

## ***EXHIBIT 1***

### **Proposal for Enhancements to the NYISO Capacity Market An Alternative to the Demand Curve**

**Advanced by New York State Electric & Gas Corporation, Rochester Gas and Electric Corporation, Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., City of New York, Luthin Associates for Refined Sugars, Inc., Columbia University, New York University, New York Presbyterian Hospital, Beth Israel Health Care System, Mount Sinai Medical Center, Long Island Power Authority, New York State Consumer Protection Board, and Multiple Intervenors<sup>1</sup>**

#### **Introduction**

The capacity market enhancements described herein are being proposed as an immediate effort to move toward a more rational and efficient capacity market. Under this proposal, the ISO would implement certain changes immediately and work with market participants during the coming months to finalize the details required to implement the remaining concepts laid out below. This proposal is being offered solely as an alternative to any demand curve proposal.

#### **Obligation Procurement Period**

The first proposed enhancement is to move back to a six month obligation procurement period (OPP) for the summer of 2003, which is May 1 through October 31, 2003, and for the winter of 2003 – 2004 which is November 1 2003 through April 30, 2004, with an extension to a one-year OPP thereafter. Monthly auctions would no longer be conducted. Capacity would be sold and procured based on Summer Dependable Maximum Net Capability (DMNC) ratings, as described below.

#### **Capacity Rating Mechanism**

A generating unit's capacity that can be sold to satisfy the New York capacity requirements is defined as the unit's Dependable Maximum Net Capability (DMNC). Currently DMNCs are determined twice a year covering the summer and winter capability periods. Under the current market rules the summer and winter DMNCs are used in the respective procurement periods. The ratings are determined using a target temperature for the summer or winter period, respectively.

In conjunction with moving to a six month and then annual OPP, the NYISO market would use the summer DMNC to reflect the quantity of supply available from each facility. The

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<sup>1</sup> As of February 4, 2003. The market participants advancing this proposal are advancing it as a package for consideration by the NYISO and the ICAP WG. These market participants individually may also (i) choose to support or oppose a demand curve, or (ii) choose to support or oppose any or all of the individual elements, or both. Also, for the purposes of this proposal, capacity supply includes Special Case Resources and other qualifying demand response, as appropriate.

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use of the Summer DMNC rating is naturally aligned with an annual requirement because a supplier offering to provide energy during every day of the annual period would be restricted by the summer rating as that is the maximum amount that it can assure supplying during the OPP.

A six-month market in the winter or annual market with summer-only DMNC has important implications for the availability and price of capacity in the winter including the potential of a shortage of capacity in the winter due to units that decide to offer capacity only in the summer period. In this design, the amount of supply would be capped at the summer-only DMNC level for both the summer and winter capability periods. To ensure that prices do not spike above summer prices and that the winter market does not become deficient, additional winter capacity would be allowed only as a replacement for summer-only capacity. The amount of winter excess would be limited to the equivalent summer amount, making both markets behave similarly, while allowing a different mix of specific units when needed.

Because of the price risk implicit in the use for the Summer DMNC in the winter OPP, the auction price in such winter OPP would be capped at the market clearing price of the immediately preceding summer OPP to ensure that winter prices would not exceed summer prices.

### **Procurement Process**

In addition, the ISO has indicated that it is concerned about the test procedures currently used to determine a unit's DMNC. Any solution must be determined concurrently with an evaluation of the DMNC testing procedures. The NYISO would separately evaluate the winter DMNC ratings to ensure that any incremental winter capacity is available to meet load requirements through the winter period consistent with reliability requirements. The process will allow incremental temperature sensitive capacity to participate in the a process which attempts to match the additional winter supply of generating capacity with (i) summer only capacity suppliers into NYISO, (ii) newly constructed resources, or both.

Under this proposal the NYISO would run an auction for all annual capacity requirements. The holders of bilateral contracts would simply report the amounts contracted for thereunder to the NYISO to match the holders' purchase requirements. The key benefit of the auction is that it would enable resources that are only available during portions of the year, e.g. summer resources from winter peaking regions such as Canada, or newly constructed resources that are placed in service part way through the OPP, to be combined to create a portfolio meeting the annual supply requirements.

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### **Retail Access and New Capacity Supply Accommodations**

Due to the OPP being longer than one month, accommodations for both the month-to-month load shifts that occur under New York's retail access program and new capacity supply that becomes available during the term of any OPP, must be made.

Each LSE would handle month-to-month load shifts through a monthly swap of the remaining capacity obligation. LSEs that gain load would take on the remaining capacity obligation from LSEs that lose load through a monthly reassignment facilitated by the NYISO. The capacity would change hands at a monthly prorated price based on the most recent OPP auction clearing price (whether one-year or six-months).

New capacity would be eligible to participate in the capacity market through the auction as well as through bilaterals. For new capacity participating through the auction, the ISO would determine appropriate penalties, credit requirements, and milestones to ensure the new capacity is available when promised. Any LSE contracting for such new capacity would take the risk of its delivery. If a new resource is not completed in accordance with the accreditation provided to the NYISO before the auction, the NYISO may assess the deficiency charge after an opportunity for the LSE to cure any deficiency in a timely manner.

### **Deficiency price to be revised to 1.5 times the cost of a new GT**

With longer-term procurement, the need for a higher deficiency charge is limited as there is a more rational approach to ensuring reliability and meeting capacity requirements. Therefore, the capacity deficiency price is revised to 1.5 times the cost of a new GT.

### **In-City Price cap implementation**

The \$105/kW-year in-city price cap would be implemented in two parts, summer and winter, if a two-capability period year is implemented. If Summer DMNC ratings are used in both six-month capability periods, the price caps would be \$52.50/kW/six-month period. If a one-year period is implemented, a single annual \$105/kW-year price cap may be implemented.

### **Mitigation and Market Monitoring**

During the coming months, the NYISO will consider whether modifications to the mitigation and monitoring capability of the NYISO are appropriate to ensure that market power is not exercised in the capacity market.

### **Sunset of Provisions**

These enhancements shall only be implemented in the event that the NYISO has not and does not implement a demand curve. If the NYISO implements a demand curve at any time after implementing the changes described above, the NYISO shall at the time it implements such demand curve also immediately nullify all changes to the capacity markets described above.