an obligation to enforce the TEP tariff provision to correct for the exclusion of Blenheim-Gilboa, as well as NYISO's failure to take reserves from western suppliers. They further state that the Commission has an independent obligation to invoke NYISO's TEP tariff provisions and "cannot delegate to NYISO the decision to enforce a tariff provision that the Commission found was a necessary protection for customers as part of the overall market-based tariff."¹⁷

20. The NYTOs argue that the Commission failed to fulfill its statutory obligations to correct prices for the Relevant Period. They state that it is possible to reasonably calculate refunds, and "difficulty" is not a valid excuse.

4. Commission Response

21. The court directed that the issue to be addressed on remand is whether "FERC should have directed NYISO to provide a remedy under its Temporary Extraordinary Procedures."¹⁸ For the reasons discussed in the March 4 Order and in the discussion below, the Commission has concluded that, based on the TEP tariff provisions, there is insufficient basis for it to direct NYISO to have invoked TEP in these circumstances. TEP included a broad grant of authority that did not mandate price redeterminations any time NYISO thought the market could be improved through tariff changes. Neither the exclusion of the western suppliers nor the failure to dispatch Blenheim-Gilboa were market design flaws under TEP, since there were reasonable bases for the failure to include these generators in the reserve markets, and neither meets the TEP standard of "reasonable certainty" to qualify for retroactive rate adjustments.

22. We address below the requests for rehearing.

a. NYISO's Obligation to Invoke TEP

23. NYTOs argue that the Commission was obligated to invoke TEP to remedy the consequences of NYISO's decision to not take reserves from western suppliers or its failure to include Blenheim-Gilboa. NYTOs further argue that the Commission has an independent obligation to invoke NYISO's TEP tariff provisions and "cannot delegate to

¹⁷ *Id.* at 21, 25.

¹⁸ *Consolidated Edison*, 347 F.3d 964, 970.

NYISO the decision to enforce a tariff provision that the Commission found was a necessary protection for customers as part of the overall market-based tariff."¹⁹

24. As the Commission found in the March 4 Order, invocation of TEP was not mandatory, but discretionary with the ISO. The TEP provision provides that if a market design flaw exists, NYISO “may take Extraordinary Corrective Action.”²⁰ NYISO itself recognized that TEP should not be invoked every time NYISO determines that a change in market design is warranted.²¹ As NYISO stated,

[c]hanges and improvements in market design do not mean that previously the market did not operate as designed; that illogical conclusion would require any market improvement to carry with it a requirement of an ECA and price redeterminations for all prior implementations of the market. The TEP were clearly never intended to impose such an absurd result.²²

25. Moreover, TEP contains requirements for notice and posting of any corrective actions that are to be undertaken, so that market participants are aware of the actions taken, and can plan accordingly.²³ TEP also requires that NYISO take the “least restrictive” action available in any circumstance, with recalculation of prices being the most restrictive. Because NYISO did not invoke TEP, obviously none of these procedural protections were followed. The inability to invoke these protections retroactively requires that the NYISO’s determination not to invoke TEP should be given considerable weight and the Commission should apply TEP retroactively only if the NYISO’s failure to use this procedure was unreasonable.

26. NYTOs argue that the Commission erred in delegating authority to the NYISO the decision whether to invoke TEP. The issue of NYISO’s invocation of its TEP authority comes to the Commission in an unusual posture. Typically, parties complain that a utility’s action exceeds its tariff authority. In this instance, the complaint is that the

¹⁹ NYTOs' April 4, 2005 Filing, at 21, 25.

²⁰ NYISO’s Services Tariff, Attachment E, Introduction and section C.

²¹ March 4 Order, 110 FERC ¶ 61,244 at P 59.

²² Motion of NYISO to Reopen Record, June 25, 2004, at 12.

²³ NYISO’s Services Tariff, Attachment E, section C,2.

NYISO failed to take action that arguably would be permissible under its tariff. NYISO's TEP, as drafted, provides the NYISO with discretion to determine whether an extraordinary event has taken place that justifies a decision to invoke TEP. In the March 4 Order, the Commission, therefore, used abuse of discretion as a means of evaluating the NYISO's decision not to invoke TEP. It is the use of the term abuse of discretion which appears to be the genesis of NYTO's claim that we improperly delegated authority to NYISO.

27. The Commission, however, was not delegating our responsibility to the NYISO.²⁴ Rather, we were responding to the court's requirement that we determine whether we "should have directed NYISO to provide a remedy under its Temporary Extraordinary Procedures."²⁵ In using the term abuse of discretion, the Commission was not seeking to delegate Commission authority to the NYISO, but was carrying out the court's instruction on remand. In looking at this issue, the Commission used abuse of discretion as being synonymous with an inquiry into whether the NYISO's determination to refrain from invoking TEP was reasonable under the circumstances faced by the NYISO at the time.

b. The Circumstances Did Not Warrant Invocation of TEP

28. The NYTOs maintain that TEP was required to be invoked because the conditions in the market resulted directly from the exclusion of the western suppliers and Blenheim-Gilboa. But NYISO itself did not attribute the perceived problems to these causes. Rather, it believed the problems resulted from high concentration and related bidding

²⁴ If, as the NYTOs maintain, the TEP provision constitutes improper delegation of authority to NYISO, the provision is *ultra vires* and could not be enforced. *See Bonneville Power Admin. v. FERC*, No. 02-70262, 2005 U.S. App LEXIS 19205 (9th Cir., Sept. 6, 2005) (Commission cannot exercise jurisdiction or authority unless authorized by statute); *Columbia Gas Transmission Corp. v. FERC*, 404 F.3d 459 (D.C. Cir. 2005) (Commission cannot enforce a tariff provision that is beyond its jurisdiction). The NYTOs fail to cite any legal authority for the Commission's obligation or authority independent of TEP to provide retroactive refunds, and the D.C. Circuit found that under the FPA, the Commission did not have independent authority to retroactively recalculate prices as a result of the alleged exercise of market power. 347 F.3d 964, 969-70.

²⁵ *Consolidated Edison*, 347 F.3d 964, 970.

behavior, concluding that "although certain flaws in NYISO's market design have become apparent, eliminating these flaws alone would not restore the 10-minute reserve markets to a workably competitive state, and cannot change the past performance of the operating reserves markets."²⁶ NYISO sought to directly address the problems by making its section 205 filing, and not invoking TEP. In these circumstances, we cannot conclude that NYISO's decision to decline to exercise its discretionary TEP authority was unreasonable, much less an abuse of discretion.

29. Moreover, as discussed below, we cannot conclude that the circumstances surrounding the exclusion of the Western suppliers and Blenheim-Gilboa reasonably warranted the invocation of TEP. Nor did these circumstances provide the reasonable certainty required by TEP for calculation of retroactive price adjustments.

i. Western Suppliers

30. The NYTOs maintain that the Commission recognized that the exclusion of the western suppliers was a market design flaw and directed NYISO to develop procedures to include the western suppliers. They therefore conclude that the Commission must find that the exclusion of the western suppliers is a design flaw that must be rectified by TEP.

31. As the Commission found in the March 4 Order, however, NYISO itself concluded at the time that the exclusion of the western suppliers was not a market design flaw. NYISO maintained that western suppliers cannot be considered reliable reserves for the Eastern market due to serious transmission constraints that apply approximately 80 percent of the time.²⁷ As NYISO explained, it chose to use the limited West-East transmission capability to provide energy, rather than reserves, at the behest of the transmission owners in order to reduce potential congestion:

The NYISO's adoption of fixed locational reserve requirements was primarily based on an assumption by the Transmission Owners that designed the NYISO that the cost of reserves would be less than the cost of energy. By maintaining fixed NYCA Eastern reserves, a greater transmission capability across the Central-East interface could be made available for energy, thereby reducing a major source of potential LBMP congestion within the NYCA. . . . Thus, at

²⁶ NYISO Answer to RG&E complaint, April 20, 2000, at 4.

²⁷ *See* NYISO Motion to Reopen the Record, at 10-12 (June 25, 2004).

present, the system is operating as it was initially proposed by the Transmission Owners, and is consistent with reliability constraints.²⁸

At the time, in fact, NYISO did not know how, given the transmission constraints, it could model the western suppliers for reserves:

[NYISO's] review indicates that Central-East was constrained approximately 80% of the time and established that the need to procure additional 10-Minute Reserves for the Central East transmission constraint could not be predicted in the day-ahead or hour-ahead market in advance of real-time. It is therefore impractical, in the short term, to develop automated or manual procedures that would permit the NYISO to rely on western supplies when there is no anticipated congestion at Central-East, because congestion is so frequent and intervals without congestion are difficult to anticipate.²⁹

32. Given the physical transmission constraints on the system, it was reasonable for NYISO to conclude that the treatment of the western suppliers was not a market design flaw. For instance, had the western suppliers been modeled for reserves rather than for energy, the market clearing price for energy could well have increased as much or more than the reserve price. It is hard to see how the NYTOs can now assert that the market design that they developed and endorsed as a reasonable way of minimizing congestion prices in energy should be considered such a serious market design flaw that TEP should have been invoked.

33. The NYTOs cite to the court's statement that the Commission "pointed out that the analysis submitted in support of market based rates contemplated that the supply market would include these suppliers."³⁰ But the court's point here was only that these allegations fell within a possible TEP remedy. The court was not making a finding that these were in fact market design flaws cognizable under TEP. Indeed, the portion of the Commission order cited by the court stands only for the proposition that "the conditions under which market-based rate authority for ancillary services was granted do not match

²⁸ See Answer of NYISO to Complaint of Rochester Gas & Elec. Corp., Docket Nos. EL00-64-000 & ER00-1969-000, at 10 (Apr. 20, 2000).

²⁹ NYISO's Combined Compliance Filing and Report, at 8-9 (September 8, 2000).

³⁰ *Consolidated Edison*, 347 F.3d at 971-72.

the current operational realities of the New York ISO's reserve markets."³¹ The Commission here was not concluding that the exclusion of the western suppliers was a market design flaw; rather it was recognizing that the reality of the market did not match the perhaps optimistic assumptions under which the market was designed.

34. While the Commission in its initial order directed NYISO to seek to develop procedures to try to "maximize access to western suppliers,"³² the Commission did not conclude that the exclusion of these western suppliers, at that time, was a market design flaw. The Commission was directing NYISO to see if it could develop procedures in the future to increase the availability of western supplies, not finding that the western suppliers at the time were a reasonable alternative for reserves. Indeed, the Commission's finding here does not conflict with its prior orders, as the NYTOs contend. In the Commission's November 8, 2001 Order in this proceeding, the Commission recognized that based on NYISO's report, "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."³³

35. As discussed above, not every effort by the Commission or NYISO to improve the market is evidence that TEP should be invoked retroactively. Indeed, as the NYTOs recognize, this issue is still, in 2005, the subject of continuing discussion.³⁴ It therefore can hardly be concluded that the exclusion of western suppliers from the reserve market due to serious transmission constraints was a design flaw in the year 2000.

ii. Blenheim-Gilboa

36. The NYTOs maintain that the Commission's finding that the failure to dispatch Blenheim-Gilboa is not a market design flaw is contradicted by the fact that NYISO is required to take the least cost mix of supplies, that Blenheim-Gilboa was intended to be a source of reserves, and that TEP was included in the tariff to address situations where a lower cost unit is available but not taken due to software problems.

³¹ May 31 Order at 61,799.

³² *Id.* at 61,800.

³³ November 8 Order at 61,677.

³⁴ NYTOs Rehearing Request at 24 (this issue has continued to be the subject of orders up until the present day).

37. NYISO itself has stated that its exclusion of Blenheim-Gilboa was because the owners of the unit at the time did not choose to use the unit for reserves, but reserved it for energy.³⁵ While excluding an available resource could be a design flaw, it is hard to find that excluding a resource that did not want to be included in the reserve market is such a flaw. NYISO's market is designed to provide generators with the ability to participate by submitting bids, not to give NYISO unconstrained authority to dispatch generators who do not want to participate.

38. The NYTOs also take issue with the Commission's conclusion that the decision not to retroactively invoke TEP to require refunds with respect to Blenheim-Gilboa was justified because refunds could not be calculated with reasonable certainty. They maintain the Commission has a statutory obligation to order refunds for tariff violations and that just and reasonable rates are not a single amount, but encompass a range of permissible rates.

39. In the first place, the NYTOs confuse the standards for determining just and reasonable rates in a prospective section 205 filing with the determination of whether refunds under TEP meet the tariff standards for recalculating prices. The issue here is not the extent of the Commission's statutory authority to determine just and reasonable rates or order refunds; rather, it is whether a specific tariff provision, TEP, should have been invoked to redetermine prices reflecting the exclusion of Blenheim-Gilboa. TEP itself recognizes that the recalculation of prices is the last potential remedy to be invoked. Indeed, TEP itself has a preference for the remedy of "notify[ing] market participants [of a shortage] and request[ing] that Market Participants submit bids which provide greater operating flexibility for such products."³⁶ It may well have been within NYISO's TEP authority to request such bids from Blenheim-Gilboa at the time these events took place.

40. But NYISO did not do so and the issue now is whether the recalculation of prices is within the conditions established by TEP. The tariff states that such recalculation is a permissible TEP remedy only "if possible, with reasonable certainty."³⁷ The point of this inquiry is to determine whether the TEP tariff provisions would have justified a

³⁵ NYISO Answer to RG&E complaint, April 20, 2000, at 5 (the operational limitations affecting Blenheim-Gilboa resulted from the scheduling agreement developed and signed by the Blenheim-Gilboa joint project contractors).

³⁶ NYISO's Services Tariff, Attachment E, section C,2.c,(1).

³⁷ NYISO's Services Tariff, Attachment E, section C,2.c,(2).

recalculation of prices.³⁸ As the Commission found in the March 4 Order, such recalculations cannot be done consistent with the TEP requirements. Blenheim-Gilboa did not bid in the NSR market at the time, and there is no evidence as to what its bid would have been or what factors would have influenced its bid. Without such information, prices cannot be recalculated with “reasonable certainty.” Moreover, there is no evidence that the inclusion of one additional bidder into the market would necessarily have had any significant effect on prices in that market or that such an effect can be determined with “reasonable certainty.”

41. While the NYPA points out that NYISO tried to make a stab at calculating such prices, this filing uses future prices, not contemporaneous prices, to try to create a proxy for what the Blenheim-Gilboa price would have been. Such *ex post* calculations do not satisfy the TEP standard, which required that the prices can be recalculated with reasonable certainty at the time the TEP is invoked.

42. The objections to NYISO’s calculation by other parties demonstrate that its attempt to recreate the bids by Blenheim-Gilboa in the absence of historic evidence cannot be found “reasonably certain.” They maintain that NYISO’s average price methodology ignores the features of a dynamic market by not reflecting hourly variations in NSR supply, demand and prices. They contend that the four year period used by NYISO is not necessarily comparable to market conditions during the period at issue due both to changes in market design, the entry of new competitors changing the supply mix, and changes in weather and load conditions. Among the changes in market design that could render the future prices unrepresentative of past prices include alternative methods of paying for opportunity costs that during the period in question had to be included in bids, as well as virtual bidding, automated mitigation, the treatment of 30 minute reserves, and the modeling of load pockets in dispatch programs.

43. The TEP tariff provision allowed NYISO as an independent entity to try to correct changes to its market design through prospective application of revised rules. While NYISO perhaps could have requested bids by Blenheim-Gilboa to include it in the market, its authority to recalculate price was limited to making a recalculation when possible with “reasonable certainty.” The NYTOs emphasize the use of the word reasonable, but ignore the “certainty” qualification, and the record here shows that trying to model past bids is not reasonably certain.

³⁸ See *Sacramento Mun. Util. Dist. v. FERC*, No. No. 04-1171, 2005 U.S. App. LEXIS 23540 (D.C. Cir. Nov. 1, 2005) (Commission decision was not arbitrary when it engaged in a straightforward application of the relevant tariff).

B. Spinning and Non-Spinning Reserve Pricing

44. The complaints addressed situations in which, if the two reserve markets were priced independently, the accepted bid for NSR would be higher than the SR price. In this situation, NYISO would use the higher NSR price to set the market clearing price for both types of reserves. Certain provisions of NYISO's tariff provided, however, that the prices of both reserves should be set independently.

1. The Commission's March 4 Remand Order

45. In the March 4 Order, the Commission concluded that although NYISO may have violated certain provisions of its tariffs, the Commission would not order refunds for setting the same market clearing price for both sets of reserves. The Commission found that, based on court precedent, requiring refunds would not be appropriate because the end result of NYISO's tariff violation was a just and reasonable rate. In fact, the Commission pointed out that although NYISO may have technically violated the sections of its tariff requiring reserves to be priced independently, its action was entirely consistent with the overall least cost pricing regime established by its tariff, and would, in the long run, produce the lowest prices to consumers. In fact, pricing the two services independently could have resulted in reliability problems because generators would have financial incentives to submit bids in the higher priced NSR market, leaving NYISO with a shortage of the more critical SRs.

2. Rehearing Requests

46. The NYTOs argue that refunds should be ordered because the court and the Commission recognize that NYISO violated its tariff when pricing SR by reference to NSR. They state that the filed rate doctrine does not permit the Commission to refuse to grant refunds and that it cannot be equitable to allow those prices that resulted from the exercise of market power to determine SR prices in direct contravention of the filed rate doctrine. NYISO states that the Commission's decision to not require refunds ignores the manipulation of NSR prices to inefficient, non-competitive levels. The NYTOs state that while the court recognized that the Commission has some degree of remedial discretion, the Commission's denial of refunds must be based upon a considered analysis of the facts of the case and the purposes of the filed rate doctrine and rule against retroactive rate making. The NYTOs and NYISO both argue that the Commission's factual findings in this case cannot be reconciled with a denial of refunds. The NYTOs state that the Commission would not have placed a bid cap³⁹ on NSR prices if the resulting prices were

³⁹ The bid cap was imposed as part of the relief that the Commission gave NYISO for the events of the Relevant Period. *See May 31 Order*, 91 FERC ¶ 61,218.

not proper. They also argue that the filed rate doctrine would be eviscerated if a public utility or NYISO or the Commission could charge a rate other than that on file simply because NYISO or the Commission preferred the rate methodology that the ISO or the agency formed later, and that market-based rates, such as the operating reserve prices, are unlawful unless they result from a competitive market. They argue that to the extent that suppliers received more money than they would have received if NSR and SR were priced separately, they received a windfall.

3. Commission Response

47. The court in this case did not mandate that refunds be ordered, recognizing that even if NYISO violated its tariff, the Commission could use its discretion to not order refunds.⁴⁰ As courts have noted many times, "the breadth of agency discretion is . . . at [its] zenith when the action assailed relates primarily not to the issue of ascertaining whether conduct violates the statute, or regulations, but rather to the fashioning of . . . remedies."⁴¹ Additionally, "the Commission ordinarily has remedial discretion, even in the face of an undoubted statutory violation, unless the statute itself mandates a particular remedy."⁴² The courts have held that refunds are not appropriate if the end result of a tariff violation is not "unjust, unreasonable, or unduly discriminatory."⁴³ In fact, the court has itself reversed the Commission when the Commission ordered refunds for a technical tariff violation when that violation was consistent with Commission policies and did not result in a windfall.⁴⁴

⁴⁰ *Consolidated Edison*, 347 F.3d at 973.

⁴¹ *Connecticut Valley Electric Co. v. FERC*, 208 F.3d 1037, 1043 (D.C. Cir. 2000) (*Connecticut Valley*), citing *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) (*Louisiana Public Service Commission*).

⁴² *Connecticut Valley*, 208 F.3d at 1043, citing *Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67, 72-73, 76 n.8 (D.C. Cir. 1992) (*Towns of Concord*).

⁴³ *Louisiana Public Service Commission*, 174 F.3d at 223; *Gulf Power Co. v. FERC*, 983 F.2d 1095, 1101 (D.C. Cir. 1993) (finding refund remedy to be disproportionate to a technical violation intended to benefit customers).

⁴⁴ *Koch Gateway Pipeline Co. v. FERC*, 136 F.3d 810 (D.C. Cir. 1998).

48. Here, the crux of NYISO's and the NYTO's claim that refunds are appropriate is that "the Commission's decision not to order refunds ignores the market manipulation that dramatically increased NSR prices in the refund period."⁴⁵ But the court in the remand order found that the filed rate and retroactive ratemaking doctrines preclude retroactive price relief for the alleged market manipulation that took place prior to NYISO's tariff filing. The issue here is limited to whether refunds should be paid for the manner in which NYISO priced reserves.⁴⁶

49. The Commission finds that based on the specific tariff violation at issue here refunds are not appropriate. As the Commission explained in detail in the March 4 Order, NYISO's approach to pricing NSR and SR was the correct method of implementing its least cost dispatch market design. While section 4.21 of NYISO's tariff required the two reserve categories to be priced independently, section 4.9 of the tariff requires NYISO to "select the least cost mix of Ancillary Services and Energy suppliers." Thus, the pricing implemented by NYISO, although technically at odds with section 4.21 comported with NYISO's pricing model and produces the least cost pricing of reserves. Indeed, in its Answer to the complaint, NYISO recognized that its pricing for NSR and SR was consistent with its least cost dispatch method. Citing to section 4.9 of its tariff, NYISO states:

Despite NYSEG's arguments to the contrary, the NYISO software design will produce the least cost mix of Ancillary Services. Specifically, the NYISO software substitutes higher quality reserves in place of lower quality reserves, when doing so would lower the total bid costs (i.e., when the marginal bid for the higher quality reserve is lower than the marginal bid for the lower quality reserve). Thus, the NYISO's software will always schedule low cost reserves on operating units instead of higher cost reserves on off-line units. As this substitution is made and a larger quantity of the 10-minute spinning reserves are accepted, the marginal bid cost of 10-minute spinning rises. Likewise, as the quantity of accepted bids for 10-minute NSR on non-synchronized units falls, the marginal bid cost of the 10-minute NSR will decrease. This substitution will continue until the marginal bid cost of 10-minute spinning reserves

⁴⁵ NYISO Rehearing Request at 1.

⁴⁶ The technical tariff violation should not be used as a back-door method of ordering the very retroactive relief that the court found beyond the scope of the Commission's authority.

and 10-minute NSR converges or the supply of 10-minute spinning reserves is exhausted. This system guarantees that the total bid cost for all reserves will be minimized. . . .

The Services Tariff defines 10-minute NSR as “Operating Reserves provided by generation facilities that can be started, synchronized and loaded within ten (10) minutes.” This definition can be met by either spinning or nonspinning reserves. Thus, NYISO’s Security Constrained Unit Commitment (SCUC) program does not distinguish operationally between reserves that are on units that are spinning or units that are not spinning but can start up quickly, except to the extent that a portion (currently, 600 MW) of the operating reserve requirement must be met by spinning reserves. *Once this requirement is met, however, the two types of reserves are substitutes, and the substitution of the two services (described above) causes the prices of the two to converge as fewer 10-minute NSR bids are accepted and more 10-minute spinning reserve bids are accepted.*⁴⁷

50. Even though NYISO is now advocating refunds, it concedes that: “the March 4 Order correctly describes the virtues of interdependent reserves pricing, “if [suppliers] offered their product competitively into the more valued reserve market.”⁴⁸ The only difference, it asserts, is that during the Relevant Period, it claims that prices were not offered competitively. But, as discussed above, whether the generators may have received higher prices as a result of market manipulation or market power has been found not susceptible to retroactive remedy.

51. NYISO and NYTOs have not shown that NYISO’s method of pricing reserves caused the alleged market manipulation or exercise of market power. If anything, NYISO’s pricing method protected system reliability by helping to ensure that sufficient SRs were bid into the market; had NYISO priced NSR and SR reserves independently, generators observing the high NSR bids would have bid into the NSR market leaving NYISO short of the more crucial spinning reserves. NYISO claims that providing refunds here would not create perverse incentives or jeopardize system integrity since the refunds would be retroactive. However, the issue here is that, as reflected above, NYISO

⁴⁷ NYISO’s Answer to Complaint, Docket No. EL00-63-000, at 7-8 (April 13, 2000) (emphasis added).

⁴⁸ NYISO Rehearing Request, at 6.

adopted this correct pricing methodology to achieve these goals. NYISO's argument amounts to a form of bait and switch. It is arguing that the market should receive the benefit from a correct pricing regime, but once those benefits have been realized the generators should be required to pay refunds.⁴⁹ NYISO should not have it both ways: it should not be able to adopt a pricing regime when necessary to preserve system reliability, and then, after reliability is preserved, require the generators that provided that reliability to pay refunds based on an alternative pricing regime that would not have preserved system reliability. When looking solely at the alleged tariff violation at issue here, the prices determined by NYISO were the correct just and reasonable prices for SRs and NSRs and generators received no windfall from this specific tariff violation.

52. Moreover, ordering refunds here would be unrelated to the alleged exercise of market power and market manipulation for which NYISO and NYTOs argue refunds are appropriate. It would require refunds not from those generators that NYISO and NYTOs allege manipulated the market to retain the high NSR prices. They would retain their high prices. Rather, it would penalize those generators that bid competitively, at low prices, in the SR market by requiring them to pay refunds.⁵⁰

53. The NYTOs maintain that the Commission's denial of refunds is at odds with the Ninth Circuit's decision in *California v. FERC*.⁵¹ Although this case is still pending at the Ninth Circuit on rehearing, the Commission finds that these cases are sufficiently different that *Lockyer*, regardless of its outcome, would not justify the ordering of refunds here. In *Lockyer*, the court addressed a situation in which firms, with market-based rate tariffs, failed to file required reports of their transactions. The court found that filing these reports were an "integral part of a market-based rate tariff,"⁵² ensuring that the rates for these transactions would be on file with the Commission. Because the firms failed to comply with the reporting requirement, the court concluded that the Commission had the

⁴⁹ NYISO's position is akin to arguing for the use of a market-clearing auction in which generators will be paid the market clearing price in order to encourage marginal cost bidding and then, after the bids are received, changing the rules and paying each generator its as-bid price in order to reduce cost.

⁵⁰ Indeed, to be consistent, if refunds were ordered here, NYISO would have to provide increased revenue to generators in those cases in which its application of least cost pricing methodology resulted in lower prices for either SRs or NSRs.

⁵¹ 383 F.3d 1006 (9th Cir. 2004) (*Lockyer*).

⁵² *Id.* at 1015.

authority to require refunds retroactively for market abuses. But the court also recognized that “FERC may elect not to exercise its remedial discretion by requiring refunds” in appropriate situations.⁵³

54. The issue in this case, in contrast, focuses on NYISO’s technical violation of a specific tariff provision, not on a failure to comply with a filing requirement deemed integral to the Commission’s acceptance of market-based rates. Unlike in *Lockyer* where the failure to file the reports prevented “monitor[ing] the market, or gaug[ing] the just and reasonable nature of the rates,”⁵⁴ we find here that NYISO’s violation of the tariff provision regarding the determination of prices for reserves was the proper method of implementing its market design and produced the most efficient prices for the market. In fact, as pointed out above, ordering refunds in this case would not target the generators that the NYTOs accuse of exercising market power or manipulating the market; rather it would require refunds for generators that bid lower prices into the SR market. Regardless of the eventual outcome of *Lockyer*, the factual situation here is much different and does not justify the provision of refunds.

C. **NYISO Did Not Violate its Tariff by Excluding Blenheim-Gilboa**

1. **The Commission’s March 4 Order Remand Order**

55. On remand, the Commission found that the NYISO tariff does not require it to include Blenheim-Gilboa in the NSR market. The Commission found that the tariff required that the ISO shall provide procedures to establish adequate operating reserves that comply with the Reliability Rules of the State of New York.⁵⁵ But the tariff did not specifically require that Blenheim-Gilboa be included as reserves, particularly when the owners of Blenheim-Gilboa intended to use the facility to produce energy, not reserves. Further, the Commission found that because NYISO was seeking to honor the choices made by its market participants, and it was not at that time apparent that that choice would have a negative impact on the reserves market, the Commission would not require refunds based on this choice.

⁵³ *Id.* at 1016.

⁵⁴ *Id.* at 1015.

⁵⁵ NYISO’s Services Tariff Original Sheet No. 137.

2. Rehearing Request

56. The NYTOs argue that refunds are required for NYISO's failure to accept Blenheim-Gilboa as an NSR resource because NYISO violated its tariff by not accepting Blenheim-Gilboa NSR bids. They argue that since NYISO is required to take the least cost mix of supplies, it violated its tariff when it excluded Blenheim-Gilboa. They state that the Commission intended Blenheim-Gilboa to be a source of reserves when it approved the tariff and that the consequences of removing Blenheim-Gilboa from the mix resulted in market power, requiring the imposition of a bid cap.

3. Commission Response

57. We do not find that NYISO violated its tariff by excluding Blenheim-Gilboa. NYISO's failure to model Blenheim-Gilboa for NSR reserves reflected the owner's choice to use the plant's output for energy rather than for operating reserves.⁵⁶ Rate Schedule 4, which established the reserve markets, states only that "the ISO shall provide procedures to establish adequate operating reserves that comply with the Reliability Rules."⁵⁷ Schedule 4 then proceeds to set up reserve markets in which generators can bid into the markets they wish to serve.⁵⁸ Nothing in Schedule 4 requires a generator to bid into these markets or to bid reserves as opposed to energy.

⁵⁶ See March 4 Order, 110 FERC ¶ 61,244 at P 59 and NYISO Answer to RG&E Complaint, April 20, 2000, at 5-6.

⁵⁷ NYISO's Services Tariff Original Sheet No. 137. Reliability Rules are defined as rules that are in accordance with various organizations standards, including the North American Electric Reliability Council (NERC), the Northeast Power Coordinating Council (NPCC), the Commission, the New York Public Service Commission, and the Nuclear Regulatory Commission, as well as rules or regulations pursuant to the New York State Reliability Council Agreement. Section 2.158 of the Services Tariff.

⁵⁸ See, e.g., section 2.1 ("Suppliers offering Generator or Demand Side Resources to provide Spinning Reserve"); section 2.2 (Suppliers who have not been scheduled to provide spinning reserve and who have uncommitted capacity "may submit Availability Bids to provide Spinning Reserve" in the real-time market); section 3.1 ("Suppliers offering Generator or Demand Side Resources to provide 10-Minute NSR and/or 30-Minute Reserve in the Day Ahead commitment shall submit availability Bids for each hour of the upcoming day"); section 3.2 (Suppliers who have not been scheduled to provide non-spinning reserve and who have uncommitted capacity "may submit Availability Bids to provide 10-minute NSR or 3-minute Reserve to the ISO").

58. While a pump storage unit like Blenheim-Gilboa would meet the requirements for providing reserves, it was not required to do so, and NYISO did not violate its tariff in modeling its software to follow the wishes of the owners of the resource. As NYISO stated, its decisions regarding Blenheim-Gilboa comported with the desires of the owners of the unit: “the operational limitations affecting Blenheim-Gilboa are the result of the Blenheim Gilboa modeling decisions detailed in the ‘B-G Scheduling Agreement with NYISO Operation’ document that was developed and signed by the Blenheim-Gilboa joint project contractors.”⁵⁹

59. The NYTOs again argue that the Commission’s finding in the March 4 Order that there was no tariff violation ignores the Commission’s determination that NYISO is required to take the least cost mix of supplies and its finding in the May 31, 2000 Order⁶⁰ that Blenheim-Gilboa was intended to be a source of reserves when the tariff was accepted.⁶¹

60. The Commission did not find in the March 4 Order that NYISO was required to take the least cost of mix of supplies without consideration of whether those supplies were actually bid into the market in question. The Commission found that NYISO’s tariff implemented a least cost dispatch system for evaluating bids.⁶² This is not the same thing as requiring a unit to provide reserves when the owners of that unit determined to provide energy instead. With respect to its initial findings in the March 31 2000 Order, the Commission was reflecting the fact that “actual operations” of NYISO did not match some of the Commission’s earlier assumptions.⁶³ But this was not a finding that the actual operations of the market violated the existing tariff as regards the modeling of Blenheim-Gilboa. On a prospective basis, the Commission agreed with NYISO’s proposal to include this unit as part of its reserve market, but that is not the same as finding that NYISO violated its tariff in honoring the Blenheim-Gilboa owners’ request not to model this unit for providing reserves. Thus, no refunds for this action are warranted.

⁵⁹ NYISO Answer to RG&E complaint, April 20, 2000, at 5.

⁶⁰ May 31 Order at 61,799-800 & n.13.

⁶¹ NYTO’s Rehearing Request at 15.

⁶² March 4 Order at P 65.

⁶³ May 31 Order at 61,799-800 & n.13.

The Commission orders:

The rehearing requests are hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.