

May 9, 2001

**VIA FEDERAL EXPRESS**

Honorable Richard J. Grossi  
Chairman, New York Independent System  
Operator Board of Directors  
C/O William J. Museler  
President and CEO  
New York Independent System Operator, Inc.  
3890 Carman Road  
Schenectady, NY 12303

Re: Motion of the Transmission Owners, LIPA and the Power Authority of the State of New York In Opposition to the Appeals to the NYISO Board Regarding the Decision of the Management Committee to Approve Revisions to the Market Power Monitoring Plan With Respect to Penalties and Public Disclosure

Dear Chairman Grossi:

Pursuant to the "Procedural Rules for Appeals to the ISO Board," the Transmission Owners,<sup>1</sup> LIPA and the Power Authority of the State of New York<sup>2</sup> respectfully submit three copies of a Motion in Opposition to the Appeals to the NYISO Board filed by: (1) the Independent Power Producers of

---

<sup>1</sup> The Transmission Owners constitute all of the Members of the Transmission Owners Sector of the NYISO Management Committee, which includes Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and Rochester Gas and Electric Corporation.

<sup>2</sup> LIPA and the Power Authority of the State of New York are Members of the Public Power/Environmental Sector of the NYISO Management Committee.

Honorable Richard J. Grossi  
May 9, 2001  
Page 2

New York, Inc. ("IPPNY"); and (2) Aquila Energy Marketing Corporation and Morgan Stanley Capital Group, Inc.

A copy of the Motion in Opposition has been transmitted by e-mail to Kristen Kranz of the NYISO's staff who has agreed to serve it on each member of the Management Committee today.

Sincerely,

Paul L. Gioia

Enclosures

cc: via e-mail  
Kristen Kranz  
Linda Moore  
William J. Museler  
Ira Freilicher  
AL69834

**MOTION OF THE TRANSMISSION OWNERS,  
LIPA AND THE POWER AUTHORITY OF THE STATE OF NEW YORK  
IN OPPOSITION TO THE APPEALS TO THE NYISO BOARD  
REGARDING THE DECISION OF THE MANAGEMENT COMMITTEE TO  
APPROVE REVISIONS TO THE MARKET POWER MONITORING PLAN  
WITH RESPECT TO PENALTIES AND PUBLIC DISCLOSURE**

In accordance with Article 5 of the ISO Agreement and Sections 1.03 and 4.01 of the NYISO's Procedural Rules of Appeal, the Transmission Owners,<sup>1</sup> LIPA and the Power Authority of the State of New York<sup>2</sup> ("Member Systems") file this motion in opposition to appeals to the New York Independent System Operation, Inc. ("NYISO") Board concerning the April 18, 2001 decision of the Management Committee to approve revisions to the NYISO's Market Power Monitoring Plan to include provisions related to penalties and public disclosure. The Member Systems are comprised of the eight electric systems in the State of New York which transferred operational control over significant portions of their transmission facilities to the NYISO and are the largest load serving entities ("LSEs") in the New York control area. The Member Systems believe that the penalty and public disclosure provisions adopted by the Management Committee are a reasonable attempt to address existing weaknesses in the Market Power Monitoring Plan and that the appeals of that decision should be denied.

---

<sup>1</sup> The Transmission Owners constitute all of the Members of the Transmission Owners Sector of the NYISO Management Committee. They include: Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., New York State Electric and Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and Rochester Gas and Electric Corporation.

<sup>2</sup> LIPA and the Power Authority of the State of New York are Members of the Public Power/Environmental Sector of the NYISO Management Committee.

## **I. Background**

On April 18, 2001, the NYISO Management Committee approved a motion that the NYISO Board concur in a joint filing to be made at the Federal Energy Regulatory Commission to amend the NYISO's current Market Power Monitoring Plan in order to establish specified penalties related to conduct that results in mitigation under existing market power mitigation standards. The penalties would escalate with recurring conduct that results in mitigation. In addition, the proposed amendment provides for the disclosure of the identity of a party whose conduct results in mitigation two or more times within a 24 month period.

Contrary to the claims of the Appellants, the penalty and public disclosure provisions approved by the Management Committee are a limited and reasonable response by market participants, acting through the NYISO's Management Committee, to legitimate concerns with respect to a weakness in the NYISO's Market Power Monitoring Plan which should be addressed in order to provide adequate protection to consumers and LSEs against unjustified prices.

## **II. Rationale For the Penalty and Public Disclosure Provisions**

The measure adopted by the Management Committee seeks to address a weakness in the current Market Power Monitoring Plan: a market participant may repeatedly engage in conduct that results in mitigation, with impunity. If a seller's bid is mitigated, its bid is changed to the reference price for the unit, which is based on previously accepted bids with appropriate adjustments. Mitigation of a bid to a unit's reference price is not a "penalty", but replaces a bid that violated the mitigation thresholds with a bid consistent with what would be expected in a workably competitive market. Furthermore, the seller is paid the market clearing price rather than its bid if the market clearing price is higher than the

unit's reference price. It also should be noted that if a bid is mitigated but is not subject to the NYISO's Automatic Mitigation Process ("AMP"), the seller may retain the excessive payments received prior to the mitigation of its bid. The penalty provisions adopted by the Management Committee are expressly limited to the mitigation of conduct that is not covered by the AMP. Consequently, the penalty would apply only in cases where the seller otherwise would benefit from conduct that warrants mitigation.

Given the legitimate concern that the NYISO markets and other competitive electricity markets are vulnerable to the exercise of market power, particularly during periods when supplies are tight, it is appropriate for the NYISO to implement measures, such as those adopted by the Management Committee, that provide some deterrence to conduct that would violate the NYISO's market mitigation thresholds.

### **III. The Measure Adopted By the Management Committee Is Reasonable and the Objections Raised by the Appellants Are Unwarranted.**

Appellants contend that the measure adopted by the Management Committee would result in "draconian" penalties, depress competitive market prices and discourage generators from selling in the NYISO markets. The Member Systems believe that these concerns are not well founded.

First, the penalties included in the proposal are proportionate to the conduct that resulted in mitigation. The penalties apply to the specific amount of energy subject to mitigation, and consists of multiples of the LBMP for that specific amount of energy. The penalty begins at two times the LBMP for the mitigated amount of energy for the first mitigation and the multiple increases by one for subsequent mitigations. The penalties, therefore, are not open ended but are limited and reasonably related to that conduct subject to mitigation. Furthermore, the NYISO is invested with discretion to reduce or waive a penalty on a finding that imposing the penalty would be onerous or is not necessary

to deter conduct that would require market mitigation. This discretion provides an opportunity for a seller to demonstrate to the NYISO that specific circumstances existed that warrant a reduction or waiver of the penalty, and provides the NYISO with the ability to reduce or waive the penalty when circumstances would render its imposition inappropriate or excessive. For example, a supplier may legitimately demonstrate that operational conditions, such as a boiler tube leak, warranted the inclusion of a risk premium to cover the risk of a forced outage between the establishment of a day-ahead commitment and actual real time operation. As with any other authority invested in the NYISO, this discretion would have to be exercised in a non-discriminatory and a rational way.

Similarly, contentions that the penalty provisions would depress market prices and discourage generators from selling into the NYISO markets are unwarranted. Penalties would apply only to sellers whose conduct resulted in mitigation under the existing Market Monitoring Program and would not affect the market clearing price. Sellers in the NYISO markets have no reasonable expectation of receiving payments based on bids that violate the NYISO's market mitigation thresholds. Sellers will be attracted to the NYISO markets if the markets operate efficiently and produce competitive market clearing prices, including the higher prices that occur when generators are called upon to serve high levels of load.

Appellants also contend that there is no evidence that the exercise of market power is a problem in the NYISO markets and, therefore, that any effort to discourage such conduct is unnecessary. The Appellants point to a statement made by David Patton, the NYISO's Market Advisor, to the effect that "except for several isolated instances" suppliers have bid in a manner consistent with workable competition. Appellants neglect to mention that the exercise of market power on a relatively few occasions can result in very substantial overpayments to suppliers. For example,

Mr. Patton's analysis indicates that on one day, June 26, 2000, non-competitive conduct resulted in an impact in excess of \$100,000,000 in the NYISO energy markets. In addition, as Mr. Patton has noted, the NYISO markets are especially vulnerable to the exercise of market power during times of tight supplies and, given the current supply outlook, the vulnerability of the NYISO markets to abuses of market power will rapidly increase in the near future.

Appellants also object to the penalty measure on the grounds that it is discriminatory because it applies only to sellers and not to LSEs and Transmission Owners ("TOs"). It is clear, however, that bidding behavior by sellers is a very significant concern in the NYISO markets and other competitive electricity markets. The NYISO has detected bidding behavior by sellers in both its energy and ancillary services markets that has resulted in price mitigation and the imposition of bid caps. On the other hand, bidding behavior by LSEs has not been a problem in the NYISO markets and abusive bidding practices by LSEs have not been detected by the NYISO. Nor has the NYISO identified instances of market abuse by TOs with respect to the scheduling of transmission facilities. At the recent Joint Meeting of the NYISO Board and the Management Committee, Mr. Patton reaffirmed the absence of any evidence of abusive bidding practices by LSEs and raised no issues with respect to TO scheduling practices.

It is totally rational for the NYISO to address penalty provisions to the type of bidding behavior that has been demonstrated to be a serious concern, and that will be an increasing concern in the near future. If at the some point abusive bidding behavior by LSEs or TOs is found to be a problem, the application of the penalty provisions can be extended to include such behavior.

## **Conclusion**

The Member Systems submit that an amendment to the NYISO's Market Monitoring Plan to discourage conduct that results in market power mitigation is warranted. The measure adopted by the Management Committee appears to be a reasonable attempt to address that issue. Consequently, the Member Systems recommend that the NYISO Board concur in the Management Committee's action. However, should the NYISO Board decide that the measure adopted by the Management Committee is unacceptable, it is respectfully requested that the Board advise the Management Committee of their specific concerns.

AL69746