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**MCDERMOTT, WILL & EMERY**

August 1, 2002

**Via Electronic Mail and Federal Express**

Richard J. Grossi  
Chairman  
c/o William J. Mueseler  
President and Chief Executive Officer  
New York Independent System Operator  
3890 Carman Road  
Schenectady, NY 12303

Re: Motion in Opposition to Appeal of the Management Committee's Denial of  
Motion to Defer Implementation of Day-Ahead Market Modeling Changes

Dear Chairman Grossi:

Pursuant to the Procedural Rules for Appeals to the ISO Board, Morgan Stanley Capital Group Inc., Consolidated Edison Company of New York, Inc., New York State Electric & Gas Corporation, and Rochester Gas and Electric Corporation hereby submit three copies of their Motion in Opposition to Select Energy Inc.'s Appeal of the Management Committee's Decision to deny Select Energy's motion to defer the implementation of certain modeling changes to the Day-Ahead Market.

A copy of the Motion in Opposition has been transmitted electronically to Kristen Kranz, with the request that, upon receipt, she serve it upon each member of the Management Committee.

Sincerely,



Donna M. Sauter

*Attorney for Morgan Stanley Capital Group Inc.*

cc: Kristen Kranz (via electronic mail)

**MOTION IN OPPOSITION TO SELECT ENERGY'S APPEAL OF THE  
MANAGEMENT COMMITTEE'S DECISION TO DENY SELECT ENERGY'S  
MOTION TO DEFER THE IMPLEMENTATION OF CERTAIN MODELING  
CHANGES TO THE DAY-AHEAD MARKET**

**I. PRELIMINARY STATEMENT**

Morgan Stanley Capital Group Inc., Consolidated Edison Company of New York, Inc., New York State Electric & Gas Corporation, and Rochester Gas and Electric Corporation oppose Select Energy, Inc.'s ("Select") Appeal of the New York Independent System Operator Management Committee's July 11, 2002 decision to deny Select's motion to defer implementation of certain modeling changes to the Day-Ahead market (the "Appeal").

The claims Select raises in its Appeal, discussed in detail below, are without merit. The NYISO provided sufficient information about, and the reasons for, the modeling changes to market participants and provided several forums in which market participants could discuss the modeling changes prior to implementing them. Select's suggestion to remove the changes for nine months so that the effects of the changes can be considered could expose the market to unnecessary and detrimental arbitrage opportunities between the Day-Ahead and Real-Time markets. The modeling changes were appropriate and necessary to implement FERC directives and to enhance the NYISO markets. For these reasons, the Board should deny Select's Appeal.

**II. ARGUMENT**

Select requests that the NYISO "remove" changes to the NYISO Day-Ahead model that were implemented effective, June 19, 2002, to comply with FERC's directive that the NYISO address out-of-merit issues, which requires corrections to software limitations that prevented consideration of the New York City sub-load pockets. Select erroneously states that these changes, which potentially could alter the price levels in New York City and, hence, the value of the TCCs it holds, were not appropriately reviewed and approved by NYISO market

participants.<sup>1</sup> Select also claims that a party has a right to expect that the data provided by NYISO at the time the party makes a decision to participate in the NYISO-administered TCC markets will remain unchanged.<sup>2</sup> In effect, Select would prohibit the ISO from making any changes, modeling or otherwise, that could affect the value of its TCCs. Indeed, under Select's theory, the ISO would be prohibited from ever making any changes that affect market prices because plant owners were not aware of those changes at the time they made a decision to participate in the NYISO-administered markets. Finally, Select asserts that, to the best of its knowledge, the NYISO did not conduct studies to measure the economic impact of the proposed changes on TCC values and, if it did, the analysis performed was not shared with the market participants.<sup>3</sup> Select's claims are factually incorrect and otherwise without merit.

To begin with, Select could not, as an active market participant, have been surprised by the modeling changes. Indeed, Select's own Appeal states that it was aware that the proposed changes to ensure consistency between the Day-Ahead and the Real-Time market were being evaluated during the second half of 2001 and early 2002, because it asked ISO representatives for more information regarding the impacts the modeling changes might have on TCCs.<sup>4</sup> The proposed modeling changes were part of the comprehensive mitigation filing made to FERC on March 20, 2002 and were detailed in the affidavit from Ricardo Gonzales appended thereto.<sup>5</sup> In that filing, the NYISO made it clear that it would correct software limitations that prevented the NYISO software from considering New York City sub-load pockets in order to comply with

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<sup>1</sup> Appeal at 1.

<sup>2</sup> Appeal at 3. Significantly, nowhere in its appeal does Select allege, much less provide evidence, that the information provided by the NYISO was unreliable at the time it was provided.

<sup>3</sup> Appeal at 5.

<sup>4</sup> Appeal at 5.

FERC's directive that NYISO address out-of-merit issues. In addition, the NYISO had conveyed to market participants that, when making this software improvement, it was important that there be consistency in all energy markets.

Moreover, consistent with FERC's directive that the NYISO work through the NYISO stakeholder process, the proposed changes were presented and vetted on several occasions during the first quarter of 2002, including: on January 4, 2002 as part of a presentation to the AMP/ICM Task Force<sup>6</sup>; as part of a presentation by Dr. David Patton to the Business Issues Committee on January 23, 2002<sup>7</sup>; and as part of the presentation regarding the comprehensive mitigation filing made to the Management Committee on February 7, 2002. Dr. Patton's analysis was performed for various weather scenarios and was presented long before the actual changes were made. The comprehensive mitigation filing contains a detailed summary of the stakeholder consultation process the NYISO followed.<sup>8</sup> Given all of this information, market participants clearly were aware that the proposed changes potentially could alter the price levels in New York City, both in the Day-Ahead and Real-Time markets, and therefore would affect TCC values.

There also is no merit to Select's claim that it was not "an immediate necessity" to implement the Day-Ahead modeling changes as part of the NYISO's efforts to execute the transfer of control over In-City transmission, and related necessary model changes, in accordance

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<sup>5</sup> See Affidavit of Ricardo Gonzalez at paragraph 8. ([http://www.nyiso.com/services/documents/filings/mar\\_2002/comprehensive\\_mitigation\\_filing/att4\\_gonzales\\_affidavit.pdf](http://www.nyiso.com/services/documents/filings/mar_2002/comprehensive_mitigation_filing/att4_gonzales_affidavit.pdf)).

<sup>6</sup> See presentation by Ricardo Gonzales at 4. ([http://www.nyiso.com/services/documents/groups/bic\\_amp\\_icm\\_task\\_force/01\\_04\\_02/oper\\_issues\\_actions.pdf](http://www.nyiso.com/services/documents/groups/bic_amp_icm_task_force/01_04_02/oper_issues_actions.pdf)).

<sup>7</sup> See presentation by Dr. Patton at 3. ([http://www.nyiso.com/services/documents/groups/bus\\_issue\\_comm/01\\_23\\_02/compre\\_mitiga\\_filing\\_patton.pdf](http://www.nyiso.com/services/documents/groups/bus_issue_comm/01_23_02/compre_mitiga_filing_patton.pdf)).

<sup>8</sup> See NYISO's March 20, 2002 compliance filing at 5-7.

with FERC orders<sup>9</sup> and that “there was no compelling need to implement the DAM and real-time changes simultaneously.”<sup>10</sup> This argument overlooks the fact that changes implemented only in the Real-Time market could create a discrepancy between the Day-Ahead and Real-Time markets, which could lead to economically unjustified and artificial arbitrage opportunities. NYISO did, in fact, implement the Real-Time model changes sixteen days prior to the Day-Ahead model changes, and just such a discrepancy occurred. Notwithstanding Select’s argument that the consecutive implementation proves that the Day-Ahead changes were unnecessary,<sup>11</sup> arbitrage opportunities created by software differences between the Real-Time and Day-Ahead markets existed between those markets during those sixteen days. The fact that NYISO did not implement the two changes simultaneously reflects only NYISO’s operational and software implementation restrictions and cannot be construed as evidence that the Day-Ahead changes were insignificant or irrelevant.

Select also is incorrect in claiming that the NYISO fundamentally changed the nature of the TCC product sold by implementing the model changes. Select cannot reasonably expect that the NYISO market model will remain unchanged so as to not affect the value of TCCs. Indeed, NYISO has made other significant changes to the model over the course of its existence via the approved stakeholder process and at FERC’s direction.

Finally, and importantly, nowhere in its Appeal does Select claim that the changes the NYISO made adversely affected the process of improving how the underlying physical system is modeled. In fact, Select’s proposal to postpone or remove the modeling changes will be

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<sup>9</sup> Appeal at 4-5.

<sup>10</sup> Appeal at 7.

<sup>11</sup> Appeal at 7.

detrimental to the process. Accordingly, we respectfully request that the Board uphold the Management Committee's decision and deny Select's Appeal.

### **III. CONCLUSION**

The modeling changes that the NYISO implemented were made in accordance with the NYISO stakeholder procedures to address FERC's directive. The NYISO market participants were adequately informed about NYISO's plans to improve the market and were afforded several opportunities to make their opinions regarding the proposed changes known. Moreover, not only is Select's Appeal without merit, Select's remedy could result in re-introducing irrational arbitrage opportunities due to institutionalized separations between the Day-Ahead and Real-Time markets.

For these reasons, Morgan Stanley Capital Group Inc., Consolidated Edison Company of New York, Inc., New York State Electric & Gas Corporation, and Rochester Gas and Electric Corporation respectfully request that the Board of Directors deny Select's Appeal.

Dated: August 1, 2002

Respectfully submitted,



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