UNITED STATE OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Central Hudson Gas & Electric Corporation	**)**	**Docket Nos.**	**ER97-1523-011**
Consolidated Edison Company of New York, Inc.	**)**		**OA97-470-010**
Long Island Lighting Company	**)**		**ER97-4234-008**
New York State Electric & Gas Corporation	**)**		
Niagara Mohawk Power Corporation	**)**	**Docket Nos.**	**ER97-1523-018**
Orange and Rockland Utilities, Inc.	**)**		**OA97-470-017**
Rochester Gas and Electric Corporation and	**)**		**ER97-4234-015**
	)		
New York Power Pool	**)**	**Docket Nos.**	**ER97-1523-019**
			OA97-470-018
			ER97-4234-016
			(not consolidated)

JOINT BRIEF ON EXCEPTIONS OF THE MEMBER SYSTEMS AND THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.

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JOINT BRIEF ON EXCEPTIONS OF MEMBER SYSTEMS AND THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC. TO THE MAY 11, 2001 INITIAL DECISION

Pursuant to Rule 711 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.711 (2000), the Member Systems[1] and the New York Independent System Operator, Inc. ("NYISO") respectfully submit their joint brief on exceptions to the May 11, 2001 Initial Decision ("the Initial Decision") of Presiding Administrative Law Judge William J. Cowan ("the Presiding Judge").[2] As set forth more fully below, the Member Systems and the NYISO take exception to the following limited aspects of the Initial Decision: (1) the finding that NYISO is contractually barred from applying the NYISO marginal loss methodology to the transmission service agreement under Niagara Mohawk FERC Rate Schedule No. 178 between Niagara Mohawk Power Corporation ("Niagara Mohawk") and Sithe/Independence Power Partners, L.P. ("Sithe") ("Sithe TSA") for the ten month locked-in period from NYISO start-up through August 2000 ("the Locked-In Period") and that the marginal loss methodology is not just and reasonable as to this TSA alone; and (2) the requirement that the otherwise appropriate Amendments to the TSA between the Consolidated Edison Company of New York, Inc. ("Con Edison") and the New York City Public Utility Service ("NYCPUS") under Con Edison's FERC Rate Schedule No. 97 ("NYCPUS TSA") must be filed with the New York State Public Service Commission ("the NYSPSC") before they can take effect.

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[1] The Member Systems include: Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc. , LIPA, Orange and Rockland Utilities, Inc., New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, and Rochester Gas and Electric Corporation.

[2] Central Hudson Gas & Electric Corp., et al., 95 FERC ¶ 63,013 (2001) ("Initial Decision").

SUMMARY OF POSITION AND POLICY CONSIDERATIONS

The Presiding Judge erred in failing to evaluate the Member Systems' proposed Amendments to the Sithe TSA and the NYCPUS TSA within the overall context of the restructuring of wholesale electricity markets in New York State of which they are an integral part. With respect to the Sithe TSA, if the Commission affirms the Initial Decision:

- The NYISO would be precluded from applying the same marginal loss provisions to the Sithe TSA that the Commission has approved for the NYISO with respect to every other transmission customer in New York, notwithstanding the Presiding Judge's express finding that the Sithe TSA specifically authorizes Niagara Mohawk to amend all of the rate provisions of that TSA, including loss rates; and

- The NYISO would be required to calculate losses for service under the Sithe TSA for the Locked-In Period on the basis of a control area that ceased to exist with NYISO start-up on November 18, 1999, despite: (1) the absence of any express language in the Sithe TSA purporting to establish this unusual requirement; and (2) the fact that this interpretation of the first sentence of Section 9.1 of the Sithe TSA conflicts with the plain requirements of the second sentence of that provision; and

- Uncontroverted eyewitness testimony -- that Sithe and Niagara Mohawk discussed and specifically agreed that the rate change provision of the Sithe TSA would provide Niagara Mohawk with rate change rights broad enough to accommodate any future change in Commission policy affecting rates, including loss rates and loss methodologies -- would be ignored; and

- Sithe would receive a refund -- estimated by the Member Systems at approximately $4,000,000 -- at the expense of all other transmission customers in the NYCA, despite the fact that: (1) all of the other NYISO customers are already subject to the marginal loss provisions from which Sithe alone would be exempted under the Initial Decision; and (2) Sithe's grandfathered rates for transmission service under the TSA for the Locked-In Period – which the Member Systems did not seek to change – are already substantially below the rates paid by other customers receiving similar levels of service under the Commission-approved NYISO OATT; and

- Evidence would be ignored that: (1) as a result of the restructuring, Sithe had an incentive to and did renegotiate the agreement under which Sithe sells the electricity transmitted under the Sithe TSA to Con Edison; (2) Sithe has been fully reimbursed by Con Edison for this change in loss methodology as a result of renegotiation of the power purchase agreement; and (3) Sithe would, therefore, receive a windfall gain if it alone were exempted from the NYISO loss charge.

With respect to the NYCPUS TSA, Commission acceptance of the Presiding Judge's Initial Decision would result in the elevation of form over substance and a tremendous and unnecessary waste of additional time and resources by all affected parties, including the Commission and the NYSPSC, since ultimately these issues will be determined by this Commission and since the parties to this proceeding have already developed a complete record upon which the Commission should act. Indeed, the Presiding Judge has found that the Amendments are appropriate and that NYCPUS should not be able to avoid the NYISO's charges that are the subject of the Amendments. Thus, no conceivable purpose would be served by sending the parties to the NYSPSC. This elevation of form over substance is directly at odds with the Presiding Judge's own findings that:

- NYCPUS should not be able to avoid the NYISO charges.
- The NYCPUS TSA provides this Commission with the ultimate authority to review and approve unilateral amendments thereto; and
- The issues present here relate to important Commission transmission policies involving the NYISO and are not related to Con Edison's local distribution rates on file at the NYSPSC that are referenced in the NYCPUS TSA.
- The Proposed Amendments were served on the NYSPSC at the commencement of this proceeding; and
- NYCPUS and the NYSPSC have participated in this evidentiary proceeding which has lasted nearly two years; and
- NYSPSC has not opposed the proposed Amendments nor requested that the Commission defer to its judgment on this issue.

BACKGROUND

1. Development of the NYISO

In Order No. 888,[3] the Commission ordered that the members of the former New York Power Pool and members of certain other "tight" power pools file joint pool-wide Final Rule pro forma tariffs and to begin taking service for all pool transactions under those tariffs by December 31, 1996. Order No. 888, at 31,727. The Commission directed that such reformed power pool agreements should establish "open, non-discriminatory membership provisions (including establishment of an [Independent System Operator ('ISO')], if that is a pool's preferred method of remedying undue discrimination." Id.

To assist power pools seeking to become ISOs, the Commission established eleven "ISO Principles" in Order No. 888. Id. at 31,730-32. Two of these principles are of particular relevance to this proceeding: ISO Principle 4 provides, in pertinent part, that an ISO "shall have the primary responsibility in ensuring short-term reliability of grid operations." Id. at 31,731. ISO Principle 8 requires, among other things, that ISOs structure their operations to promote the efficient use of and investment in generation, transmission and consumption:

> An ISO's transmission and ancillary services pricing policies should promote the efficient use of and investment in generation, transmission, and consumption.

Id. at 31,732. On rehearing, the Commission clarified that ISO Principle 8 "allows the use of appropriate locational marginal cost pricing." Order No. 888-A, at 30,251.

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[3] Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services By Public Utilities: Recovery of Stranded Costs By Public Utilities and Transmitting Utilities, FERC Stats. & Regs., [Regulations Preambles 1991-1996] ¶ 31,036 (1996) ("Order No. 888"); order on rehearing, III FERC Stats. & Regs. [Regs. Preambles] ¶ 31,048 (1997) ("Order No. 888-A"); order on rehearing, 81 FERC ¶ 61,248 (1997) ("Order No. 888-B); order on rehearing, 82 FERC ¶ 61,046 (1998) ("Order No. 888-C); aff'd and remanded sub nom.,Transmission Access Policy Study Group et al. v. FERC, 225 F.3d 667 (D.C. Cir. 2000); cert. granted sub nom. New York v. FERC, 69 U.S.L.W. 3574 (Feb. 26, 2001).

On January 31, 1997, the Member Systems filed with the Commission a proposal to establish an ISO and related entities "in order to form a fully competitive wholesale electricity market in New York." Central Hudson Gas & Electric Co., 86 FERC ¶ 61,062 at 61,205. That proposal, as modified and supplemented on December 19, 1997, was conditionally accepted by the Commission in orders dated June 30, 1998 ("the June 30 Order")[4] and January 27, 1999 ("the January 27 Order").[5]

In the June 30 Order, the Commission found that the Member System's restructuring proposal satisfies the requirements of ISO Principle 4.[6] In reaching this conclusion, the Commission noted that the NYISO "will also act as the NERC-defined control area operator" for the bulk power system in New York State.[7]

In the January 27 Order, over the objections of Sithe, the Commission approved the rate design for the NYISO proposed by the Member Systems, including the proposal to shift both the loss component of spot market sales of electricity and all transmission losses from average losses to marginal losses. In accepting this proposal, the Commission expressly accepted the Member Systems' contention that marginal losses provided more accurate and efficient price signals to market participants in competitive markets than average losses:

> Member Systems' express concern that the use of average costs would not accurately reflect the actual cost of losses associated with each transaction. . . . For example, when choosing between two purchase options that have the same input cost except for losses, the buyer will select the one with the lowest marginal losses. When a purchaser makes this choice, the cost of system losses is, in fact, reduced by the marginal losses as computed by Member Systems.

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4 Central Hudson Gas & Electric Corp., 83 FERC ¶ 61,352 (1998).

5 Central Hudson Gas & Electric Corp., 86 FERC ¶ 61,062 (1999).

6 June 30 Order at 62,410-13.

7 Id. at 62,411.

> The use of marginal losses is a significant component of the LBMP pricing method that we approve later in this order. Moreover, the method used to compute the marginal losses is the same method that individual utilities typically use to decide how to dispatch their resources in a manner that minimizes variable costs.

January 27 Order at 61,214.

The Commission went on to expressly reject the notion that any group of customers should be excluded from the uniform application of this marginal loss methodology:

> Member Systems point out that, if a different loss scheme is used for spot market and bilateral transactions, it will create a bias between them, i.e., self scheduled transactions will be preferred when average losses are lower than marginal losses and spot market transactions will be preferred when marginal losses are lower than average losses. We agree that losses for all transmission services, whether accomplished through a spot market transaction or a self-scheduled bilateral transaction, must be consistent.

January 27 Order at 61,214 (emphasis supplied).

As an integral part of this comprehensive restructuring process, the Member Systems also proposed in their January 31, 1997 filing to revise all of their pre-existing transmission service agreements to include the provisions of the NYISO's Open Access Transmission Tariff ("OATT") providing for the recovery by the NYISO of its costs of acquiring the ancillary services and losses associated with the transmission services under those agreements along with a pro rata share of the residual revenue requirements of the Power Authority of the State of New York ("NYPA"), which are collected through the NYPA Transmission Adjustment Charge ("NTAC"). In the January 27 Order, the Commission declined to approve tariff provisions generically amending the Member Systems' grandfathered agreements with third parties and

directed the Member Systems to file under Section 205 or 206 of the Federal Power Act, 16 U.S.C. 824d or 824e (1994), as appropriate, to implement those changes.[8]

2. The Amendments

In accordance with the January 27 Order, the Member Systems filed certain limited amendments ("Amendments") to 41 grandfathered TSAs in August and November of 1999. The Amendments were designed to harmonize those TSAs with the fundamental change in the structure of the transmission industry in New York resulting from the formation of the NYISO. The proposed Amendments did not propose to change any of the rates that the customers under those grandfatherd TSAs were required to pay to the Member Systems. Instead, the Amendments only seek to require grandfathered customers to reimburse the NYISO for its new services according to the same rates, terms and conditions which the Commission has previously found to be just and reasonable for customers served under the NYISO OATT.

Notably, the Member Systems also proposed, and the Commission approved, the same amendments to their own transmission agreements between and among the various Member Systems to incorporate all of these same requirements.[9]

3. Procedural History

The Commission accepted these Amendments for filing and set this matter for hearing in orders dated September 30, 1999 and January 14, 2000.[10] An evidentiary hearing was held in these proceedings on September 19-22 and 27-28, 2000.

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[8] January 27 Order at 61,218.

[9] Central Hudson Gas & Electric Corp., et al., Letter Order issued in Docket Nos. ER97-1523-008, et al. (Aug. 19, 1999).

[10] Central Hudson Gas & Electric Corp., et al., 88 FERC ¶ 61,306 (1999), reh'g denied, 90 FERC ¶ 61,042 (2000).

Prior to the hearing, the Member Systems submitted twelve full or partial settlements reducing the scope of the issues to be resolved at hearing. During the course of the hearing, two additional settlements were reached. Subsequent to the hearing, the Member Systems filed three additional settlements, bringing the total number of full or partial settlements to seventeen.

4. The Initial Decision

On May 11, 2001, the Presiding Judge issued the Initial Decision.[11] In the Initial Decision, the Judge approved the application of the Amendments proposed by the Member Systems to all of the TSAs still at issue in these proceedings except two: the Sithe TSA and the NYCPUS TSA. Sithe only contests the application of the Member Systems' marginal loss proposal to service under the Sithe TSA during the Locked-In Period. With respect to this narrow issue, the Presiding Judge found that Niagara Mohawk was contractually barred from filing the Amendments under Section 205,[12] that the Member Systems' request for relief under Section 206 of the FPA was moot,[13] and that the Member Systems had not met their burden of demonstrating that the Amendments were just and reasonable as applied to that rate schedule.[14]

With respect to the NYCPUS TSA, the Presiding Judge found the Member Systems' proposed Amendments to be in all respects just and reasonable and concluded that NYCPUS should not be able to avoid these charges.[15] However, despite this finding, he also concluded that the NYISO was contractually barred from recovering these costs from NYCPUS unless Con Edison first filed the Amendments with the NYSPSC for its action prior to submitting them to

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11 See n.1 *supra.*

12 Initial Decision, at 65,158-60.

13 Initial Decision, at 65,164.

14 Initial Decision, at 65,162-64.

15 Initial Decision at 65,181-82; 65,183-84.

the Commission;[16] and, therefore, the Presiding Judge rejected the Amendments to the NYCPUS TSA.[17]

SPECIFIC EXCEPTIONS AND SPECIFICATION OF ERRORS OF FACT AND LAW

Pursuant to Rule 711 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.711 (2000), the Member Systems and the NYISO take exception to three aspects of the Initial Decision and enumerate the associated errors of fact and law as follows:

1. The Presiding Judge erred in ruling that, as a matter of law, Niagara Mohawk was contractually barred from amending the TSA to incorporate the marginal loss provisions of the NYISO OATT.

2. The Presiding Judge erred in ruling that the Member Systems and the NYISO had failed to demonstrate that the marginal loss provisions of the NYISO OATT were just and reasonable as applied to the Sithe TSA.

3. The Presiding Judge erred in concluding, as a matter of law, that the NYCPUS TSA precludes the otherwise proper Amendments to that Commission jurisdictional TSA from becoming effective until they are first filed with the NYSPSC for acceptance or approval.

ARGUMENT

I. THE JUDGE ERRED IN CONCLUDING THAT, AS A MATTER OF LAW, THE SITHE TSA REQUIRES THE NYISO TO CALCULATE SITHE'S TRANSMISSION LOSSES ON THE BASIS OF A CONTROL AREA THAT CEASED TO EXIST WHEN THE NYISO COMMENCED OPERATION

The Presiding Judge begins his analysis of the proposed Amendments to the Sithe TSA by conceding, as he must, that Section 8.1 of the Sithe TSA "clearly and unambiguously gives Niagara Mohawk the right to unilaterally make application to the Commission for a change in rates under Section 205." Initial Decision, at 65,159.[18] However, the Presiding Judge then went

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16 Initial Decision at 65,184-85.

17 Initial Decision at 65,185.

18 Section 8.1 of the Sithe TSA provides, in pertinent part, that:

on to find that Section 9.1 of the Sithe TSA "clearly and unambiguously envisions a particular means of determining compensation for losses" pursuant to which "losses incurred or avoided will be determined with reference to Niagara Mohawk and its control area." Id. Because Section 14.1 of the Sithe TSA bars any changes to that agreement (other than to Sections 4, 7 and 8) except with the mutual consent of the parties, the Presiding Judge concluded that "[t]here is no avenue within the four corners of the contract that would permit the unilateral filing of changes to non-rate terms and conditions of service…." Id.

This conclusion is clearly erroneous for a number of reasons. First, the Presiding Judge failed to give effect to the express language of Section 8.1 of the Sithe TSA which unambiguously provides Niagara Mohawk with full rate change rights and allows Niagara Mohawk to unilaterally submit to the Commission any "change in rates" notwithstanding any other provision to the contrary. Second, the Presiding Judge failed to consider Commission precedent interpreting such rate change language.

Third, the Presiding Judge adopted an unwarranted and inappropriate interpretation of the first sentence of Section 9.1 of the Sithe TSA that requires the NYISO to calculate losses on the basis of a control area that ceased to exist with NYISO start-up on November 18, 1999, despite the absence in that provision of any language expressly requiring this unusual result and despite the fact that the second sentence of Section 9.1 expressly requires that Sithe's losses be calculated in the same manner used for other similar transactions.

Fourth, the Presiding Judge refused to consider the uncontroverted eyewitness testimony of Niagara Mohawk witness Clement E. Nadeau that he specifically discussed this issue with his

(..continued)

Nothing contained herein shall be construed as affecting in any way Niagara Mohawk's right under this rate schedule to unilaterally make application to the . . . Commission . . . for a change in rates under Section 205 of the Federal Power Act . . . .

Initial Decision, at 65,156 n.9 (citation omitted).

counterparts at Sithe during the negotiation of the Sithe TSA, and the parties agreed that the provisions of the Sithe TSA would place no limits on Niagara Mohawk's unilateral rate change rights, including with respect to loss rates. The Presiding Judge's refusal to even consider this testimony is in direct conflict with his own prior orders, as well as those of the Commission, concluding that such evidence was required to properly evaluate the claims that the Member Systems were contractually barred from unilaterally filing to amend the Sithe TSA and certain other TSAs at issue in this case. Finally, the Presiding Judge also erred in failing to apply established principles of New York law in interpreting the Sithe TSA.

A. As A Matter of Law, The Sithe TSA Authorizes Niagara Mohawk To Make Any Just And Reasonable Change To Transmission Loss Rates

As previously noted, Section 8.1 of the Sithe TSA expressly provides that:

> Nothing contained herein shall be construed as affecting in any way . . . Niagara Mohawk's right under this rate schedule to unilaterally make application to the Federal Energy Regulatory Commission . . . for a change in rates under Section 205 of the Federal Power Act . . . .

Ex. MS-3, Schedule E at 19 (emphasis supplied).

The Presiding Judge, having concluded this to be a rate change, this provision expressly provides that no other provision of the Sithe TSA may be construed as precluding Niagara Mohawk from unilaterally proposing that change in rates. However, the Presiding Judge totally ignored this language and found that, as a matter of law, the TSA unambiguously requires another provision of the TSA to take precedent over Niagara Mohawk's rate change rights.

The Presiding Judge's ruling is not only at odds with the plain language of the Sithe TSA, it also is at odds with Commission precedent interpreting such rate change language. Surprisingly, the Presiding Judge failed to even address this precedent in the portion of the Initial

Decision explaining his reasons for concluding that Niagara Mohawk was contractually barred from unilaterally filing to incorporate the marginal loss provisions of the Sithe TSA.

In Niagara Mohawk Power Corporation, 75 FERC ¶ 61,087 (1996) ("Watertown"), the Village of Watertown, New York ("Watertown") claimed that, in its TSA with Niagara Mohawk ("the Watertown TSA"), "the parties expressly agreed to [kilo]watt hour metering and billing."[19] In rejecting Watertown's claim that the method of metering and billing were "non-rate provisions" beyond the scope of Niagara Mohawk's rate change rights, the Commission first quoted the express provisions of Section 2.1 of the Watertown TSA, which were strikingly similar to the provisions of the Sithe TSA at issue in this case:

> Section 2.1 of the agreement between Niagara Mohawk and Watertown provides in relevant part that:
>
> Beginning on January 1, 1996, and on each January 1 of every fifth year thereafter, NIAGARA shall update the rate contained in Attachment II to reflect the then current cost of service. Except as provided in the immediately preceding sentence, nothing contained herein shall be construed as affecting in any way the right of NIAGARA to unilaterally make application to . . . FERC for a change in the transmission service rates under [S]ection 205 of the Federal Power Act.

75 FERC ¶ 61,087, at 61,262 (emphasis in original).

The Commission found that the meaning of this provision was clear:

> As quoted above, [the Watertown TSA] states 'except as provided in the immediately preceding sentence,' - - the update - - Niagara Mohawk may file for a rate change under [S]ection 205 of the FPA. Niagara Mohawk legitimately exercised its contractual right to seek the new billing method.

[19] Motion to Intervene, Protest, Motion to Reject and Answer to Request for Blanket Waiver and Alternate Motions for Five Month Suspension, Summary Disposition and Hearing of the City of Watertown, New York, Niagara Mohawk Power Corporation, Docket No. ER96-225-000, at 22 (filed Dec. 1, 1995).

Id. (footnote omitted). The Commission went on to expressly reject Watertown's claim that this rate change right was limited by the non-rate provisions of the Watertown TSA cited by Watertown:

> For this reason, Watertown's remaining references (Protest at 21-22) to other provisions of its power purchase agreement and transmission service agreement with Niagara Mohawk do not undermine Niagara Mohawk's 'unilateral' ability under [S]ection 2.1 to apply for a 'change in the transmission service rates,' as long as such a proposed change is not inconsistent with its obligation to 'update' its cost of service every five years.

Id. at 61,262 n.3.

Although the Presiding Judge noted the Member Systems' citation to the Watertown case in the portion of his Initial Decision summarizing the positions of the parties,[20] he failed to even mention that case in his discussion of his reasons for concluding that Niagara Mohawk was contractually barred from amending the Sithe TSA to incorporate the marginal loss provisions of the NYISO OATT. Instead, as previously noted, the Presiding Judge improperly concluded that a proposed change that clearly constituted a "change in rates," when viewed in isolation,[21] was nonetheless contractually precluded because it conflicted with the non-rate provisions of Section 9.1 that agreement. The Presiding Judge failed to give effect to the express language of Section 8.1 quoted above and the Commission's interpretation of a similar contractual provision in the Watertown case.

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[20] Initial Decision, at 65,156. The claims of Staff and Sithe that Watertown does not involve a conflict between the exercise of Niagara Mohawk's rate change rights and the "non-rate" provisions of the Watertown TSA cannot be reconciled with the Commission's express rejection of precisely this claim in footnote 3 of the Watertown case. See Niagara Mohawk Power Corporation, 75 FERC ¶ 61,087, at 61,262 n.3.

[21] See, e.g., PacifiCorp, 84 FERC ¶ 61,303 at 62,393 ("We agree with Trial Staff that transmission losses are a component of overall transmission rates. . . . ").

B. The Presiding Judge Erred In Finding That The Provisions Of Section 9.1 Of The TSA Unambiguously Require The NYISO To Calculate Losses For The Sithe TSA On The Basis Of A Control Area That Ceased To Exist At The Time Of NYISO Start-Up

Even in the absence of the unambiguous language of Section 8.1 of the Sithe TSA precluding any other provision of that agreement from limiting Niagara Mohawk's rate change rights, the Presiding Judge's conclusion that Section 9.1 precludes Niagara Mohawk from applying the loss provisions of the NYISO OATT to the Sithe TSA would be clearly erroneous. Section 9.1 of the Sithe TSA, which the Presiding Judge fails to quote in the Initial Decision, provides that:[22]

> PRODUCER shall compensate NIAGARA MOHAWK for losses incurred by NIAGARA MOHAWK in its control area and NIAGARA MOHAWK shall compensate PRODUCER for losses avoided by NIAGARA MOHAWK in its control area as a result of NIAGARA MOHAWK's provision of transmission services hereunder. The determination of such losses and the procedure for compensation thereof shall be determined by NIAGARA MOHAWK's Power Control Department in accordance with NIAGARA MOHAWK's practices relating to other similar transactions and in accordance with GOOD UTILITY PRACTICE.

Ex. MS-3, Schedule E at 19.

In applying this contract provision to the facts of this case, the Commission must recognize the unique and unforeseeable circumstances in which the parties now find themselves as the result of the comprehensive restructuring of markets for wholesale electricity in New York State resulting from the formation of the NYISO: As all parties agree, at no time during the Locked-In Period has Niagara Mohawk operated a control area of its own, as it did prior to that time.[23] Instead, as a result of the formation of the NYISO, and in conformance with the

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[22] These types of unforeseen changed circumstances are exactly what lead the parties to include contract language pressing the supremacy of the rate change rights.

[23] Tr. at 610, lines 6-9; Ex. MS-3 at 21, lines 5-17; Ex. MS-9, Schedule N.

requirements of the Commission's ISO Principle 4, Niagara Mohawk has turned over control of its bulk power transmission facilities to the NYISO, which has operated those facilities on an integrated basis with all other bulk power facilities in New York State since that time. Ex. MS-3 at 7, lines 6-20 As a result of these changes – which could not possibly have been foreseen under the Sithe TSA which was negotiated in 1992 – transmission losses on the bulk power facilities previously included in Niagara Mohawk's control area are now incurred by the NYISO and not by Niagara Mohawk. Ex. MS-3 at 20, lines 31-34; 21 line 1. See also MS-3 at 8, lines 12-14. Because of its not-for-profit status, the NYISO must recover all of the costs of these losses either from Sithe or from the other transmission customers it serves.[24]

In such circumstances, the only reasonable interpretation of the first sentence of Section 9.1 of the Sithe TSA with respect to transmission service provided after NYISO start-up on November 18, 1999 is that the term "Niagara Mohawk's control area," as used therein, should be construed to refer to the only control area of which Niagara Mohawk's transmission facilities are now a part. Since November 18, 1999, Niagara Mohawk has been a part of only one control area: the New York Control Area operated by the NYISO. Thus, far from prohibiting Niagara Mohawk from calculating losses under the Sithe TSA on the basis of the NYCA as a whole, this provision actually requires that result.

This interpretation of the first sentence of Section 9.1 of the Sithe TSA also avoids a conflict with the requirement of the second sentence of Section 9.1. That sentence provides that Sithe's transmission losses must be calculated "in accordance with NIAGARA MOHAWK's practices relating to other similar transactions," all of which have been subject to the marginal loss provisions of the NYISO OATT at all times subsequent to November 18, 1999.

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[24] NYISO Open Access Transmission Tariff at Original Sheet Nos. 514-515; See also Tr. at 592, at lines 2-23.

Although the Presiding Judge clearly rejected this reasonable interpretation of the Sithe TSA, it is impossible to tell from the Initial Decision precisely why he believes that the Sithe TSA "clearly and unambiguously envisions" some other result or specifically what he believes that other result to be. To the extent that the Initial Decision concludes that Niagara Mohawk's transmission losses associated with service under the Sithe TSA on and after NYISO start-up on November 18, 1999 may only be calculated on the basis of a control area that ceased to exist as of that date, the Member Systems and the NYISO submit that there is nothing in the language of Section 9.1 – or any other provision of the Sithe TSA – that would support that conclusion in any way. In the absence of an explicit agreement among the parties specifically providing for this unlikely result, the Commission should not blithely assume that the parties intended for loss rates to be set on any basis other than the actual losses incurred in the actual control area in which the services in question were provided. This is particularly true where, as in this case, the utility has retained the broadest possible rate change rights and seeks to use those rights to base its loss rates on actual costs.

The Presiding Judge's conclusion that the Sithe TSA requires Niagara Mohawk to calculate losses for Sithe on and after NYISO start-up on November 18, 1999 on the basis of a control area that ceased to exist on that date must also be rejected because it conflicts with the express requirement of the second sentence of Section 9.1 of the Sithe TSA. That sentence provides, in pertinent part, that losses for service under the Sithe TSA must be calculated "in accordance with NIAGARA MOHAWK's practices relating to other similar transactions." Ex. MS-3, Schedule E at 19. This provision of the Sithe TSA is just as valid and binding as the provisions of the first sentence of Section 9.1 referring to Niagara Mohawk's control area.

As previously noted, transmission losses for all other transmission customers using Niagara Mohawk's facilities on and after NYISO's start-up on November 18, 1999 have been and continue to be determined in accordance with the marginal loss provisions of the NYISO OATT. Thus, as the Member Systems have repeatedly pointed out,[25] the second sentence of Section 9.1 can only be satisfied if losses under the Sithe TSA are also calculated on that basis. Because the Member Systems' interpretation of Section 9.1 is the only interpretation of that provision that harmonizes the requirements of both sentences in that section of the Sithe TSA, the Presiding Judge's rejection of that interpretation was clearly erroneous.

C. The Presiding Judge Erred In Refusing To Even Consider The Uncontroverted Eyewitness Testimony Of Niagara Mohawk Witness Clement E. Nadeau Conclusively Establishing That The Parties To The Sithe TSA Specifically Intended To Preserve All Of Niagara Mohawk's Rate Change Rights

While the Member Systems and the NYISO believe that the rate change provisions of Section 8.1 of the Sithe TSA are clear on their face in authorizing Niagara Mohawk to unilaterally file this change in transmission loss rates and that the only reasonable interpretation of Section 9.1 of that agreement is that losses must be calculated on the basis of the only control area in which Niagara Mohawk's transmission facilities are located, still the Member Systems and the NYISO recognize that the Commission has determined that a hearing is required to more closely determine the meaning of the provisions. Under New York law, the existence of ambiguous or conflicting contract clauses creates a contested issue of material fact concerning the intentions of the parties to be resolved by an evidentiary hearing. See, e.g., Arthur Glick Truck Sales, Inc. v. General Motors Corp., 865 F.2d 494, 498 (2d Cir. 1989) ("Glick has, at the very least, raised a genuine issue of material fact as to whether Article 1.5 of this form document

[25] Ex. MS-3 at 19-20; Ex. MS9 at 6-7.

permits discontinuance of individual models but not of entire product lines."). In this case, the Commission has already had the benefit of the evidentiary hearing required in the Glick case.

At that hearing, the Member Systems were the only parties to present testimony from an actual participant in the negotiation and execution of the Sithe TSA concerning the intentions of the parties with respect to the interplay of these two provisions. Specifically, Niagara Mohawk witness Clement E. Nadeau testified that he was the executive at Niagara Mohawk responsible for negotiating the Sithe TSA and that he personally discussed the interplay between these two provisions with Mr. Pat Jones, the executive at Sithe's predecessor, Lake View, Inc., responsible for this agreement.

Mr. Nadeau testified that he clearly recalled the negotiations he had conducted with Mr. Pat Jones of Lake View, Sithe's predecessor, in which Mr. Nadeau expressly rejected Mr. Jones' proposals to fix either the loss rate or the loss methodology to be used under the Sithe TSA:

> I told you that we explained to Sithe. Soon after that, Mr. Jones came into my office looking for us to fix the numbers. We said we could not fix the number, we could not fix the methodology. Unfortunately, we could not change the language. That was exactly what he was looking for - - to commit first to a fixed number, second to a methodology. We could not do either.
>
> Q. What did you do for him?
>
> A. Unfortunately, on this issue, we could not do anything.[26]

Mr. Nadeau further testified that Mr. Jones ultimately accepted and agreed to Mr. Nadeau's position in exchange for concessions from Niagara Mohawk on other issues:

> The parties ultimately compromised this and other disagreements in reaching the final agreement embodied in Rate Schedule 178. As part of this compromise, Lake View [Sithe's predecessor] agreed that Niagara Mohawk would retain unilateral right to file changes to the transmission charges and loss rates established in

[26] Tr. at 1302, lines 9-15.

> that TSA and that no other provision of that TSA could be construed as limiting those rate change rights.

Ex. No. MS-9 at 6, lines 6-11 (emphasis in original).

It is, therefore, not surprising that Sithe was unable to introduce testimony by any participant in the negotiation of its TSA with Niagara Mohawk to contradict any of Mr. Nadeau's statements. In fact, no other party presented evidence disputing Nadeau's eyewitness account of the negotiation of the Sithe TSA. Staff admitted in its Initial Brief to the Presiding Judge that Mr. Nadeau was a forceful and credible witness whose testimony on issues concerning the Sithe TSA should be given "controlling weight":

> The agreement was negotiated by Niagara Mohawk personnel who reported to Mr. Nadeau and Mr. Nadeau had ultimate responsibility over whether the agreement was acceptable to Niagara Mohawk. Tr. at 1610. Under these circumstances, Staff submits that the views of Mr. Nadeau concerning what constitutes reasonable cause to refuse consent to an assignment should be accorded controlling weight.

Staff Initial Br. at 25, n.41.

The Presiding Judge's refusal to even consider this compelling evidence of the parties' understanding and intent in executing the Sithe TSA was clearly erroneous, particularly in light of the Commission's and the Presiding Judge's prior rulings concerning the need for precisely this type of evidence to resolve the issues in this case. The Presiding Judge based his refusal to consider Mr. Nadeau's testimony on the ground that, as a matter of law, the Sithe TSA is so clear on its face that no extrinsic evidence may be considered in interpreting its provisions. This claim cannot be reconciled with either the Commission's January 14, 2000 Order Denying Rehearing of its September 30, 1999 order accepting for filing the Member Systems' proposed Amendments in Central Hudson Gas & Electric Co., 90 FERC ¶ 61,042 (2000), or the Presiding Judge's own Order on Legal Issues dated April 25, 2000.

In the Order on Rehearing, the Commission expressly rejected the claims of Sithe and certain other parties that their TSAs were was so clear on their face that there was no need for a hearing to determine whether Niagara Mohawk was contractually precluded from unilaterally filing under Section 205 of the FPA to amend those agreements:

> There was good reason for the Commission to set this case, including any Mobile-Sierra issues, for hearing. A hearing provides a forum in which to conduct the intricate legal and factual examinations that need to be done to decide whether the Mobile-Sierra doctrine, in fact, applies. Each of the 37 contracts at issue in this proceeding thus needs to be individually and carefully examined as to whether it allows or prevents modifications such as those proposed here.

90 FERC ¶ 61,042 at 61,196.

Similarly, in his Order on Legal Issues, the Presiding Judge recognized that these contractual issues could not be resolved on the face of any of those TSAs, including the Sithe TSA and, consequently, that a hearing was required to develop the record required to determine the meaning of these contract provisions:

> In my judgment, the Commission's decision proved wise in that these issues, while "legal" in the broad sense, are so imbued with factual disputes and so dependent upon factual context that they should not be considered in a vacuum occupied only by briefs and argument. This will no doubt disappoint the parties seeking summary determinations, but it would be unwise to rush to a judgment on these issues when they can be better developed and explained in an evidentiary hearing where intent, implications, benefits and detriments can be examined carefully.

Order on Legal Issues, slip op. at 4.

In reliance on these orders, the Member Systems, the NYISO and the other parties to this proceeding, including Sithe, expended significant resources in providing the Commission with the "intricate legal and factual" analyses required to "individually and carefully" examine each of the TSAs at issue in this case, including the Sithe TSA. The Presiding Judge's decision to

ignore this factual record in its entirety and to belatedly decide that the Sithe TSA is so clear on its face that the Commission is precluded by law from considering any extrinsic evidence in determining the meaning of that provision is flatly inconsistent with these prior rulings and therefore clearly erroneous.

D. The Presiding Judge Erred In Failing To Give Precedence To Niagara Mohawk's Rate Change Rights Under Section 8.1 Of The Sithe TSA

In the unlikely event that the Commission concludes that there is a direct conflict between Sections 8.1 and 9.1 of the Sithe TSA and that there is no credible extrinsic evidence to assist the Commission in discerning the intentions of the parties, the Commission must apply the simple rule of construction used by New York courts in such circumstances: the clause first appearing in the contract must be given effect at the expense of the second clause. See, e.g., Honigsbaum's Inc. v. Stuyvesant Plaza, Inc., 178 A.D.2d 702, 704 (3d Dept. 1991) ("[I]n the case of total repugnancy between two contract clauses, the first of such clauses shall be received and the subsequent one rejected.").

In this case, Section 8.1 of the Sithe TSA preserving Niagara Mohawk's full rate change rights precedes both Sections 9.1 and 14.1 of that TSA, upon which the Presiding Judge relied in reaching his conclusion. Accordingly, to the extent that the Commission accepts the Presiding Judge's suggestion to ignore not only the express language of both Section 8.1 and 14.1 of the Sithe TSA preserving Niagara Mohawk's full rate change rights but also the compelling and uncontroverted eyewitness testimony of Niagara Mohawk witness Clement E. Nadeau that the parties specifically intended those provisions to reserve Niagara Mohawk's full rate change rights, the Commission must still give effect to Niagara Mohawk's rate change rights under

Section 8.1 rather than to the provisions of Section 9.1 or the provisions of Section 14.1 for the simple reason that Section 8.1 precedes both of those other provisions in the Sithe TSA.[27]

II. THE PRESIDING JUDGE ERRED IN CONCLUDING THAT THE MEMBER SYSTEMS AND THE NYISO FAILED TO SHOW THAT THE APPLICATION OF THE NYISO MARGINAL LOSS METHODOLOGY TO THE SITHE TSA WAS JUST AND REASONABLE

The Presiding Judge also concluded that the Member Systems' proposed change to the Sithe TSA should be rejected because the Member Systems and the NYISO failed to demonstrate that this change was just and reasonable as required by Section 205 of the FPA.[28] The Presiding Judge reached this conclusion for three basic reasons. First, he erroneously characterized the Member Systems' and NYISO's position as relying exclusively on the theory that "the Commission's approval of the marginal loss methodology as contained in the NYISO OATT [shifts] the burden of proof to parties seeking to justify departures from the Commission-approved marginal cost methodology." Initial Decision, at 65,162. Second, he concluded that because marginal losses exceed total losses, and because Sithe is exempted from the NYISO Schedule 1 charge against which any overrecovery of total losses is credited under the NYISO OATT, Sithe "is likely to be charged amounts greater than actual loss costs and is without a means to share in the distribution of the overcollection." Id. at 65,163. Finally, the Presiding Judge concludes that any alleged benefits received by Sithe, including reimbursement from Con Edison for Sithe's marginal loss payments, as a result of this restructuring process are simply not

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[27] To the extent the Presiding Judge's ruling is affirmed and Niagara Mohawk's control area must be fictitiously reconfigured, the Member Systems pointed out to the Presiding Judge in the post-hearing briefs that there would be no contractual preclusion from utilizing and applying the NYISO's marginal loss methodology to losses calculated for that reconfigured control area. The Presiding Judge failed to consider or to even address this position in the Initial Decision. See Joint Reply Brief of Member Systems and the NYISO at 57-58.

[28] Initial Decision, at 65,169-71.

relevant to determining whether the Member Systems' proposal is just and reasonable. Id. at 65,163-64. These determinations are clearly erroneous for the following reasons.

A. The Presiding Judge Erred In Mischaracterizing The Position Of the Member Systems and the NYISO And Ignoring Uncontroverted Evidence That Sithe's Total Payments Under The Sithe TSA Are In Fact Substantially Lower Than The Rates Sithe Would Have Paid For Similar Service Under The NYISO OATT

The Presiding Judge's claim that the Member Systems and the NYISO made no effort to demonstrate that the overall rates that Sithe would pay under the Sithe TSA if the Amendments were approved were just and reasonable is simply not true. Niagara Mohawk witness Nadeau stated in his Direct Testimony that the revenues that Niagara Mohawk received under the Sithe TSA and fourteen other TSAs "are substantially below the revenues that Niagara Mohawk would receive for similar service furnished under the rates accepted by the Commission for service under the NYISO OATT." Ex. MS-3 at 9, lines 20-24. As previously noted, the Member Systems did not propose any change in Sithe's payments to Niagara Mohawk under the Sithe TSA.

In his rebuttal testimony, Mr. Nadeau specifically calculated that as a result of the Member Systems' decision not to change the grandfathered rates contained in the Sithe TSA to the Commission-approved rates applicable to service under the NYISO OATT, Sithe's charges for transmission service were reduced from $33,511,716 per year to only $18,113,681 per year. Id. at 13, lines 25-27. This represents a savings of over $15,000,000 on an annual basis over the transmission service charge component of the NYISO OATT rates which the Commission has been found to be just and reasonable.

In such circumstances, it would plainly be appropriate to require Sithe to compensate the NYISO for its fair share of all of the expenses incurred by the NYISO in providing transmission

services under the Sithe TSA on the same terms and conditions as all other transmission customers in New York State. In actual fact, Sithe has also been exempted from all of the NYISO ancillary services charges (other than losses) and has also been exempted from the NTAC. See May 16, 2000 Settlement, Docket No. ER97-1523-045, et al., approved by Letter Order issued Sept. 18, 2000. Thus, far from being burdened relative to other market participants as the Presiding Judge erroneously found, Sithe, one of the largest transmission customers in the NYCA, has in fact received a substantial advantage as a direct result of both its exemption from these ancillary service and NTAC charges and the reduced payments to Niagara Mohawk under its grandfathered TSA.

The Presiding Judge's decision that Sithe should also be relieved of the obligation to compensate the NYISO for the losses associated with its transmission service on the same basis as all other market participants who do not receive the benefits accorded to Sithe -- and that the roughly $4,000,000 cost of that exemption should be transferred to the NYISO's other customers who are already paying higher rates than Sithe -- is clearly erroneous. This is particularly true in light of: (1) the Commission's previous determination that marginal losses accurately reflect the losses that would actually be avoided if Sithe's transmission service was curtailed,[29] (See also Ex. MS-9 at 20, lines 2-8); and (2) Mr. Nadeau's uncontroverted testimony that the transmission service provided under the Sithe TSA imposed actual losses on the NYISO that were substantially above system average losses, due to both the extreme length of the transmission path and the fact that this service crosses New York's frequently congested Total East Interface. Ex. MS-12 at 7, lines 1-15.

[29] January 27 Order, at 61,214 ("[W]hen choosing between two purchase options that have the same input cost except for losses, the buyer will select the one with the lowest marginal losses. When a purchaser makes this choice, the cost of system losses is, in fact, reduced by the marginal losses as computed by [the] Member Systems."). Id.

The Presiding Judge's failure to consider this uncontroverted evidence of the overall impact of the amended TSA on Sithe in the broader context of the restructuring of New York's wholesale markets for electric power is particularly troublesome in light of the fact that the Presiding Judge expressly affirmed the appropriateness of determining the reasonableness of the Amendments at issue in these proceedings on the basis of such rate comparisons in another part of the Initial Decision. In rejecting the claims of the Municipal Electric Utilities Association ("MEUA") that the Member Systems and the NYISO could only meet their burden of proving those Amendments to be just and reasonable by submitting a comprehensive cost-of-service analysis, the Presiding Judge concluded that:

> I also reject MEUA's argument that a complete Section 205 filing, with full cost and revenue support, is required to show that the proposed charges are just and reasonable. In Central Hudson, at p. 61,212, the Commission authorized use of previously determined revenue requirements to design the Transmission Service Charge, noting that it had done so in approving similar ISO tariffs proposed by PJM and NEPOOL. In the light of this precedent, additional fact-finding on the cost and revenues underlying the proposed TSA changes for specific utilities would be burdensome and unnecessary. It is clear that the Commission is willing to use existing information to simplify and facilitate the transition to new transmission market regimes.

Initial Decision, at 65,171.

B. The Presiding Judge Erred In Failing To Evaluate the Reasonableness Of the Member Systems' Proposal In Light Of The Overall Restructuring Of New York Markets Of Which It Is An Important Part

Recognizing that their proposed changes to the Sithe TSA were fully consistent with the overall restructuring of New York markets for wholesale electricity, the Member Systems and the NYISO also urged the Presiding Judge to determine the reasonableness of those changes in light of that broader restructuring. Specifically, the Member Systems and the NYISO demonstrated that as a result of this comprehensive restructuring process, Sithe had an incentive

to restructure its power purchase agreement, and the power purchase agreement under which Sithe sold the electricity transported under the TSA to Con Edison was indeed restructured to reflect the marginal loss methodology established in the NYISO OATT. Ex. MS-7 at 15, lines 22-24; 16, lines 1-8. As a result of this change, the uncontroverted testimony of Dr. Scott Harvey, a witness for the Member Systems and the NYISO, established that Sithe was fully reimbursed by Con Edison for the increase in costs resulting from the imposition of marginal losses on service under the TSA, on a dollar for dollar basis. Ex. MSI-6 at 3, lines 8-12 ("My point has been only that the marginal losses charge that Sithe pays for transmission service is determined using the same LBMP price that was used to determine payments to Sithe under the Con Edison PPA. As a result, increases in the charge for losses between Independence and Pleasant Valley also increased the LBMP price that was used to determine payments to Sithe under the Con Edison PPA."); See also, Ex. MSI-5 at 10, lines 2-11; 11, lines 1-21; 13, line 14-21. In such circumstances, Sithe would obtain an unfair windfall at the expense of other market participants if it were allowed to take advantage of this comprehensive restructuring process to increase the prices at which it would sell to Con Edison while at the same time refusing to pay to NYISO loss charges for which it has been fully reimbursed. [30]

The Presiding Judge refused to evaluate the Member Systems' proposal in this broader context, asserting without explanation that this contention "fails as probative evidence of justness and reasonableness of the new methodology, as compared to the old, under [S]ection 205." Initial Decision, at 65,163. The Presiding Judge' narrow approach to Section 205 ignores the broader context in which these changes are proposed and is likely to impede rather than foster the restructuring process. The fundamental objective of the Commission's reasonableness

[30] This is particularly odd since the Presiding Judge recognized that Sithe has maintained that the Sithe TSA had to be read in conjunction with the Con Edison PPA.

determination is to ensure that rates are fair to both the transmission provider and the transmission customer. The Presiding Judge has not identified any reason why this fundamental fairness test should be limited to the specific facts of the transmission agreement where, as here, the record clearly establishes that the proposed change is part of a broader comprehensive restructuring process that benefits the transmission customer in other ways. Moreover, in reaching this conclusion, the Presiding Judge also ignored the Commission's determination in the January 27 Order that the overall efficiency objective of the comprehensive restructuring of New York's wholesale markets for electricity would be imperiled if any market participant were exempted from this marginal loss methodology:

> Member Systems point out that if a different loss scheme is used for spot market and bilateral transactions, it will create a bias between them, i.e., self-scheduled transactions will be preferred when average losses are lower than marginal losses and spot market transactions will be preferred when marginal losses are lower than average losses. We agree that losses for all transmission services whether accomplished through a spot market transaction or a self-scheduled bilateral transaction, must be consistent.

January 27 Order, at 61,214 (emphasis supplied).[31] For both these reasons, the Presiding Judge's refusal to consider the Amendments to the Sithe TSA in this broader context was clearly erroneous.

[31] The Presiding Judge's finding that Sithe had a limited ability to respond to price contracts because of its inflexible contract during the locked-in period (Initial Decision at 65,163) is contradicted by his recognition that Sithe renegotiated its power purchase agreement with Con Edison to reflect the restructuring. Initial Decision at 65,155. Dr. Harvey also testified that experience has demonstrated that allegedly inflexible contracts can be, and

III. THE PRESIDING JUDGE ERRED WHEN HE CONCLUDED, AS A MATTER OF LAW, THAT THE NYCPUS TSA PRECLUDES THE OTHERWISE PROPER AND APPROPRIATE AMENDMENTS FROM BECOMING EFFECTIVE UNTIL THEY ARE FIRST FILED WITH THE NEW YORK PUBLIC SERVICE COMMISSION

The Presiding Judge's requirement that the Amendments to the NYCPUS TSA must be filed first with the NYSPSC before it can become effective is directly at odds with:

- the Presiding Judge's own findings that NYCPUS should not be able to avoid the NYISO charges;
- the Presiding Judge's own findings that the Amendments relate to important Commission transmission policy issues and do not relate in any way to Con Edison's retail rates on file with NYSPSC;
- a longstanding Commission policy not to defer to state agencies in cases that relate to transmission services within the Commission's jurisdiction and do not involve, in any way, matters of local concern; and
- the testimony of Con Edison as to its intent underlying the rate change contract language at issue, which evidence the Presiding Judge refused to even consider.

Moreover, the Presiding Judge's ruling, by elevating form over substance, at this late date, would require the needless and wasteful expenditure of considerable additional time and resources of the Commission, the NYSPSC and all affected parties since this Commission has the ultimate authority over the proposed Amendments to the TSA.

A. The Presiding Judge Properly Found That The Amendments Relate To Important Commission Transmission Policy Issues And Do Not Relate In Any Way To Con Edison Retail Rates On File With The NYSPSC

The NYCPUS TSA provides for the filing of rate changes with the NYSPSC but vests ultimate authority over the rate change with the FERC. Deference to the NYSPSC is neither necessary nor appropriate in this case, where the Amendments relate exclusively to the

(..continued)
will be renegotiated, as in the case of Sithe, when provided with appropriate economic incentives. MSI-5 at 8, lines 8-18.

implementation of a state-wide ISO and a new pricing structure that eliminates pancaked rates. This is particularly true in light of the fact the NYSPSC facilitated and actively supported the development of the ISO. Moreover, in this case, the NYSPSC has participated in this proceeding for the last two years, has not taken any position with respect to NYCPUS' claims that the Amendments had to be filed with the NYSPSC, and has not requested that the Commission defer to the NYSPSC's judgment on the subject of these Amendments. Based on these circumstances, as well as the Presiding Judge's own factual findings and Commission precedent, the subject Amendments were not required to be filed with the NYSPSC.

In ruling on NYCPUS' substantive challenges, the Presiding Judge made the following findings:

a. NYCPUS should not be able to avoid the NYISO charges. Initial Decision, at 65,184. ("[NYCPUS] should not be allowed to evade responsibility to the new statewide regime by a strained interpretation of a settlement that deals with retail rates and has nothing really to do with the provision of ancillary services in the context of an ISO." Id.).

b. The NYISO services that are the subject of the Amendments are not services that were previously provided by Con Edison to NYCPUS under the TSA prior to NYISO start-up. Initial Decision, at 65,181. ("I find that Con Edison was under no obligation to provide ancillary and LSE services to NYCPUS." Id.).

c. The rates being charged by Con Edison to NYCPUS do not relate in any way to the NYISO services at issue here. Initial Decision, at 65,184 ("Con Edison is not changing its rates to NYCPUS. . . The new services provided by the NYISO to effectuate the competitive electric markets in New York must be paid for by entities that they are intended to benefit. NYCPUS is one such entity." Id.).

Having rejected all of the substantive challenges to the appropriateness of the Amendments, the Presiding Judge erred in determining that the Amendments could not be effective because they were not first filed with the NYSPSC. This finding is arbitrary and capricious in light of the Presiding Judge's other findings that: the Amendments do not relate to NYSPSC retail rates; the Amendments do not relate to services provided by, or charges paid to Con Edison; and NYCPUS should reimburse the NYISO for the costs it incurs in providing services to NYCPUS. Moreover, this procedural ruling elevates form over substance contrary to Commission precedent which the Presiding Judge failed to even consider.

B. The Presiding Judge's Finding That The TSA Language, Nevertheless, Requires These Amendments To Be Filed With The NYSPSC Is Contrary To Commission Precedent

The NYCPUS TSA incorporates Con Edison's retail rates on file with the NYSPSC. It also grants Con Edison the unilateral right to file Amendments to the TSA with the NYSPSC "subject to FERC review." Thus, the TSA vests final authority over proposed changes with FERC, not the NYSPSC. The Presiding Judge completely ignored this aspect of the rate change provision and the related Commission precedent.

In cases involving other similar Con Edison TSAs, prior to the issuance of Order No. 888, the Commission approved rate changes and affirmed its complete and independent authority over such TSAs. Consolidated Edison Co. of New York, Inc., 15 FERC ¶ 61,174 (1981). Faced with the question, in that case, as to whether it had jurisdiction over the entire transaction or only the transmission portion, the Commission ruled that it has jurisdiction over the entire service. Since Con Edison's rates were tied to its local rate schedules, the Commission stated that it would generally defer to NYSPSC rate determinations but that it would conduct its own independent analysis. In this regard, the Commission stated:

> *In adopting this procedure, we do not abandon our statutory responsibilities in this or future proceedings.*

Id. at 61,405-406 (emphasis added)(footnote omitted).

In another case predating Order No. 888, the Commission dealt with another Con Ed/NYPA TSA for the delivery of NYPA's EDP power that involved the same rate change language present here:

> The agreement also *provides* that in the event that the parties fail, as they have, to reach an agreement as to the rates, terms, and conditions of this service, Con Ed would unilaterally file a rate schedule with the New York State Public Service Commission (NYSPSC), subject to ultimate review by the Commission.

Consolidated Edison Co. of New York, Inc., 39 FERC ¶ 61,003, at 61,006 (1987). There, the Commission noted that it has "delegated" the "initial" rate determination to the New York PSC and would not "insist that the rates be developed, in all respects," according to its rate making policies. Id. at 61,008. However, the Commission again made it clear that, even with respect to the Con Edison TSAs that relate to PSC retail rate schedules, the Commission's delegation of the initial determination of the rates did not deprive the Commission of its jurisdiction. In the instant case, the rates in question are not PSC rates for local service from Con Edison. Rather, the rates are FERC-jurisdictional rates for NYISO service, which the Presiding Judge has found bear no relationship to Con Edison PSC retail rates. Initial Decision, at 65,181-84.

In Order No. 888, the Commission held that retail delivery services would henceforth be regarded as consisting of two components, a transmission component subject to the jurisdiction of the FERC and a local distribution component subject to state authority:

> [W]hen unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes - a transmission component and a local distribution component. The Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component. [citation omitted]. Thus, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. When this occurs, we will generally expect unbundled retail wheeling

> customers to take service under the same FERC tariff that applies to wholesale customers. However, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff [citation omitted] to accommodate the design and special needs of such programs. In such situations, the Commission will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by this Final Rule. In addition, rates must be consistent with our Transmission Pricing Policy Statement, and the guidance herein concerning ancillary services.

Order No. 888 at 31,784-85 (emphasis added).

In subsequent proceedings where the rate issue involved the Commission's open access transmission policies, the Commission has refused to defer to State Commissions with respect to matters relating to the transmission component of retail delivery service.[32] In one case,[33] the Commission noted that the state agency had not requested deference:

> While we find that we have jurisdiction over NYSEG's transmission of economic development power, we also recognize New York State's legitimate interest in using economic development power to promote local economic development. Out of deference to that interest, and to avoid disrupting the parties' existing contractual arrangements, we will grant NYSEG's request for a waiver of our notice and filing requirements so that the tariff and all existing service agreements can become effective as of the time of the parties' contractual arrangements. However, *we see no need at this juncture to exempt any transactions with new retail customers, or revisions to the arrangements with existing customers, from the requirements of our Open Access Rule.* While we indicated in the Open Access Rule that we would defer to state requests for variations from the pro forma open access tariff to accommodate the design and special needs of state retail access programs, *the New York Commission has not made such a request.*

Id. (emphasis added). On rehearing of the NYSEG decision, the Commission rejected the arguments advanced by the NYSPSC that the express contract language undercuts the Commission's exercise of jurisdiction stating:

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[32] See Joint Reply Brief of Member Systems and NYISO at 84-86.

[33] New York State Elec. & Gas Corp., 77 FERC ¶ 61,044 at 61,154 (1996) ("NYSEG"), reh'g denied, 83 FERC ¶ 61,203 (1998), (appeal pending sub nom. People of New York v. FERC, No. 98-4276 (2nd Cir. July 14, 1998).

> While we agree that the contract language is the appropriate starting point for analysis, and that the language indicates that NYPA is selling EDP to NYSEG, the Commission is bound to look not only at the contract language, but also at the substance of the transaction. . . based on a review of all the evidence and the details before us, we concluded that the contract language was not determinative.
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> ***
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> To rely solely, or even principally, on the parties' contractual recitations, as the New York Commission urges, is to elevate form over substance. . . .

83 FERC at 61,903; See also Joint Reply Brief of Member Systems and NYISO at 85-86.

In other post-Order No. 888 cases, the Commission has rejected arguments advanced by utilities that it should defer to state jurisdiction. In particular, the Commission rejected two Direct Access Delivery Service ("DADS") tariffs proposed by Washington Water Power finding, the tariffs included unbundled retail transmission service in interstate commerce by a public utility, and that this service was within its jurisdiction.[34] According to the Commission:

> Washington Water Power asserts that deferring to state jurisdiction would allow the experiment to proceed without delay, and that if it is required to offer the service under its open access tariff, 'the experiment may fail at the outset.' . . . We deny Washington Water Power's request to use its DADS tariffs for unbundled retail transmission service under the experiment, and require it to offer unbundled retail transmission service pursuant to its open access transmission tariff . . . As discussed above, it was our expressed policy in Order No. 888 except NEPCO [citation omitted], for unbundled retail transmission service to be offered under a public utility's open access transmission tariff on file with the Commission. Id. at 61,725.

These cases make clear that the Commission has declined to defer to State Commissions where, as in this case, there is no compelling local interest at stake and the service in question is clearly within the Commission's jurisdiction.

C. The Presiding Judge Improperly Failed To Consider The Evidence Of The Parties' Intent With Respect To The Contract Language At Issue

The Presiding Judge held that the parties clearly intended the requirement to file any TSA changes first at the NYSPSC to be a substantive and required step prior to seeking FERC

[34] Washington Water Power Company, 78 FERC ¶ 61,178 (1997), order denying reh'g and granting clarification, 79 FERC ¶ 61,142 (1998).

approval.[35] The Presiding Judge tacitly acknowledged, by way of a footnote, the arguments of the Member Systems and the NYISO that this was intended to apply only to NYSPSC jurisdictional rates and cases where the NYSPSC rates had to be modified; however, he speculated that "the NYSPSC played a broader role and the parties probably intended precisely what they said."[36] The Initial Decision was notably devoid of any support for this finding. Moreover, it lacks any discussion or analysis of the Member Systems' and NYISO's evidence as to the parties' intent. This is particularly odd since this evidence is entirely consistent with the Presiding Judge's finding that the proposed Amendments do not relate in any way to Con Edison's retail rates. The Presiding Judge's ruling also is logically inconsistent with the intent of the TSA. Since the Amendments do not change any of Con Edison's retail rates, why would it be necessary to make a filing with the NYSPSC for its approval?

Con Edison witness, Mr. Raymond Turkin, testified that the contract language at issue only related to retail rates and not to the situation where, as here, FERC is implementing state-wide transmission policies related to services not previously provided under the TSA. As Raymond Turkin testified:

> The NYCPUS Agreement requires Con Edison, in certain circumstances, to first negotiate with NYCPUS any changes in the rates, terms, and conditions of the service provided by Con Edison and then to seek approval from the NYSPSC for any such changes prior to seeking FERC approval. However, since Con Edison was not seeking to change the base rates, terms, or conditions of the service that Con Edison is providing to NYCPUS, it was not necessary for Con Edison to either negotiate with NYCPUS or to file with the NYSPSC prior to making the necessary filing with the FERC. Because the rate change contemplated by the Amendment calls for NYCPUS to pay certain additional NYISO charges, no changes were required to any Con Edison rate schedule on file with or approved by the NYSPSC. What Con Edison filed at FERC was an amendment to the NYCPUS Agreement itself, not an amendment to the rate schedule (NYSPSC Rate Schedule No. 9) which is a separate filing with the NYSPSC and is not part of the NYCPUS Agreement. The amendment simply seeks to require NYCPUS to pay the NYISO for new services that NYCPUS will now receive as a result of

[35] Initial Decision at 65,185.

[36] Initial Decision at 65,185 n.52.

> the FERC approval of the NYISO and, therefore, Con Edison was not required to first negotiate with NYCPUS or to make a filing with the NYSPSC before seeking FERC approval.

Ex. No. MS-1 at 11, lines 6-22. In rebuttal testimony, Mr. Turkin testified that:

> Con Edison's actions were consistent with the explicit terms of the NYCPUS Agreement and the 1997 Settlement Agreement. Both agreements set forth provisions to be followed in the event that Con Edison was to seek a change in its rates. As stated in my direct testimony (p. 11), since Con Edison was not seeking to change the base rates, terms, or conditions of the service that Con Edison is providing to NYCPUS it was not necessary for Con Edison to follow the rate change procedures of the 1987 NYCPUS Agreement or the 1997 Settlement Agreement. Con Edison is only seeking to require NYCPUS to pay the NYISO for the new services that NYCPUS now receives from the NYISO as a result of the FERC's approval of the NYISO. Con Edison did, however, serve a copy of the filing with FERC to amend the NYCPUS Agreement on the NYSPSC.

Ex. No. MS-7 at 9, lines 11-24; 10, lines 1-2.

Had the Presiding Judge evaluated the discrete contractual terms in context and considered evidence as to the parties' intent, a different result would have been reached. This is plain error. It is imperative, therefore, for the Commission to review the Member Systems' evidence and find that an initial review by the NYSPSC is not needed prior to the Commission's review of the Amendments that relate to NYISO charges for new services and which do not relate to Con Edison's retail rates.

D. The Presiding Judge's Ruling Would Require The Needless And Wasteful Expenditure Of Additional Time And Resources By The Commission, The NYSPSC And All Affected Parties

The Amendments were served on the NYSPSC at the commencement of this proceeding on August 3, 1999. Both NYCPUS and the NYSPSC have participated in these proceedings which have been underway for nearly two years, and they have had an adequate opportunity to conduct discovery, to file testimony and briefs and to participate in the evidentiary hearing.

Although the Presiding Judge accepted, without discussion, that FERC would be the final arbiter, he failed to explain how or why there is a valid purpose in requiring prior NYSPSC

approval or why the parties would have intended such a result. The Presiding Judge failed to address why NYSPSC approval was needed for the Amendments that did not change any NYSPSC-jurisdictional rates nor change the revenue collected by a NYSPSC-regulated entity. The Presiding Judge also failed to address the concerns enunciated by the Member Systems and the NYISO that it is absurd to ignore the fully developed record in this proceeding, to start anew and to later come full circle back to FERC for the final determination particularly since the Amendments pertain to new NYISO services and charges and do not relate to state retail issues. The Presiding Judge completely ignored the Member Systems' and the NYISO's evidence that the requirement to seek prior NYSPSC approval prior to the effectiveness of the Amendments will merely be a rote exercise with no effect but at considerable expense and the substantial devotion of significant resources. This is particularly true in light of the Presiding Judge's determination that NYCPUS should not be allowed to evade responsibility for the NYISO charges.

NYCPUS has fully litigated the proposed Amendments in this case, and the Commission already has a fully developed record in this proceeding. Moreover, the Presiding Judge already has ruled on, and rejected, the arguments advanced by NYCPUS in opposition to the Amendments. The Presiding Judge also has found that the Amendments do not change Con Edison's retail rates nor the amount of revenues that Con Edison collects; thus, any filing with the New York PSC would be purely informational.

There is simply no useful function for the NYSPSC to perform with regard to this matter. Moreover, in any event, the Commission would have ultimate and independent authority to review any NYSPSC decision and would reach the same conclusions on the substantive issues as those reached by the Presiding Judge based on the extensive record in this case.

Moreover, Con Edison and the Member Systems note that this procedural argument was implicitly rejected by the Commission in setting the Amendments to the NYCPUS TSA for hearing and by the Presiding Judge in his Order on Legal Issues. There also is clear prejudice to Con Edison and the other Member Systems resulting from this belated dismissal of their

Amendments to the NYCPUS TSA on this technicality only at this late date in the proceedings, since an earlier dismissal of the Amendments to the NYCPUS TSA could have permitted them to cure this defect and refile.

CONCLUSION

WHEREFORE, for the above stated reasons, the Member Systems and the NYISO respectfully request: that the Commission reverse those portions of the Presiding Judge's May 11, 2001 Initial Decision that:

(1) reject the application of the marginal loss provisions of the NYISO OATT to the Sithe TSA; and

(2) require the Member Systems to obtain the approval of the NYSPSC before making a filing with the Commission to modify the NYCPUS TSA as proposed in this case; and

that the Presiding Judge's May 11, 2001 Initial Decision be in all other respects accepted and affirmed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day, the 11th day of June, 2001, served the foregoing document upon each person designated on the restricted service list for Docket No. ER97-1523-011, et al., compiled in this proceeding, pursuant to Rule 2010 of the Commission's Rules of Practice and Procedure, 18 CFR § 385.2010(a)(1)(i), by United States first class mail.

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Rebecca J. Michael