Reserve Self Supply

BIC

9/21/05

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Reserve Self Supply Status

- Compliance filing due in response to FERC order to continue working with MPs to arrive at an acceptable self supply option.
- Physical self supply is an impractical option under the NYISO financial market design.
- Previous NYISO filing indicated the possibility of taking no further action if East and West reserve price differential was essentially nil under SMD2.
- One objecting intervention was filed. FERC agreed that their argument has merit and ordered continuing work.
- We have met with the objecting party to discuss their concern. We believe that we can address their concern and be responsive to FERC's order.

Reserve Self Supply Under SMD2

- Price Difference Summary March – July*

  - 10 Minute spin E/W differential is $3 or less 96% 0f the time.

  - 10 Minute non-spin is $3 or less nearly 98% of the time.

* See Charts provided separately

Reserve Self Supply Under SMD2

- LECG Reserve cost analysis under SMD2. (Estimated savings available through buying less expensive Western reserves to meet the Eastern requirement when the transmission system was unconstrained.)
  - Estimated maximum DAM production cost savings for 2003/4 (using both availability bids and constraint shadow prices to approximate SMD2 rules):

    $163,247
  - Projected estimated maximum production cost savings – 2005:

    $3,618,511
    - Projecting annual savings using 2/01/05 to 8/31/05 data
  - Production cost savings do not directly translate into actual customer savings.

Reserve Self Supply Under SMD2

- Why did the estimated possible DAM savings increase with 2005 data?
  - West to East transmission constraint is seldom the binding constraint on reserves
  - Eastern prices didn’t change; western reserve prices dropped
  - The estimated savings methodology assumed, in the absence of a transmission constraint, that the balance of the Eastern requirement could be filled with Western reserves. This produces an unrealistically high production cost savings estimate.

Reserve Self Supply
Filing Plan (Staff recommendation)

Objective is to gain 100% approval of the 9/30/05 report to FERC and the subsequent tariff filing.

- In the 9/30/05 report, make our case that *physical* self supply is an impractical option under the NYISO financial market design.
- Approve a Motion today recommending that the Management Committee approve tariff language that asserts physical self supply is unavailable in the New York Market and identifying the two financial options that are currently noted in the tariff as the only presently available self-supply options.
  - The two existing financial options are: (i) bidding a generator into the reserves market or (ii) using CFDs.

Reserve Self Supply Filing Content

- <u>If Market Participants feel it also necessary, the NYISO could agree to:</u>
  - Continue to monitor reserve prices and further analyze production cost savings to fine tune the estimated savings available when the transmission system is unconstrained.
  - Begin engineering analysis in 2005 with analysis results and further decisions in 2006.
  - Note that MPs are satisfied that implementing a more perfect financial hedge for reserve costs could be a complex task and they do not feel any threat exists at present that NYISO reserve markets will fail.
  - Note that any improvement in the reserve cost hedging mechanism that would contain a move to locational settlements would also have to address the potential need for transmission optimization at that time.
  - No further financial hedge would be available before 2007.
  - Note that this effort may displace other projects over this time frame.
- These additional items would also be included in the FERC 9/30/05 report.

Reserve Self Supply
Filing Options
Summary

Amend the tariff to eliminate physical self supply as an option and:

1. Assert that no further action on additional reserve cost hedges is necessary

-or-

2. Recommend that the NYISO continue to monitor reserve prices and further analyze production costs savings bringing a recommendation to the BIC in 2006 as to whether a further financial hedge is warranted