

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

New York Independent System) Docket No. ER11-2224-000
Operator, Inc.)

**MOTION FOR LEAVE TO INTERVENE AND PROTEST OF THE
ELECTRIC POWER SUPPLY ASSOCIATION**

Pursuant to Rules 211, 212 and 214 of the Federal Energy Regulatory Commission's ("FERC" or the "Commission") Rules of Practice and Procedure, 18 C.F.R. §§ 385.211, 212 and 385.214 (2010), the Electric Power Supply Association ("EPSA")¹ respectfully files for leave to intervene and protest the November 30, 2010 filing by the New York Independent System Operator, Inc. ("NYISO") proposing changes to key parameters of the Installed Capacity ("ICAP") Demand Curves for Capability Years 2011/2012, 2012/2013 and 2013/2014 for the NYISO capacity market.²

As filed, EPSA submits the revised Demand Curves and underlying net cost of new entry ("Net CONE") values are significantly understated and not reflective of reasonable costs faced by generators, and are therefore insufficient to signal efficient investment in new or existing resources, which threatens long-term market stability and reliability. The NYISO Proposal is unjust, unreasonable, and contrary to the Commission's original intent in approving the ICAP Demand Curves. Accordingly, EPSA requests that the Commission direct

¹ The comments contained in this filing represent the position of EPSA as an organization, but not necessarily the views of any particular member with respect to any issue.

² *New York Independent System Operator, Inc.*, Tariff Revisions to Implement Revised ICAP Demand Curves for Capability Years 2011/2012, 2012/2013, 2013/2014, Docket No. ER11-2224-000 (filed November 30, 2010)("NYISO Proposal").

the NYISO to modify the ICAP Demand Curves as discussed herein, to incorporate (1) realistic excess capacity risk assumptions; and, (2) deliverability upgrades and New York City property tax costs into the Net CONE calculation. These changes are necessary to ensure the fundamental purpose of the Demand Curves is met, which is to provide the proper signals to suppliers to make the necessary investments to retain existing and build new resources in time to meet New York's reliability needs. For a more detailed discussion of these issues, EPISA has also reviewed and supports the requested modifications contained in the intervention and protest (and accompanying affidavits) filed concurrently in this proceeding by the Independent Power Producers of New York, Inc. ("IPPNY"). Additionally, EPISA has reviewed and supports the requested modifications contained in the protest (and accompanying affidavits) filed concurrently in this proceeding by the New York City Suppliers.

I. INTERVENTION AND COMMUNICATIONS

EPISA is the national trade association representing competitive power suppliers, including generators and marketers. These suppliers, who account for 40 percent of the installed generating capacity in the United States, provide reliable and competitively priced electricity from environmentally responsible facilities. EPISA seeks to bring the benefits of competition to all power customers.

Many of EPISA's member companies have made significant investments in generation assets in New York and/or are market participants in the NYISO ICAP market, and consequently, will be affected by the NYISO Proposal in this

proceeding. EPSA member companies are also active participants in NYISO stakeholder processes, including the stakeholder process leading to the instant filing. Further, EPSA and its members have been and continue to be active in many of the Commission's ongoing proceedings on NYISO issues. Accordingly, EPSA has a direct and substantial interest in the outcome of this proceeding that cannot be adequately represented by any other party. Therefore, allowing EPSA to actively participate in this proceeding would be in the public interest.

All pleadings, correspondence and other communications concerning this proceeding should be directed to:

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II. BACKGROUND

In 2003, the Commission first approved the ICAP Demand Curves for the NYISO Capacity market's three areas – New York City (“NYC”), Long Island (“LI”), and the entire New York Control Area (“NYCA”) – to replace a critically flawed capacity market structure that led to severely depressed ICAP market clearing prices.³ The ICAP Demand Curves are used in determining the ICAP price in the monthly ICAP spot market auctions. The NYISO Market Administration and Control Area Services Tariff (“Services Tariff”) requires that a periodic review of the Demand Curves be undertaken every three years in

³ *New York Independent System Operator, Inc.*, 103 FERC ¶ 61, 201, *reh'g denied*, 105 FERC ¶ 61, 108 (2003).

accordance with a specified schedule and procedures, including use of an outside consultant to perform required analysis, a stakeholder process, NYISO Board review of proposed changes to the Demand Curves, and a FERC filing, among other things.

This is the third periodic review, or Demand Curve “reset” process, that has been undertaken to date. The current Demand Curve reset process for the 2011-2014 timeframe commenced in December 2009 when NYISO retained National Economic Research Associates and Sargent and Lundy, as NERA’s subcontractor (collectively, “NERA”) to conduct a comprehensive analysis and provide recommendations on the various parameters used to establish the Demand Curves.

Importantly, the Demand Curve reset process determines the Net CONE of the proxy peaking unit(s) and the other parameters used to establish the NYC, LI, and NYCA Demand Curves. The NYISO Proposal poses a number of significant concerns for suppliers, including the absence of deliverability costs or property taxes (for NYC) in the Net CONE for the proxy units, as well the NYISO’s arbitrary reduction of expected levels of excess capacity during the lifetime of the proxy units, among others.

I. PROTEST

A. The Basis and Importance of Capacity Markets

Due to market mitigation mechanisms and other ways in which markets artificially suppress market prices, market experts have reported that generators generally do not earn sufficient revenues to recover the fixed costs of building

new plants.⁴ Thus, administratively determined resource adequacy structures have been put in place to ensure that capacity needs are fulfilled and correct price signals are reaching investors. Whether an ISO has a formal capacity auction mechanism in place or utilizes a more basic Resource Adequacy (“RA”) program that requires bilateral contracting for capacity, the goals of both types of programs remain the same. The two historical goals of any RA program have been: (1) to maintain future reliability of the system; and, (2) to attract the necessary amount of investment in new and existing resources necessary to do so.⁵ In approving the NYISO ICAP Demand Curves, the Commission determined that:

[W]e conclude...there is a reasonable expectation that it will achieve the goal of improving reliability in New York, as well as promoting greater stability in the ICAP and energy markets. The proposed Demand Curve rests on a more rational economic basis than the current demand curve, as it more realistically reflects the economic value of capacity reserves.

[T]he proposed modification to NYISO’s ICAP market will benefit customers because it will provide better price signals to investors for the construction of new generation, encourage the formation of long-term bilateral transactions, and reduce incentives to withhold capacity.⁶

More recently, public policy objectives have been included as an additional goal of RA programs, as more and more states institute renewable portfolio standards, and therefore need to attract the investment necessary for

⁴ *Testimony of Joseph E. Bowring, Independent PJM Market Monitor at the Pennsylvania PUC Hearing on Current and Future Wholesale Electricity Markets.* (October 23, 2008), pp. 7-11.

⁵ See: *Order Conditionally Accepting Midwest Independent Transmission System Operator Tariff Sheets to Start Energy Markets and Establishing Settlement Judge Procedures*, 108 FERC ¶ 61, 163 at P 397 (August 6, 2004); *Initial Order on Reliability Pricing Model*, 115 FERC ¶ 61, 079 at P 29 (April 20, 2006); *Order Accepting ISO-NE LICAP Settlement*, 115 FERC ¶ 61, 340 at P 113 (June 16, 2006).

⁶ *New York Independent System Operator*, 103 FERC ¶ 61, 201, PP 35-36 (2003).

renewable energy to be viable and reliable, as well as incent increased participation by demand response and energy efficiency resources. New York is among the states with aggressive renewable portfolio standards, and has also experienced an increase in participation by demand side resources. Further adding to these operational challenges, near term environmental regulations are expected to result in premature generator retirements affecting various states and regions, including New York State.⁷

Several markets meet these stated RA goals by holding an auction that procures capacity on a multi-year forward basis in order to signal investment needs several years in advance. In New England, one of the first markets to institute a forward capacity market, that market evolved as a direct result of the Commission's concern that bilateral Reliability Must Run ("RMR") contracts would have a negative effect on competitive markets. The Commission held that:

RMR agreements suppress market-clearing prices and deter investment in new generation. Moreover, the market participants that pay for the agreements pay out-of-market prices for the service provided under the RMR agreements, which broadly hinders market development and performance.⁸

In a December 2006 order approving PJM's RPM settlement, the Commission noted that it "must approve market designs and rate policies that elicit sufficient investment in energy, transmission and demand response," and stated the Commission approved the RPM settlement, with conditions, "because

⁷ See New York Independent System Operator, Reliability Needs Assessment, Final Report, September 2010 ("NYISO 2010 RNA") at 41-55. Available at: http://www.nyiso.com/public/media_room/press_releases/index.jsp.

⁸ *Bridgeport Energy, LLC*, 118 FERC ¶ 61, 243 at P 41 (2007) (fns. omitted).

it achieves those goals, and ensures just and reasonable rates.”⁹ The RPM settlement and subsequent approval by the Commission stemmed from an earlier finding by the Commission that, as a result of a combination of factors, PJM’s market rules at that time were unjust and unreasonable because they failed to set prices adequate to ensure sufficient resources.¹⁰ Both the PJM and ISO-NE forward capacity markets have continued to be refined since their inception, including addressing important operational issues such as managing increasing amounts of demand response and variable resources on their respective systems.

In sum, it should be noted that capacity revenues are more important today than ever before to provide incentives for investment in both new and existing generation resources given the newly mandatory reliability standards and the challenging policy demands of renewable energy goals. Unfortunately, the NYISO’s proposed changes to the Demand Curves inject considerable regulatory uncertainty and risk into the capacity market framework at a time when long-term market stability is critical to encourage necessary investment.

B. The Commission Must Ensure The Demand Curves Are Set Correctly

Without question, the proper setting of the Demand Curves for the next three-year cycle starting in May 2011 is the most important issue for the health of the wholesale competitive markets in New York in terms of sending appropriate market signals and enhancing reliability. As such, it is imperative that the NYISO

⁹ *PJM Interconnection, L.L.C.*, Order Denying Rehearing and Approving Settlement Subject to Conditions, 117 FERC ¶ 61,331 at P1 (December 22, 2006).

¹⁰ *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 1-6 (April 20, 2006).

utilizes a fair and balanced process in proposing any changes to its tariff and makes reasonable assumptions relating to key market parameters. Particularly at this time when there will be a need for enormous amounts of capital investment, whether in new or retrofits to existing facilities, suppliers, investors and other stakeholders must be confident that price signals will be viable over the long-term to support necessary investments.

Put simply, the NYISO Proposal threatens to undermine confidence in the Demand Curves and will create greater regulatory uncertainty and risk. As filed, the Demand Curves are significantly understated, and thus, are unjust and unreasonable, due to the NYISO's exclusion of deliverability costs or property taxes (for NYC) in the Net CONE for the proxy units, as well the NYISO's arbitrary reduction of expected levels of excess capacity during the lifetime of the proxy units, as discussed in more detail below, among other changes. All reasonable costs that a new entrant would face should be included in setting the reference prices for the Demand Curves, and they must be set correctly during each periodic review to ensure there is no price suppression. Indeed, that is the concept behind the triennial re-set process, i.e., to accurately reflect the current cost of new entry. EPSA urges the Commission to carefully scrutinize whether the NYISO filing is true to the tariff's original intent. As stated by Dr. David Patton, the NYISO's Market Monitor, in his affidavit accompanying the NYISO Proposal:

If the assumptions are not realistic, then there can be no expectation that the market will facilitate efficient investment as reality differs substantially from the assumptions. In particular, unrealistic assumptions that lower the Demand Curve will produce economic signals that will likely be insufficient

to incent investors to build new resources when necessary to satisfy the minimum capacity requirements if the new resources have costs similar to the peaking resource that is used to establish the Demand Curves.¹¹

It is critical to investors, market participants and potential new market entrants that there is “process integrity” surrounding the NYISO Proposal and the revised Demand Curves, including the Commission’s oversight of these markets. The Commission must be the ultimate arbiter of these markets and as such, be willing to make the hard calls on difficult and complex matters, such as those presented in this proceeding. Therefore, EPSA requests that the Commission ensure the NYISO’s Demand Curves are set correctly to incent the construction of new capacity and retention of existing capacity to maintain electric system reliability, and ensure the long-term integrity of the market.

C. The Commission Should Require NYISO To Increase Assumed Levels Of Excess Capacity To NERA’s Recommended Levels

For the most part, the NYISO adopted the assumptions and recommendations of the NERA report developed as part of the Demand Curve reset process.¹² However, in a departure with potentially significant ramifications, the NYISO arbitrarily proposes reducing the assumed levels of excess capacity over the lifetime of the proxy unit for all three New York areas.¹³

¹¹ NYISO Proposal, Patton Affidavit at P 20.

¹² Proposed NYISO Installed Capacity Demand Curves for Capability Years 2011/2012, 2012/2013, and 2013/2014, September 3, 2010, amended September 7, 2010 and October 30, 2010 (“NYISO Report”), available at http://www.nyiso.com/public/webdocs/committees/bic_icapwg/meeting_materials/2010-11-09/NYISO_demand_curve_recommendations_10_30_2010_clean.pdf.

¹³ NYISO Proposal at 18. NERA recommended an excess capacity risk factor based upon as assumption that the market will be long, on average, an amount equivalent to 1.5 times the size of the Proxy Unit. This resulted in the following levels of excess: NYCA average excess of 1.5%; NYC average excess of 3.0%, and LI average excess of 6.0%. However, in the NYISO

There is no analysis or justification provided by the NYISO in support of this change. The NYISO's reduction of NERA's proposed average excess capacity levels is unrealistic (as some level of excess capacity will always exist) and will result in artificially suppressed capacity payments and hinder development of new and maintenance of existing resources needed for reliability. Of significant note, with regard to the proposed reductions for the NYC and LI areas, the NYISO's Market Monitor Dr. David Patton states in his affidavit:

In order for the levels for NYC and LI to be achieved without any shortages (i.e., the local requirement is satisfied continuously), a new peaking resource would have to enter precisely when capacity levels fall to the minimum requirement. After entry of the peaking resource, the excess capacity level would equal the size of one peaking resource. The level of excess would then gradually fall until it reaches zero and another resource enters. The only way that this pattern of entry could be considered realistic is if:

- Entry is perfectly coordinated; and,
- Forecasting is perfect.¹⁴

Dr. Patton continues, noting that, "Unfortunately, these conditions do not hold in the real world."¹⁵ He discusses other forecasting and investment planning challenges, and concludes that, "[h]ence, long-term demand forecast uncertainty should lead to higher excess capacity levels than the perfect forecast assumption implied by the NYISO's proposal for NYC and LI."¹⁶ EPSA asserts such

Proposal, those levels of excess were arbitrarily reduced down to an assumption that the market excess would average only one-half the size of the Proxy Unit, with the NYISO now supporting NYCA at 1% excess, or 101% of the Installed Reserve Market; NYC at 1.1% excess and LI at 2.1%.

¹⁴ NYISO Proposal, Patton Affidavit at P 23.

¹⁵ Patton Affidavit at P 24.

¹⁶ Patton Affidavit at P 27.

concerns regarding perfect forecasting should also apply in considering the NYISO proposed reductions to the NYCA area.

EPSA is extremely concerned regarding the arbitrary nature of the NYISO's proposed changes for all three New York areas, which are contrary to the NERA recommendations and insert unnecessary regulatory uncertainty into a well-functioning market. Furthermore, by artificially reducing capacity surplus levels, the need for RMR and other out-of-market agreements will increase, contrary to the Commission's clear policy goals and preference for market solutions. Accordingly, EPSA requests that the Commission require NYISO to reincorporate the excess capacity assumptions recommended by NERA and reset the NYCA, NYC and LI Demand Curves.

D. CONE Levels Must Be Set Correctly

The centerpiece of any capacity market is the CONE parameter. Consequently, CONE must be set at a level and updated on a periodic basis to ensure that this central parameter reflects prevailing market conditions and economic realities. EPSA has previously commented on the need for adequate CONE values to promote efficient pricing in capacity markets.¹⁷ CONE is the foundation for establishing a competitive price signal; therefore, it is essential for this value to be set at a level sufficient to incent necessary investment in new and

¹⁷ See Motion for Leave to Intervene and Protest of the Electric Power Supply Association, ISO New England Inc. and New England Power Pool, Docket No. ER10-787-000 (filed March 15, 2010); Comments of the Electric Power Supply Association, PJM Interconnection, LLC, Docket No. ER05-1410-010, et al. (filed January 9, 2009); and, Motion to Intervene and Comments in Support of the Electric Power Supply Association, PJM Interconnection, LLC, Docket No. ER08-516-000 (filed February 21, 2008). The filings may be accessed at: www.epsa.org.

existing infrastructure, assure the ICAP price over the long term reflects the entry costs of a peaking generator, and to maintain the viability of the ICAP construct.

In commencing the Demand Curve reset analysis process, the NYISO instructed NERA to calculate a Net CONE price with and without deliverability costs and property taxes incorporated, but did not require that NERA provide specific recommendations on whether those costs should be included.¹⁸

Ultimately, the NYISO made the unjustified determination that both deliverability costs and property taxes (for NYC) should be excluded from the calculation of Net CONE for the proxy unit. EPSA asserts the resulting Net CONE for the proxy units is unjust, unreasonable, and will result in rates that are too low to effectively provide appropriate price signals when investment in new and existing resources is needed.

i. System Deliverability Upgrade Costs Should Be Included Into The Calculation Of Net CONE For The NYCA Proxy Unit

The NYISO proposes to exclude all System Deliverability Upgrade (“SDU”) costs from the calculation of Net CONE for the NYCA Proxy Unit. This exclusion is proposed despite the fact that the NYISO Services Tariff requires a capacity provider to be fully deliverable throughout its capacity zone in order to be eligible to sell capacity. If the NYCA Demand Curve is set without incorporating these costs, the revenues that the Demand Curve will provide will

¹⁸ NYISO Proposal, NERA Report at 10, “Independent Study to Establish Parameters of the ICAP Demand Curve for the New York Independent System Operator.” (Final – Issued September 3, 2010, Revised September 7, 2010, November 15, 2010): (“In particular we have been requested by NYISO to provide updated Demand Curves with and without inter zonal deliverability and with and without NYC tax abatement.”)

not be sufficient to induce new entry of a peaking unit in the Upstate region, and thus, will not ensure that the NYISO can meet its reliability requirements. The NYISO appears to rely on the potential creation of a new capacity zone(s) at some future point in time as the rationale for the exclusion and the lack of need to properly establish the correct price signals in this proceeding.¹⁹ EPSA strongly submits the Commission must require the establishment of the Demand Curves and underlying Net CONE and other parameters based on the NYISO's tariff requirements for capacity providers and the circumstances that currently exist in the NYISO market.²⁰ Presently, circumstances dictate that the proxy unit would either have to pay to make its capacity deliverable or locate in an area that is fully deliverable throughout the capacity zone. Accordingly, EPSA requests that the Commission require the NYISO to include SDU costs in the Net CONE for the proxy unit in the NYCA and reset the NYCA Curve. In the alternative, the Commission should order that the proxy unit be located in the Lower Hudson Valley zone, which, although it has a higher Net CONE than the NYISO recommended proxy unit due to other factors, is fully deliverable in the NYCA capacity zone.

ii. Property Taxes Should Be Incorporated Into The Calculation Of Net CONE For The NYC Proxy Unit

Since the last Demand Curve reset process occurred in 2007, changes have occurred with respect to tax abatement offered to new generating facilities

¹⁹ NYISO Proposal at pp12-13.

²⁰ NYISO Open Access Transmission Tariff, Attachment S ("Attachment S") and Services Tariff, Section 5.14.1(b).

in NYC.²¹ Specifically, the current program adopted by the New York City Economic Development Corporation (EDC) establishes a discretionary tax abatement program,²² meaning there is significant risk that the entity in charge of granting such abatements may choose to deny a request for abatement either in its entirety or otherwise place limitations on such a request. After considering the NERA report and stakeholder input, the NYISO determined that “the most reasonable approach to setting the first post-ICIP NYC Demand Curve was to assume full tax abatement treatment for the NYC peaking unit.”²³

The NYISO has concluded that “it is in NYC’s economic interest to grant abatements to peaking units because so doing would result in lower capacity prices.”²⁴ However, as the NYISO Proposal acknowledges, it is unclear how this discretionary policy will actually be applied.²⁵ As it stands now, the current NYC Demand Curves are understated by almost 40% when property taxes are

²¹ For the last two Demand Curve resets, one of the most significant factual inputs to the calculation of the Net CONE for the NYC Demand Curves was the real property tax exemption awarded as a matter of right to new investment in utility property including new electric generating facilities, under New York City’s Industrial and Commercial Incentive Program (“ICIP Real Property Tax Exemption”). This factual input, a law which had been in place for over 24 years, was eliminated by the New York State Legislature effective June 30, 2008. N. Y. REAL PROP. TAX LAW Section 489-eeee(1) (McKinney 2008).

²² The replacement program enacted as of the same date expressly excludes utility property, including electric generating facilities, from receiving any real property tax exemptions as a matter of right under the new program.

²³ NYISO Proposal at 15.

²⁴ Id.

²⁵ Id. at 16. (“Nevertheless, the NYISO believes it is important that future Demand Curve reset reviews build upon the **actual** disposition of qualifying generators’ applications for the PlaNYC Energy Program Benefit. Thus, prior to the next Demand Curve reset cycle, the NYISO will review the outcome of applications that qualified for abatement under the PlaNYC Energy Program and will recommend that the percentage of tax abatement applied in establishing the next NYC Demand Curve reflect the actual awards made.”)(emphasis added)

excluded.²⁶ This makes the argument even more compelling that the Commission should not approve a Net CONE value for the NYC area that excludes property taxes under a discretionary program. The NYISO Proposal is unjustified, and if a blanket tax abatement is not provided to new generation, will result in the NYC Demand Curve being significantly understated, resulting in greatly decreased capacity payments. Accordingly, EPSA requests that the Commission direct the NYISO to incorporate property taxes into the calculation of the Net CONE for the Proxy Unit in NYC and reset the NYC Demand Curve.

²⁶ Subsequent to the repeal of the ICIP Real Property Tax Exemption, IPPNY and other parties jointly filed a complaint against the NYISO with the Commission requesting that the Commission direct the NYISO to reset the Demand Curves to reflect the property tax costs that would be levied on the NYC Proxy Unit. The Commission denied the complaint, stating that “it is reasonable to await the scheduled three year update to account for the elimination of the tax exemption and other changes which will apply to Demand Curves for the 2011-12 Capability Year.” See *Independent Power Producers of New York, Inc.*, 125 FERC ¶ 61311, at P 34 (2008).

Also, see NYISO Board of Directors Decision on Whether Repeal of the ICIP Requires Resetting the NYC ICAP Demand Curve at 5 (August 27, 2008) available at <http://www.nyiso.com/public/webdocs/documents/regulatory/market_participant_notices/ICIP_Repeal.pdf>.

IV. CONCLUSION

WHEREFORE, EPSA respectfully requests that the Commission grant its motion for leave to intervene in this proceeding and condition its acceptance of the NYISO Proposal on the changes requested herein.

Respectfully Submitted,



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December 21, 2010

CERTIFICATE OF SERVICE

I hereby certify that I have served a copy of the comments via email upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, D.C., December 21, 2010.



Nancy Bagot, VP of Reg. Policy