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August 27, 2010

VIA E-MAIL

Mr. David J. Lawrence
New York Independent System Operator, Inc.
10 Krey Boulevard
Rensselaer, NY 12144

Re: New York Independent System Operator, Inc.'s Draft Recommendations
Regarding the 2011-2014 Installed Capacity Demand Curve Reset

Dear Dave:

Pursuant to the request of the New York Independent System Operator, Inc. ("NYISO") and in accordance with the 2011-2014 Installed Capacity ("ICAP") Demand Curve Development Schedule developed by NYISO staff, Multiple Intervenors hereby submits these comments in response to NYISO staff's draft recommendations issued on August 13, 2010 regarding the 2011-2014 ICAP demand curve reset ("Draft Recommendations"). With the few exceptions detailed herein, Multiple Intervenors generally is supportive of the Draft Recommendations. Specifically, Multiple Intervenors strongly urges the adoption of the following modifications to the Draft Recommendations: (a) reduce the New York Control Area ("NYCA") ICAP demand curve's zero crossing point from 112% of the applicable minimum ICAP requirement to 110%; (b) reduce the escalation factor for the 2012/2013 and 2013/2014 ICAP demand curves from 2.4% to 1.7%; and (c) reduce the assumed level of excess capacity in years 4-30 of the nominal life of the proposed NYCA peaking unit from 1.0% to 0.5%.

BACKGROUND

As you may recall, on May 21, 2010, Multiple Intervenors advanced a proposal for consideration of the NYISO and market participants as a means to resolve the current 2011-2014 ICAP demand curve reset process absent litigation, while simultaneously remaining consistent with the requirements of the NYISO Market Administration and Control Area Services Tariff ("Services Tariff"), the ICAP Manual and Federal Energy Regulatory Commission ("FERC") precedent relating to the ICAP demand curves. Multiple Intervenors advocated that the NYISO complete the process of developing the ICAP demand curves for the 2011-2014 period, as required by the Services Tariff. Significantly, however, under Multiple Intervenors' proposal, the implementation of those ICAP demand curves would be

delayed until a trigger is activated indicating a need for new resources in the near-term, thereby leaving the existing ICAP demand curves in effect until such time.¹

Given (i) the projected lack of need for new resources from a reliability perspective during the 2011-2014 period, as determined by the 2009 Reliability Needs Assessment (“RNA”) and the Draft 2010 RNA and (ii) the projected substantial level of capacity excess during the 2011-2014 period, Multiple Intervenors continues to believe that adoption of its proposal represents an appropriate outcome for the ongoing ICAP demand curve reset process. Significantly, however, based on the general lack of support for Multiple Intervenors’ proposal to date, and the fact that the proposal was presented as a compromise to avoid litigation which now appears necessary, Multiple Intervenors is left no choice but to proceed with its litigation positions with respect to this matter.

DELIVERABILITY COSTS

Prior to addressing its recommended modifications to the Draft Recommendations, Multiple Intervenors hereby indicates its strong support for NYISO staff’s recommendation to exclude deliverability costs from the cost of new entry for the proposed NYCA peaking unit. NYISO staff correctly notes that the inclusion of deliverability costs within the cost of new entry for the proposed NYCA peaking unit is completely inconsistent with the fundamental purpose of imposing the deliverability requirements – to require new generators seeking to sell capacity to pay the costs of transmission system upgrades necessary to make their capacity deliverable, thereby providing more effective economic signals regarding the most efficient locations for new entry.²

Moreover, the inclusion of deliverability costs within the cost of new entry for the proposed NYCA peaking unit would directly contradict the cost allocation methodology approved by FERC with respect to any required deliverability upgrades. In approving the deliverability requirements, FERC clearly held that consumers would be exposed to the costs of deliverability only in very limited circumstances where the minimum feasible highway

¹ The rationale and support for Multiple Intervenors’ proposal is discussed in further detail in its May 21, 2010 presentation to the Installed Capacity Working Group, which is incorporated herein by reference.

² *New York Independent System Operator, Inc. and New York Transmission Owners*, 126 FERC ¶ 61,046 at P 8 (2009).

upgrade exceeds the minimum upgrade required to make the generator at issue deliverable.³ Specifically, FERC declared:

[w]e find that the Filing Parties' proposed approach allocates costs of transmission consistent with Commission policy and recognizes the competing interests of those involved. Entities other than interconnection customers [generators], such as LSEs [and, thus, consumers], would be exposed to upgrade costs only to the extent that the 90 percent threshold is not realized for highway facilities (i.e., only if the minimum feasible upgrade is more than 90 percent of the size of the actual upgrade).⁴

To include deliverability costs within the cost of new entry for the proposed NYCA peaking unit would require consumers to pay for all deliverability costs in direct contravention to the cost allocation methodology approved by FERC.

Furthermore, the inclusion of deliverability costs within the cost of new entry for the proposed NYCA peaking unit in light of the projected lack of need for new resources and forecasted capacity excess for the 2011-2014 period would create an unjustified wealth transfer from consumers to existing generators. A condition attendant to the approval of the deliverability requirements by the NYISO's market participants was the grandfathering of all then existing generators, thereby granting them deliverability rights at no cost. The inclusion of deliverability costs during the 2011-2014 period when no new resources are needed from a reliability perspective, therefore, would result in substantial windfall profits to the existing generators that were granted deliverability rights free of cost.

NYCA ICAP DEMAND CURVE ZERO CROSSING POINT

NYISO staff should modify its recommendation regarding adjustments to the ICAP demand curves' slope and length, and adopt a reduction to the zero crossing point of the NYCA ICAP demand curve from 112% of the applicable minimum ICAP requirement to 110%. Throughout the current ICAP demand curve reset process, Multiple Intervenors continually has raised concerns regarding the growing level of excess capacity in New York, the costs associated therewith to consumers, and whether consumers continue to derive tangible benefits from such excess capacity. In fact, in just the year that has lapsed since the

³ See, e.g., *New York Independent System Operator, Inc. and New York Transmission Owners*, 122 FERC ¶ 61,267 at P 30-32 and 46 (2008); and *New York Independent System Operator, Inc. and New York Transmission Owners*, 126 FERC ¶ 61,046 at P 43-44 (2009).

⁴ *New York Independent System Operator, Inc. and New York Transmission Owners*, 122 FERC ¶ 61,267 at P 46 (2008).

development of the 2009 RNA, the projected level of capacity excess above the current 18 percent IRM during the 2011-2014 period has more than doubled from nearly 5 percent under the 2009 RNA to more than 10 percent according to the Draft 2010 RNA.

Furthermore, despite such persistent levels of significant excess, substantial amounts of new capacity are proposed to commence operation in the Rest of State capacity region during the next four years.⁵ These factors indicate that the NYCA ICAP demand curve likely is sending artificially-high price signals regarding the value of excess capacity. Accordingly, action must be taken to address this problem and reduce the level of excess capacity that consumers are funding to remain on the system, which provides, at best, marginal benefits. Thus, Multiple Intervenors recommends that the NYISO reduce the zero crossing point of the NYCA ICAP demand curve to 110% of the applicable minimum ICAP requirement to aid in sending more effective economic signals to investors that capacity excess greater than 10 percent of the minimum requirement does not provide additional benefits and, thus, has no corresponding value warranting compensation. Absent this modification, the NYCA ICAP demand curve will perpetuate the existence of substantial levels of capacity excess by providing artificially-high price signals regarding the value of such excess.

The rationale provided by NYISO staff and its consultants for rejecting this modification, at this time, is unacceptable and inconsistent with the requirements of the Services Tariff. According to NYISO staff and its consultants, the zero crossing point of the ICAP demand curves cannot be modified during a period of excess capacity because such a modification would have adverse impacts on the revenue expectations of existing supply resources. Rather, NYISO staff and its consultants allege that such a change only can be considered during periods at which the capacity market is at or near equilibrium to ensure that adverse impacts to expected generator revenues do not result.⁶

Importantly, however, Section 5.14.1.2 of the Services Tariff expressly mandates the “appropriate shape and slope of the ICAP Demand Curves, and the associated point at which the dollar value of the ICAP Demand Curves should decline to zero” as one of four factors that must be considered during each triennial ICAP demand curve reset process. Therefore, the Service Tariff provides all market participants with clear notice that the zero crossing

⁵ For example, the following new resources are proposed to commence operation during the next four years: (a) the 635 MW Empire Generating Facility in Zone F; (b) the proposed 630 MW CPV Valley Energy Center project in Zone G; and (c) the proposed 1,000 MW Cricket Valley Energy project in Zone G.

⁶ Multiple Intervenors is concerned that this preoccupation with preserving generator revenues, even if dependent upon excess payments by consumers, is preventing the true consideration, and an adequate evaluation, of the optimal zero crossing point for the NYCA ICAP demand curve.

point of the ICAP demand curves is a factor subject to evaluation and potential modification during each triennial review process.

Moreover, since the implementation of the ICAP demand curves, the market has experienced a persistent level of excess capacity – as noted above, this excess has continued to increase significantly over the past several years and is projected to continue increasing during the 2011-2014 period. Therefore, the position of NYISO staff and its consultants that adjustments to the zero crossing point only are appropriate during periods at or near equilibrium essentially renders this tariff-mandated factor for review meaningless because, absent modification of existing price signals, the market is unlikely to be at or near equilibrium at any time during the foreseeable future. Accordingly, and consistent with the requirements of the Services Tariff, Multiple Intervenors recommends that NYISO staff adopt a reduction in the zero crossing point for the NYCA ICAP demand curve from 112% of the applicable minimum ICAP requirement to 110% in order to address the issue of substantial capacity excess and more accurately reflect a level of excess which continues to derive benefit for consumers.

ESCALATION FACTOR

While Multiple Intervenors does not oppose NYISO staff's proposal to utilize a forecast of average inflation as the escalation factor to determine the parameters of the 2012/2013 and 2013/2014 ICAP demand curves, Multiple Intervenors adamantly opposes the NYISO staff's proposed 2.4 percent escalation factor. The proposed escalation factor is based on the average 10-year forecasted inflation rates for the 2010-2019 period, as determined by the Survey of Professional Forecasters published by the Federal Reserve Bank of Philadelphia. Multiple Intervenors fails to comprehend any legitimate rationale for utilizing a forecast of inflation rates for a period that is significantly longer than the 2011-2014 period covered by the ongoing ICAP demand curve reset. Indeed, Multiple Intervenors questions what, if any, relevance the projected level of inflation in 2019 has on determining the parameters of the 2012/2013 and 2013/2014 ICAP demand curves. Moreover, the data relied upon by the NYISO has since been revised, decreasing the forecasted future inflation rates due to less optimistic projections for the country's economic recovery than previously were being predicted.

Accordingly, Multiple Intervenors urges the NYISO to determine the appropriate escalation factor based on an average forecasted inflation rate that is more representative of the period actually covered by the ongoing ICAP demand curve reset process. Specifically, Multiple Intervenors recommends that the NYISO utilize an escalation factor of 1.7 percent. Multiple Intervenors derived this recommended escalation factor based on the average of three publicly-available inflation rate forecasts, covering the 2010-2014 period, including the recently updated Survey of Professional Forecasters published by the Federal Reserve Bank of Philadelphia.

The table below shows the average inflation rate forecast for the 2010-2014 period from each source and the resulting average forecasted inflation rate for the 2010-2014 period recommended for use by Multiple Intervenors.⁷

Data Source	Average Forecasted Inflation Rate for 2010-2014
SPF	1.9%
OMB	1.7%
CBO	1.5%
<i>Average</i>	<i>1.7%</i>

Adoption of an excessive escalation factor based on a single forecast for an irrelevant time period, as proposed by NYISO staff, would result in artificially-high capacity prices for consumers. Multiple Intervenors' recommended escalation factor, in contrast, reflects the average of three different forecasts encompassing an appropriate time period for consideration in determining the parameters of the 2012/2013 and 2013/2014 ICAP demand curves.

ASSUMED LEVEL OF EXCESS CAPACITY

Multiple Intervenors applauds NYISO staff's recommendation to reduce the assumed level of excess capacity over the final 27 years of the nominal life of the proposed NYCA peaking unit from 1.5 percent to 1.0 percent. Multiple Intervenors contends, however, that such assumption is inconsistent with the requirements of the Services Tariff and should be further reduced to 0.5 percent – equal to the assumed level of excess for the three years covered by the ongoing ICAP demand curve reset process.

As noted in the Draft Recommendations, the use of the 0.5 percent excess comports with the requirements of Section 5.14.1.2 of the Services Tariff that energy and ancillary service revenues be estimated “under conditions in which the available capacity would equal

⁷ See Federal Reserve Bank of Philadelphia, *Third Quarter 2010 Survey of Professional Forecasters* (August 13, 2010) at Table Seven, available at <http://www.phil.frb.org/research-and-data/real-time-center/survey-of-professional-forecasters/2010/spfq310.pdf> (hereinafter, “SPF”); U.S. Office of Management and Budget, *Mid-Session Review: Budget of the U.S. Government – Fiscal Year 2011* (July 23, 2010) at 9, available at http://www.whitehouse.gov/sites/default/files/omb/assets/fy2011_msr/11msr.pdf (hereinafter, “OMB”); and U.S. Congressional Budget Office, *The Budget and Economic Outlook: An Update* (August 2010) at 78, available at <http://www.cbo.gov/ftpdocs/117xx/doc11705/08-18-Update.pdf> (hereinafter, “CBO”).

or slightly exceed the minimum Installed Capacity requirement.” However, Multiple Intervenors disagrees with NYISO staff’s assertion that this tariff requirement applies only to the three-year period covered by the ICAP demand curve reset, and, thus, the tariff is silent regarding the assumptions that apply to the remaining 27 years of the nominal life of the proposed NYCA peaking unit. In fact, FERC expressly has determined that the conditions imposed by Section 5.14.1.2 of the Services Tariff apply equally to the remaining 27 years of the nominal life of the proposed NYCA peaking unit.⁸ Accordingly, because the same tariff requirements apply to both periods and the NYISO acknowledges that the assumption of 0.5 percent excess comports with the tariff requirements, this assumed level of capacity excess should apply to the entire nominal life of the proposed NYCA peaking unit.⁹

Moreover, NYISO staff has failed to provide any compelling justification for the need to assume a greater level of excess during the remaining 27 years of the nominal life of the proposed NYCA peaking unit than that assumed for the first three years. The unjustified assumption of additional excess places additional upward pressure on the cost of new entry for the proposed NYCA peaking unit, thereby artificially increasing capacity prices to consumers. Such an assumption merely exacerbates the issues associated with the existing ICAP demand curves with respect to perpetuating the continued existence of an unreasonable level of excess capacity. Accordingly, to provide more effective economic signals regarding the value of excess capacity, Multiple Intervenors recommends that NYISO staff reduce the assumed level of excess during the remaining 27 years of the nominal life of the proposed NYCA peaking unit from 1.0 percent to 0.5 percent, consistent with the level of excess assumed during the first three years.

⁸ *New York Independent System Operator, Inc.*, 122 FERC ¶ 61,064 at P 31 (2008).

⁹ Multiple Intervenors is unaware of any market participant contending that 0.5 percent assumed excess is inconsistent with the requirements of Section 5.14.1.2 of the Services Tariff.

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If you have any questions regarding these comments or would like to discuss them further, please do not hesitate to contact me directly at (518) 320-3437, or via e-mail at gbissell@couchwhite.com.

Respectfully submitted,

MULTIPLE INTERVENORS

Garrett E. Bissell

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GEB/dap

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