



Couch White, LLP
540 Broadway
P.O. Box 22222
Albany, New York 12201-2222
(518) 426-4600
Telecopier: (518) 426-0376

Michael B. Mager
Partner
Direct Dial: (518) 320-3409
Direct Telecopier: (518) 320-3495
e-mail: mmager@couchwhite.com

May 9, 2001

VIA HAND DELIVERY

Mr. Richard J. Grossi
Chairman of the Board of Directors
c/o Mr. William J. Museler
President and Chief Executive Officer
New York Independent System Operator
3890 Carmen Road
Schenectady, New York 12303

Re: Motion in Opposition to Appeals

Dear Messrs. Grossi and Museler:

Enclosed are the original and three copies of the Motion in Opposition to Appeals submitted by Multiple Intervenors, an unincorporated association of approximately 65 large commercial and industrial energy consumers with manufacturing and other facilities located throughout New York State, on behalf of its five member companies -- Alcoa/Reynolds Metals Company, IBM Corporation, Occidental Chemical Corp., Praxair Inc. and Xerox Corporation -- that are members of the New York Independent System Operator ("NYISO") Management Committee. The enclosed Motion opposes the appeals of the Independent Power Producers of New York, Inc. and, jointly, Aquila Energy Marketing Corp. and Morgan Stanley Capital Group, from the Management Committee's April 18, 2001 decision to request that the NYISO Board of Directors concur in a joint filing to the Federal Energy Regulatory Commission to amend the NYISO's Market Monitoring Plan to include a Penalties and Public Disclosure Proposal that was approved by the Management Committee.

Very truly yours,

COUCH WHITE, LLP

Michael B. Mager

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Enclosures
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## **MOTION IN OPPOSITION TO APPEALS**

### **PRELIMINARY STATEMENT**

Multiple Intervenors, an unincorporated association of approximately 65 large commercial and industrial energy consumers with manufacturing and other facilities located throughout New York State, hereby files with the New York Independent System Operator (“NYISO”) Board of Directors (“Board”) this Motion in Opposition to the appeals filed recently by the Independent Power Producers of New York, Inc. (“IPPNY”) and, jointly, Aquila Energy Marketing Corp. and Morgan Stanley Capital Group, Inc. (“Aquila/MSCG”) (collectively, the “Appellants”). The Appellants appeal from the Management Committee’s April 18, 2001 decision to request that the Board concur in a joint filing to the Federal Energy Regulatory Commission (“FERC”) to amend the NYISO’s Market Monitoring Plan to include a Penalties and Public Disclosure Proposal (“Proposal”) that was approved by the Management Committee. Five members of Multiple Intervenors -- Alcoa/Reynolds Metals Company, IBM Corporation, Occidental Chemical Corp., Praxair Inc. and Xerox Corporation -- are active members of the Management Committee and voted in favor of the Proposal. This Motion in Opposition is submitted on behalf of those members of Multiple Intervenors. For the reasons set forth below, the Board should deny Appellants’ appeals in their entirety.

**SUMMARY OF THE PROPOSAL APPROVED**  
**BY THE MANAGEMENT COMMITTEE**

The Proposal approved by the Management Committee provides a reasonable and much-needed deterrent against the exercise of market power by generators.<sup>1</sup> As the Board is well aware, the NYISO presently is not authorized to correct retroactively prices that are impacted by conduct that results in the application of market mitigation measures, or to impose financial penalties on a generator to recover the gains that it made from such conduct.<sup>2</sup> Because of this “void” in the NYISO’s authority, a generator knowingly can engage in conduct that warrants mitigation and still reap the full financial benefit of doing so up to the time that its conduct is detected and mitigated on a going forward basis.

Significantly, in order to appease objections raised by the generators as the Proposal was being developed, the Proposal does not require any corrections or changes to previously-established market clearing prices. Importantly, the Proposal includes a series of significant compromises from a Price Correction Authority measure was defeated at the Management Committee on March 1, 2001 in a very close vote. That measure would have reset market clearing prices in the prior day for all participants. The compromises were made in an effort to allay objections raised by the Generator and Other Supplier sectors represented

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<sup>1</sup> The Proposal, in a slightly modified form, also was approved by the Business Issues Committee.

<sup>2</sup> The NYISO does have authority to impose a financial obligation on a generator that is physically withholding or overproducing. The formula for calculating that financial obligation would be eliminated and replaced by the Proposal.

by Appellants. Instead, the Proposal is targeted to deter the exercise of market power before it occurs by imposing financial penalty provisions and, for repeat offenders, public disclosure provisions on generators that engage in conduct which warrants mitigation.

The financial penalty provisions of the Proposal are applicable to energy markets (i.e., the day-ahead and the real-time markets), but not the ancillary services markets. Subject to the NYISO's exercise of discretion, penalties imposed under the Proposal are triggered by an action by the NYISO to mitigate the behavior of a generator. However, the penalties do not apply to mitigation actions that occur through application of the NYISO's Automatic Mitigation Process ("AMP") or FERC-approved localized market mitigation measures applicable to sales of capacity, energy and certain ancillary services from specified generating units in New York City.

The penalties set forth in the Proposal increase in severity, with a lesser penalty imposed the first time a generator is mitigated by the NYISO, and increasingly larger penalties imposed for subsequent actions by the same generator that result in mitigation. The penalty for the first mitigation action during mitigated hours is:

$$1^{\text{st}} \text{ penalty} = (\# \text{ of MWs mitigated during mitigated hours}) \times (\text{LBMP at the mitigated generator's bus}) \times 2^3$$

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<sup>3</sup> In this formula, "2" is the multiplier. The multiplier increases with subsequent penalties. The "MWs mitigated" input is based on the MW amount of the entity's generation capacity that exhibited the behavior that was found by the NYISO to warrant mitigation. The MW value is converted into a MWh value by applying it to the number of hours in which the conduct occurred, subject to limitations on the duration of activities encompassed by the penalty.

The penalty for a second mitigation action within 24 months of the first mitigation action by the same generator owner is calculated by using the above formula, but with “3” inserted as the multiplier instead of “2.” The penalty for a third and subsequent mitigation actions within 24 months of the second mitigation action by the same generator owner also is calculated using the above formula, with “4” inserted as the multiplier. Additionally, the third time that a generator owner is mitigated by the NYISO, the bids of all its generators are constrained to their reference bid curve for a six-month period.

Once a penalty is triggered, it is applicable to all previous market activities by the generator that: (a) are deemed to be the same type as the activity that was mitigated; and (b) occurred not more than 14 days prior to the implementation of mitigation by the NYISO for physical withholding, and not more than five days prior to the implementation of mitigation by the NYISO for all other actions (e.g., economic withholding).

Pursuant to an amendment to the Proposal advocated by generators and approved by the Management Committee, the NYISO may waive all or part of a penalty if it determines that the penalty is onerous or provides no deterrent value. Additionally, generators subject to a penalty will have the right to appeal that penalty through the NYISO Alternative Dispute Resolution (“ADR”) process. That process will determine whether the NYISO properly applied mitigation under its market monitoring authority.<sup>4</sup>

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<sup>4</sup>The penalty will not be assessed until the ADR process is complete. A generator also may appeal the imposition of a penalty to FERC.

The public disclosure provisions of the Proposal similarly are intended to provide a deterrent to a generator considering the exercise of market power. Pursuant to the provisions approved by the Management Committee, the first time an entity is mitigated by the NYISO, the entity will not be named. Subject to an exercise of discretion by the NYISO, an entity will be named if it is mitigated again by the NYISO within 24 months of the first mitigation action. The entity also will be named after subsequent mitigation actions by the NYISO. No confidential information (e.g., bids) will be revealed as part of the public disclosure process.

Importantly, mitigation that occurs through the AMP and FERC-approved localized market mitigation measures applicable to sales of capacity, energy and certain ancillary services from specified generating units in New York City will not be subject to the public disclosure mechanism. Similar to the penalty provisions, the NYISO may waive public disclosure if it determines that such disclosure would have no deterrent value. Additionally, if an entity wishes to appeal, the public disclosure will be delayed until the resolution of that appeal in the NYISO's ADR process and of any subsequent appeal to FERC.

### **ARGUMENT**

#### **APPELLANTS' APPEALS ARE WITHOUT MERIT AND SHOULD BE DENIED**

IPPNY and Aquila/MSCG raise numerous arguments as to why the Board should reject the Proposal that was approved by the Management Committee (and previously by the

Business Issues Committee). For the reasons set forth below, Appellants' arguments are without merit and their appeals should be denied in their entirety.

Appellants initially complain that the penalty provisions in the Proposal are "draconian." Appellants are wrong. This claim is completely unfounded. The Proposal is a muted, reasonable approach to a serious problem -- the potential exercise of market power. As noted earlier, the penalty provisions of the Proposal were reduced several times and represent a compromise that secured the support of the Management Committee. In response to arguments by generators, the penalty provisions were tempered considerably to pertain solely to: (a) the generator engaging in conduct that results in market mitigation; and (b) the specific generation capacity that exhibited the conduct that warranted mitigation. Moreover, at the generators' urging, a number of procedural checks were introduced, including providing the NYISO with discretion regarding the imposition of penalties. Thus, Appellants' claim that the Proposal is "draconian" clearly is without support.

Moreover, the Proposal's relatively muted approach must be weighed against the harm that it is intended to eliminate. Conduct which spurs market mitigation can have the effect of increasing electricity prices paid by tens of thousands -- if not millions -- of consumers. Moreover, the impact of exercises of market power on consumers is devastating -- one need only look at June 26, 2000 for an example of how such impacts can run into the hundreds of millions of dollars in a very short period of time. Under the circumstances, the penalties contained in the Proposal are comparatively tame, and reflect modifications advocated by many generators. When the Board evaluates the penalties contained in the

Proposal, it must remain cognizant of the significant harm that a generator exercising market power can invoke on the State's electricity consumers.

IPPNY argues that there has been no demonstration that market participants have contributed to the sharp rise in electricity prices. IPPNY is mistaken. Again, the impacts of June 26, 2000, and other days in which one or more generators have exercised market power, demonstrate that such conduct can have a dramatic impact on prices. IPPNY also asserts that the NYISO's Market Advisor has concluded that the market is competitive. However, the Market Advisor also has acknowledged that there still are times when the State's markets are not workably competitive. It is during those critical times that the Proposal will act as a much-needed deterrent to any generator contemplating the exercise of market power.<sup>5</sup>

Aquila/MSGC criticizes that portion of the Proposal which accords the NYISO discretion to waive penalties and/or public disclosure. Ironically, such discretion is a protection that was desired by generators and other suppliers during negotiations on the Proposal, and which was included in the Proposal by means of an unfriendly amendment that garnered over 70% of the votes within the Management Committee. Multiple Intervenors would have no objection if the Proposal is modified by the Board to render the penalties and

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<sup>5</sup> Absent the deterrent effect of the Proposal, such conduct could cost consumers even more money this year, when the State's supply situation is expected to be tighter -- and the summer hotter -- than was the case last year.



public disclosure provisions contained therein automatic, and not subject to the NYISO's discretion.<sup>6</sup>

Appellants also complain that the Proposal does not contain corresponding provisions subjecting transmission owners ("TOs") and load serving entities ("LSEs") to penalties and public disclosure. Those complaints lack merit and also fail to inform the Board of relevant history leading up to the Management Committee's approval of the Proposal. During the numerous debates on the Proposal in its various incarnations, generators raised this same argument as to applicability of the penalty and public disclosure provisions. In response to such arguments, generators were invited repeatedly to develop a detailed proposal that would address their concern. Significantly, no party ever advanced a detailed proposal designed to subject TOs and LSEs to comparable penalties and public disclosure. To the extent a need for such provisions is demonstrated to exist and a detailed proposal is advanced, the Management Committee can address that proposal at a future meeting.<sup>7</sup>

Finally, Appellants raise several "due process" concerns, all of which are without merit. In fact, the Proposal was modified numerous times to address those types of concerns. It should be noted that: (a) the Proposal is subject to FERC approval prior to implementation;

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<sup>6</sup> Allowing the NYISO discretion to waive penalties and/or public disclosure operates solely to the benefit of generators whose conduct resulted in market mitigation.

<sup>7</sup> The Management Committee did reject a spur-of-the-moment unfriendly amendment to the Proposal which would have subjected TOs and LSEs to various penalties. That amendment lacked detail and was not distributed previously to the Management Committee. In the opinion of Multiple Intervenors, the proponents of the amendment also failed to demonstrate a compelling need to subject TOs and LSEs to comparable penalties.

(b) the penalty and public disclosure provisions apply only when generator conduct results in market mitigation; (c) conduct that results in mitigation through the AMP and certain In-City mitigation measures would not be subject to penalties or public disclosure; (d) the penalties are very limited in scope to serve as a deterrent to “bad actors,” and do not penalize “innocent” generators; (e) the NYISO has discretion to waive penalties and public disclosure where circumstances warrant; (f) generators subject to penalties and/or public disclosure may pursue an appeal through the NYISO’s ADR process; and (g) such generators also may appeal penalties and/or public disclosure to FERC. Clearly, the Proposal contains significant procedural safeguards which generators can utilize if they feel that a penalty or public disclosure should not be imposed. In closing, in assessing the appeals, the Board should consider the potential harm to the State’s consumers, who maybe forced to pay hundreds of millions of dollars in extra costs if market power abuses are left unchecked. The Proposal fills a huge void by providing a reasonable set of penalties designed to deter exercises of market power by generators.

**CONCLUSION**

For all the foregoing reasons, Multiple Intervenors, including its five member companies that also are members of the Management Committee, urge the Board to reject the appeals of IPPNY and Aquila/MSCG.

Dated: May 9, 2001  
Albany, New York

Respectfully submitted,

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Michael B. Mager, Esq.  
COUCH WHITE, LLP  
Attorneys for Multiple Intervenors  
540 Broadway  
P.O. Box 22222  
Albany, New York 12201-2222  
(518) 426-4600

*Of Counsel:*

Robert M. Loughney, Esq.  
Michael B. Mager, Esq.

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