UNITED STATES OF AMERICA 93 FERC ¶ 61,058
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: James J. Hoecker, Chairman;
William L. Massey, Linda Breathitt,
and Curt Hébert, Jr.

Morgan Stanley Capital Group Inc. v. New York Independent System Operator, Inc. — Docket No. EL00-103-000

ORDER ON COMPLAINT

(Issued October 25, 2000)

On August 23, 2000, Morgan Stanley Capital Group Inc. (Morgan Stanley) filed a complaint against New York Independent System Operator, Inc. (NYISO). Morgan Stanley requests that the Commission order NYISO to temporarily postpone its planned auction of two- and five-year Transmission Congestion Contract (TCC)[1] products until various software and market flaws in the NYISO are corrected. Morgan Stanley claims that a TCC auction in a flawed market would place market participants in an unfair position of having to analyze and purchase TCCs without correct price signals and that without correct price signals, market participants cannot protect against or otherwise mitigate congestion risk.

We deny Morgan Stanley's complaint on the basis that market participants would not be disadvantaged by the sale of two- and five-year TCCs since the market clearing prices would reflect any uncertainty perceived by all market participants. The difficulties Morgan Stanley notes, to the extent they have not yet been corrected, are faced by all market participants, not just Morgan Stanley. Additionally, NYISO's secondary auctions (monthly Reconfiguration Auctions) limit risks associated with longer-term TCCs.

Background

[1] A TCC gives the holder the ability to hedge against congestion costs associated with transmitting energy from point of injection to point of withdrawal. See, Central Hudson Gas & Electric Co., et al., 86 FERC ¶ 61,062 (1999).

Morgan Stanley is a power marketer and a participant in the brokering markets and TCC auctions operated by NYISO. Morgan Stanley also has approval to sell at market-based rates.[2]

There have been several auctions of TCCs. After a transitional auction in September 1999, six-month and two-year TCCs were sold at the April 2000 auction.[3] On July 20, 2000, the NYISO Business Issues Committee adopted a provision to reduce the number of six-month TCCs from 65% to 35% of the market capability and sell the 30% of market capability as two-year and five-year TCCs (the 30% is split equally between the two- and five-year TCCs). NYISO plans to implement these changes during the Autumn TCC Auction, which runs from September 1 to October 27, 2000.

Complaint

Morgan Stanley points out that the Commission granted NYISO Temporary Extraordinary Procedures (TEP) authority to correct inconsistent energy pricing caused by pricing problems and software errors.[4] Morgan Stanley states that in its last order granting a TEP extension, the Commission ordered NYISO to submit a detailed report concerning each price correction that NYISO made under the TEP during the period of June 1, 2000 to September 1, 2000. The report also directed NYISO to provide details regarding corrective measures that it has taken or is taking to resolve situations in which it exercised its TEP authority.

Morgan Stanley states that the NYISO market is in transition and that various software and design flaws exist in the NYISO's pricing model. As a result, Morgan Stanley believes that accurate price signals for congestion risks don't exist in the NYISO markets, and market participants cannot mitigate against congestion risk. Morgan Stanley complains that NYISO's plan to auction two- and five-year TCC commitments threatens market participants and bidders with substantial and possibly irreparable injury, since TCC prices

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[2] Morgan Stanley Capital Group, Inc. 69 FERC ¶ 61,175 (1994).

[3] NYISO held Reconfiguration Auctions in June, July and August in which TCCs with a duration of one month were sold.

[4] The Commission first approved the TEP for NYISO for a period of 90 days from commencement of operations on November 18, 1999, until February 16, 2000. New York Independent System Operator, Inc., 88 FERC ¶ 61,228 (1999). Subsequent extensions were granted. See, New York Independent System Operator, Inc., 90 FERC ¶ 61,320 (2000) and New York Independent System Operator, Inc., 92 FERC ¶ 61,051 (2000).

that are artificially biased will remain in force for two and five years, perpetuating the effects of the flawed market.

Morgan Stanley also asserts that NYISO is uncertain about its own transmission system and has instituted a long-term transmission study and that the NYISO market model is undergoing continual changes. Therefore, Morgan Stanley states that it is unreasonable for NYISO to sell long-term TCC products in a market that NYISO must change in the near term and at the conclusion of its transmission study. Morgan Stanley maintains that NYISO should only offer long-term TCC products once it has created an accurate and viable market system. It states that congestion charges in the NYISO model are to be based on actual market prices of energy; however, the unstable nature of the marketplace ensures that they will not be priced based on actual energy prices.

Morgan Stanley also finds fault with its access to NYISO's Real-Time Market (RTM). As a power marketer, Morgan Stanley claims that it has no access to the RTM but that load-serving entities and generators do have such access. As a result, it states that market participants that trade in the RTM will influence prices and all market participants will not be able to protect themselves appropriately.

Answer to the Complaint

NYISO

NYISO states that the Commission should reject the complaint because it is inappropriately filed under the Commission's Fast-Track processing procedures. NYISO submits that Morgan Stanley should not have waited until August 23, 2000, to file this complaint for an auction scheduled to begin on September 1, 2000. NYISO asserts that its Business Issues Committee endorsed the issuance of long-term TCCs on July 20, 2000 with nearly 90% of the market participants voting in favor of the measure. It also states that Morgan Stanley failed to participate in the committee decision-making process and has not used the NYISO's established appeals procedures.

NYISO also believes that the complaint should be rejected because NYISO's Open Access Transmission Tariff (OATT) allows NYISO to issue long-term TCCs and Morgan Stanley's complaint does not adequately explain how transitional flaws, temporary uncertainty and other remedial actions, which the Commission has already indicated have little effect on TCC valuation, will obstruct Morgan Stanley's TCC purchasing decisions.

NYISO maintains that TCCs in prior auctions have been priced properly and that there have been no previous allegations of market flaws affecting those TCC auctions. Additionally, monthly Reconfiguration Auctions allow market participants to make adjustments in each month during the life of any TCC and to compensate for any long-term risk that Morgan Stanley claims are present.

NYISO states that Morgan Stanley's inability to participate in the RTM for energy is irrelevant to the question of whether long-term TCCs should be offered in the current auction. NYISO submits that TCCs are not sold in the RTM for energy, so ownership of TCCs has no real impact in the RTM for energy. NYISO asserts that even if there were an impact, the impact would be the same for short-term and long-term TCCs.

NYISO contends that Morgan Stanley's complaint does not describe any identifiable harm related to the sale of long-term TCCs. Rather, according to NYISO, Morgan Stanley's complaint reflects a general dissatisfaction with NYISO-administered markets and fails to show the harm created by the sale of long-term TCCs. NYISO states that it does not believe that any radical overhaul is needed to cure its market flaws, many of which have been, or will be, remedied.[5] NYISO states that Morgan Stanley will not be disadvantaged, since market clearing prices for TCCs would reflect any perceived market uncertainty or instability, and that any problems would equally affect all market participants.

Notice, Motions to Intervene and Other Pleadings

Notice of Morgan Stanley's complaint was published in the Federal Register, 65 Fed. Reg. 52,725 (2000), with protests, answers, and motions to intervene required to be filed on or before September 5, 2000. Three intervenors commented on the complaint. In a late-filed notice of intervention, the New York Public Service Commission (New York Commission) states that while it is sympathetic to the concerns raised by Morgan Stanley, it does not support interfering with the auction now taking place. However, the New York Commission recommends that the results of all of the TCC auctions be carefully evaluated by NYISO and the Commission before a final decision is made regarding the mix of products to be sold in the spring auction. Accordingly, it requests that the Commission direct the NYISO to evaluate the TCC auctions' results and submit that evaluation and recommendations for future auctions in the 15-month report on the first year of operation required by the Commission in ordering paragraph K of its January 27, 1999 order in Docket No ER97-1523-000, et al.[6] Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc. (ConEd) support Morgan Stanley's proposal. They

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[5]See, New York Independent System Operator, Inc.'s, combined compliance filing and report in Docket Nos. ER00-1969-000, EL0057-000, EL00-60-000, EL00-63-000, EL00-64-000, EL00-67-000, ER00-2624-000, ER00-3038, EL00-70-001 and EL00-82-000.

[6]Central Hudson Gas & Electric Corporation, et al., 86 FERC ¶ 61,061 (1999).

believe that the proposed limitation on TCCs is necessary in view of the current lack of stability in the NYISO markets. The Member Systems[7] assert that in order to balance the impacts of the current volatility in the NYISO markets with the desire of some transmission customers for longer term TCCs, the Commission should direct the NYISO to limit the term of TCCs offered in the upcoming TCC auction to no more than two years.

Discussion

Procedural Matters

Under Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2000), the timely, unopposed motions to intervene serve to make the movants parties to this proceeding. At this early stage of the proceeding, given the lack of undue prejudice or delay and given the parties' interests, we also find good cause to grant under Rule 214 the unopposed, untimely notice of intervention in this proceeding. Similarly, the Commission grants NYISO's motion for leave to submit its answer one day out of time.

Complaint

TCC auctions of products with durations of six months to five years are consistent with the NYISO's OATT.[8] The NYISO's proposal to auction a portion of TCCs as long-term TCCs was approved in July by nearly 90% of market participants. Thus, an overwhelming majority of market participants see value in the offer of long term TCCs at this time. NYISO has a governance process through which its actions are approved and this process allows market participants to have input prior to a decision being made. If a party is dissatisfied with the outcome, it can use the NYISO appeals process to raise its issue(s). Morgan Stanley had that opportunity here but failed to exercise it. Morgan Stanley should have used the NYISO established process (one which the Commission approved through its approval of the NYISO OATT) to seek any modifications that it felt were necessary. Morgan Stanley has not presented a sufficient basis for changing at the last minute the auction that was approved through NYISO's process and upsetting the expectations of the market participants.

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[7]The Member Systems are comprised of five of the eight electric systems in the State of New York: Central Hudson Gas & Electric Corporation, LIPA, the Power Authority of the State of New York, Niagara Mohawk Power Corporation, and Rochester Gas and Electric Corporation.

[8]See, ISO OATT, Attachment M, § 8.4; Central Hudson Gas & Electric Corporation, et al., 86 FERC ¶ 61,061 (1999); order on reh'g, 88 FERC ¶ 61,138 (1999).

We agree with Morgan Stanley that the NYISO's Day Ahead and Real-Time energy markets have experienced a number of significant problems, but we do not agree that these transitional problems are a basis for delaying the auction of two and five year TCCs, as Morgan Stanley requests. A major purpose of a TCC is to provide the holder with a hedge against congestion costs. The problems in NYISO's Day Ahead and Real-Time energy markets do not keep TCCs from performing this function. Since the imperfections of the NYISO are well known, TCC prices will reflect those imperfections. We agree with NYISO that Morgan Stanley would not be disadvantaged relative to other TCC market participants, since any uncertainty would be equally applicable to all market participants. We also agree with NYISO that its monthly Reconfiguration Auctions will allow market participants to make adjustments for any previous decisions and limit the long-term impact of the two- and five-year TCC products. Morgan Stanley has also mis-characterized the nature of NYISO's long-term transmission study. The long-term transmission study is intended to address alternative dispatch scenarios, including potential transmission upgrades and expansions as expected new capacity is added to the market over the next several years.

New York Commission requests that the Commission direct NYISO to evaluate the TCC auction results and submit that evaluation and recommendations for future auctions in a report filed with the Commission. Since NYISO reports the results of its auctions on its website and since the members of NYISO can bring up any issues through the appropriate committee within NYISO, we see no compelling reason to require a report with the Commission at this time.

Accordingly, we deny the complaint.

<u>The Commission orders</u>:

Morgan Stanley's complaint is denied.

By the Commission.

(S E A L)

David P. Boergers,
Secretary.