133 FERC ¶ 61,030
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
John R. Norris, and Cheryl A. LaFleur.

New York Independent System Operator, Inc. Docket No. ER10-2220-000

ORDER ON PROPOSED MITIGATION MEASURES

(Issued October 12, 2010)

1. On August 13, 2010, the New York Independent System Operator, Inc. (NYISO) submitted, pursuant to section 205 of the Federal Power Act (FPA),[1] revisions to the NYISO Market Administration and Control Area Services Tariff (Services Tariff). The revisions, which are contained in Attachment H (section 23)[2] of the Services Tariff, propose to apply a market power mitigation measure that will apply to all generators located in the rest-of-state capacity region (i.e., outside of New York City and Long Island) that are able to exercise market power when committed or dispatched to maintain system reliability (rest-of-state mitigation). The proposed measure is similar to the mitigation measure that was accepted by the Commission on May 20, 2010, in Docket No. ER09-1682-000, *et al*., which applies to three specifically identified generators.[3] In this order the Commission accepts the proposed revisions to be effective on October 12, 2010, as requested, subject to the conditions discussed below.

# I. Background

2. Attachment H of the Services Tariff sets forth market power mitigation measures to mitigate the market effects of conduct that would substantially distort competitive outcomes in the NYISO markets. Sections 23.3.1 and 23.3.2, respectively, identify the conduct and market impact thresholds used by NYISO to determine whether bids by market participants should be mitigated. In a September 4, 2009 filing in Docket ER09-1682-000, NYISO identified bidding behavior by three specific generators (Specified

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[1] 16 U.S.C. § 824d (2006).

[2] Under the Commission's e-Tariff, Attachment H is enumerated as section 23, *Market Mitigation Measures*, of the Services Tariff.

[3] *See New York Independent System Operator, Inc.*, 131 FERC ¶ 61,169 (2010) (May 20, 2010 Order), *reh'g pending*.

Generators) that, when the generators were committed for reliability as Day-Ahead Reliability Units (DARU), departed from the conduct that would be expected under competitive market conditions and also met the market impact threshold of former section 3.2.3 of NYISO's Market Mitigation Measures.[4] As a result of this bidding behavior, the increase in guarantee payments received by each of the Specified Generators for operating out of economic merit order triggered the impact threshold of section 3.2.3. NYISO proposed mitigation measures under that provision to apply only to the Specified Generators when called upon to meet a reliability need in the NYISO day-ahead market as a DARU or through Supplemental Resource Evaluation (SRE).

3. In the May 20, 2010 Order, the Commission found NYISO's proposed mitigation measures to be just and reasonable as they apply to the Specified Generators. The Commission found that NYISO had demonstrated that during August 2009 the Specified Generators were able to bid at prices substantially above their respective marginal costs reflected in their reference levels and that this conduct departed significantly from the conduct that would be expected under competitive conditions, thereby breaching the conduct standard under section 3.2.3. The Commission reasoned that "the ability to include and recover costs in excess of marginal cost, including fixed costs, in bids during periods when the generators are required to run for reliability is evidence of market power"[5] and that "mitigation may be required."[6] The Commission explained that "in a competitive market, a generator lacking market power would be expected to submit bids into the NYISO spot market at a level that, if accepted at that bid price, would be expected to cover the generator's marginal costs."[7] The Commission also found that the subject bidding conduct caused the impact threshold of section 3.2.3 to be exceeded.

4. With regard to the rest-of-state region, in the May 20, 2010 Order, the Commission expressed its concern "with the absence of a generally applicable mitigation measure to address the exercise of market power in those instances where a generator is the only solution to a reliability need."[8] The Commission further stated its belief that "it may be appropriate for NYISO to be authorized to immediately mitigate such conduct rather than having to not only investigate whether the conduct and impact thresholds of

[4] The NYISO's Market Mitigation Measures are set forth in Attachment H (currently, section 23) to its Market Services and Control Area Administration Tariff. To avoid confusion due to the numeration changes to NYISO's tariff resulting from its eTariff baseline tariff filing, we will continue to refer to section 3.2.3 of the prior tariff.

[5] May 20, 2010 Order, 131 FERC ¶ 61,169 at P 73.

[6] *Id*. P 78.

[7] *Id*. P 73.

[8] *Id*. P 101.

section 3.2.3 have been met on a case-by-case basis for specified individual generators but then delay mitigation by having to file a mitigation proposal under section 205."[9] The Commission encouraged NYISO's efforts to develop a generally applicable mitigation measure to address the exercise of market power in those instances where a generator is the only solution to a reliability need.

## II. NYISO August 13, 2010 Filing

5. NYISO states that its proposed mitigation measure in the instant filing would identify any rest-of-state generator that has become a pivotal supplier as a result of being required for reliability, and thus possesses market power and should be subject to mitigation. NYISO states that mitigation will only be applied if such a pivotal supplier engages in bidding conduct that is substantially inconsistent with competitive conduct, as measured by proposed thresholds that are consistent with those previously approved by the Commission. NYISO adds that any such bids will necessarily have a significant impact on guarantee payments.

6. NYISO states that this market power mitigation measure is similar to the mitigation measure that was accepted in the May 20, 2010 Order. NYISO adds that it applies to a generator committed as a DARU or via an SRE and subsequently dispatched out-of-merit above its minimum generation level to protect or maintain New York Control Area or local reliability. NYISO's proposed mitigation measure requires a determination that a supplier is in a position to exercise market power by requiring one of three conditions to be met. Section 23.3.1.2.3.2 provides:

> i. the Market Party (including its affiliates) that owns or offers the generator is the only market party that could effectively solve the reliability need for which the generator was committed or dispatched, or
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> ii. when evaluating an SRE that was issued to address a reliability need that multiple market parties' generators are capable of solving, NYISO only received bids from one market party (including its affiliates), or
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> iii. when evaluating a DARU, if the market party was notified of the need for the reliability commitment of its generator prior to the close of the day-ahead market.[10]

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[9] *Id.*

[10] NYISO Transmittal at 6 (citing NYISO Services Tariff, section 23.3.1.2.3.2).

7. NYISO states that, if the generator meets one or more of these three conditions, then the generators bid parameters are assessed relative to the applicable reference level to determine whether they meet specific conduct thresholds for the application of mitigation. If the specified conditions are met, proposed section 23.3.1.2.3 provides for mitigation to the generator's reference level. Section 23.3.1.2.3.3 provides:

> The Bids or Bid components submitted for the Generator that were accepted outside the economic evaluation process to protect or maintain New York Control Area or local system reliability:
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> i. exceeded the Generator's Minimum Generation Bid reference level by the greater of 10% or $10/MWh, or
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> ii. exceeded the Generator's Incremental Energy Bid reference level by the greater of 10% or $10/MWh, or
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> iii. exceeded the Generator's Start-Up Bid reference level by 10%, or
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> iv. exceeded the Generator's minimum run time, start-up time, and minimum down time reference levels by more than one hour in aggregate, or
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> v. exceeded the Generator's minimum generation MW reference level by more than 10%, or
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> vi. decreased the Generator's maximum number of stops per day below the Generator's reference level by more than one stop per day, or to one stop per day.[11]

8. NYISO explains that subsection (vi) above addresses the potential for the maximum number of stops per day, which are specified in a generator's bid parameters, to be manipulated to artificially increase its guarantee payment by extending the required commitment period if the generator is in a position to exercise market power. NYISO adds that this threshold would apply to start-up time and minimum down time, in addition to minimum run time, for the same reason.

9. NYISO states that imposing guarantee payment mitigation when the above conduct thresholds are exceeded recognizes that conduct at or exceeding the threshold will always have a material impact.

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[11] *Id.* (citing NYISO Services Tariff, section 23.3.1.2.3.3).

10. Existing section 23.3.3.3.1 provides a consultation process and timeline for real-time guarantee payments. In the instant filing, NYISO revises this section to include consultation stemming from its proposed mitigation measures.

11. NYISO states that in order to address transparency concerns raised by the Generation Owners sector in the stakeholder process, it agreed to require a transmission owner that requests a local reliability commitment to identify the suppliers that are capable of meeting the reliability need, or to inform NYISO that the requested supplier is the only one that can meet the reliability need. NYISO adds that also in response to a request from the Generation Owners sector, it developed a proposal for temporarily providing additional compensation to generators that are not able to recover their going-forward costs in the NYISO's markets, but while most stakeholders indicated willingness to participate in further discussions, no stakeholder supported the proposed measure.

12. NYISO also states that the Management Committee's approval of the mitigation proposal was appealed to the NYISO Board of Directors (NYISO Board). According to NYISO, Generation Owners claimed that existing cost recovery mechanisms do not provide an adequate opportunity for must-run units to recover their fixed costs. The NYISO Board issued a decision that denied the appeal, but did direct the NYISO management to work with stakeholders in the governance process to examine claims that existing cost recovery mechanisms are inadequate and to review the process by which permanent solutions to specific reliability needs are evaluated and planned for, particularly in terms of timing and cost to consumers.[12]

## III. Notice of Filing and Responsive Pleadings

13. Notice of NYISO's August 13, 2010 filing was published in the *Federal Register*, 75 Fed. Reg. 51,453 (2010) with comments, interventions, and protests due on or before September 3, 2010. Calpine Corporation; Dynegy Power Marketing, Inc., Dynegy Northeast Generation, Inc., and Sithe/Independence Power Partners, L.P (collectively, Dynegy); NRG Companies, PSEG Energy Resources & Trade LLC, and PSEG Power New York LLC (collectively, PSEG); and AES Eastern Energy, L.P. filed timely motions to intervene. Constellation Energy Commodities Group, Inc. and Constellation NewEnergy, Inc. (collectively, Constellation) filed a motion to intervene out-of-time.

14. The New York Transmission Owners (NYTO);[13] Mirant Parties, and the New York Association of Public Power filed timely motions to intervene and comments. The

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[12] NYISO August 13, 2010 Filing at 8 (citing *NYISO Board of Directors' Decision on Appeal of the Management Committee's May 28, 2010 Decision Adopting Mitigation Measures that will Apply to Rest-of-State Generators that are Committed for Reliability,* (July 29, 2010) (appended to the Filing)).

[13] The NYTOs consist of Central Hudson Gas & Electric Corporation,

New York State Public Service Commission (New York Commission) filed a notice of intervention and comments.

15. Electric Power Supply Association (EPSA), TransCanada Power Marketing, Ltd, and TC Ravenswood, LLC (collectively, Ravenswood), and Independent Power Producers of New York, Inc. (IPPNY) filed timely motions to intervene and protests. AER NY-Gen, LLC, Alliance Energy Marketing, LLC, AG-Energy, L.P., Seneca Power Partners, L.P., and Sterling Power Partners, L.P. (collectively, Alliance Utilities) filed a motion to intervene out-of-time and protest. The NYTOs filed an answer to the protest of EPSA. NYISO filed an answer to the protests of EPSA, Ravenswood, and IPPNY.

### A. Comments in Support

16. The New York Commission states that it is essential that the mitigation measures proposed by NYISO are in place to protect against generators that inappropriately exercise market power by bidding in a manner that departs from conduct that would be expected under competitive market conditions. The New York Commission believes that the proposed measures will act to bring market outcomes closer in line with competitive conduct, reduce the ability of generators to exercise market power, and help ensure that rates are just and reasonable. The New York Commission states that, as was the case with the three generators, it believes that the "tighter mitigation thresholds are reasonable for ensuring competitive bidding even when market conditions are not competitive."[14]

17. The NYTOs and the New York Association of Public Power state that they share the concerns expressed by the Commission in the May 20, 2010 Order and support an expeditious approval of the instant filing.

### B. Protests

18. IPPNY, supported by the Mirant Parties, argues that NYISO must be directed to develop a defined payment mechanism for generators that are required to run for reliability to recover their fixed costs if such costs cannot be recovered in the market and that the "gap solution" to cost recovery is inadequate to provide cost recovery for these units.[15] IPPNY also contends that the proposed rest-of-state mitigation measures are

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Consolidated Edison Company of New York, Inc., Long Island Power Authority, New York Power Authority, New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and Rochester Gas and Electric Corporation.

[14] New York Commission September 3, 2010 Comment at 4 (citing May 20, 2010 Order, 131 FERC ¶ 61,169 at P 93).

[15] IPPNY cites Dr. Shanker's affidavit, which states that under NYISO's

flawed in the following respects: (1) a supplier could be subject to mitigation without first being made aware of that fact, as NYISO's proposed reporting requirements will not be available to the generator until after the bid has been submitted, and are therefore useless in informing a generator's bidding behavior; (2) the NYISO proposal should be revised to specify that if generators are the sole unit available to meet a reliability need and submit bids within the greater of 10 percent or $10/MWh of the bid reference level, then these generators have complied with the NYISO tariffs and will not be subject to market power allegations under any provisions of NYISO's tariffs; (3) NYISO errs in asserting that a generator is in a position of market power when multiple market parties' generators are capable of solving the reliability need but only one market party submits bids; (4) NYISO should clarify that a market party must be the only unit that can respond to a reliability need in order for NYISO to apply the proposed ROS measures when a market party is notified of the need for a DARU out-of-merit request prior to the close of the day-ahead market; and (5) while proposed section 23.3.3.3.1.3.3 specifies several generator parameters that are subject to mitigation, it fails to memorialize that these parameters are only subject to mitigation when the generator has changed its operating parameters, which was clarified by a NYISO representative during the stakeholder process on this issue.

19. EPSA argues that the proposed ROS mitigation is not just and reasonable because it fails to combine reduced mitigation thresholds with a new mechanism that would provide generators committed for reliability the opportunity to earn adequate revenues to recover their fixed costs. EPSA asserts that the instant filing does not resolve an underlying failure of NYISO's software to appropriately model the reliability constraints. EPSA argues that mitigated generators must have an opportunity to recover fixed costs[16] and that implementation of the instant proposal should not be allowed until a companion mechanism for fixed cost recovery is developed. EPSA states that without such a complementary mechanism, generators needed for reliability may not be able to recoup sufficient revenues to support their continued operation. EPSA also states that reliance on NYISO's Attachment Y "Gap Solution" process poses a number of timing and other

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Locational Based Marginal Pricing (LBMP) market design, infra-marginal generators are able to recover their marginal operating costs and a contribution toward their fixed costs; however, a unit that is committed out of merit is not able to be infra-marginal and has lost an important avenue for recovery of its fixed costs. Further, Dr. Shanker states that units subject to NYISO's proposed ROS Measures may not be able to earn sufficient energy or capacity revenues due to the lack of a locational definition in the capacity markets beyond the New York City and Long Island locational zones. Shanker Aff. at P 17-19.

[16] EPSA September 3, 2010 Protest at 9-13 (citing *Bluefield Waterworks & Imp. Co. v. Pub. Serv. Comm'n of West Virginia*, 262 U.S. 679, 692 (1923); *FPC v. Hope Natural Gas Co.,* 320 U.S. 591, 603 (1944); *Midwest Independent Transmission System Operator, Inc.*, 102 FERC ¶ 61,196, at P 49 (2003)).

concerns, but the primary concern is that a generator would have to file a retirement notice with the New York Commission prior to becoming eligible for a form of reliability payment. According to EPSA, this is an extreme action that may trigger a number of financial and other material adverse consequences. EPSA references previous Commission decisions in the Midwest Independent Transmission System Operator, Inc. that encouraged recovery of fixed and variable costs,[17] and in PJM Interconnection, L.L.C. (PJM) that established a frequently mitigated unit adder to cost-based bids for units frequently called for reliability purposes.[18] EPSA requests the Commission direct NYISO to develop tariff provisions, similar to those the Commission has previously approved for PJM and ISO New England, Inc., which provide for a generator to make a section 205 filing requesting the establishment of a reliability-must-run agreement.

20. According to Ravenswood, every NYISO State of the Market report has indicated that market returns to suppliers have been insufficient to cover their costs since the inception of the markets. Ravenswood states that if a market participant knows that it has market power and competitive markets no longer exist, Commission policy and precedent has established that a supplier has the right to receive its costs, including a reasonable return on and of its prudent investment, especially when required for reliability. Without competitive markets, Ravenswood contends that a price mitigated to a very narrow threshold is not just and reasonable. According to Ravenswood, pursuit of cost recovery opportunities, including a return of and on investment, is not an abuse of market power in competitive or regulated markets where a resource is required for reliability. Ravenswood asserts that even in a competitive market, an entity with market power should not be required to lose money or be subject to rules that cause it to lose money just because it possesses market power. Ravenswood states that if energy offers are going to be limited to cost, then, during frequent scarcity conditions when there is only one resource left to provide reliability, there needs to be a scarcity adder over and above cost and the supplier should receive that premium and the market should see that scarcity price.

21. Ravenswood asserts that the Commission should require NYISO to include an appropriate mitigation measure to protect against uneconomic entry. Ravenswood believes that NYISO's proposed mitigation measures are one sided and that the potential for buy-side market power and uneconomic entry is likely to occur due to the relative size of load interests compared to suppliers. Ravenswood asserts that the proposed mitigation will be relied on more frequently as uneconomic wind investments cause more frequent reliability calls on existing dispatchable resources.

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[17] *Id*. at 11 (citing *Midwest Independent Transmission System Operator, Inc.,* 102 FERC ¶ 61,196 at P 49).

[18] *Id*. (citing *PJM Interconnection, L.L.C.,* 107 FERC ¶ 61,112, at P 39 (2004); PJM Operating Agreement, section 6.4.2 (a)(ii)).

22. Ravenswood argues that the Commission should require NYISO to design and implement balanced mitigation measures and market rules that address both potential supply-side and buy-side market power (i.e. uneconomic entry) in order to provide a level of compensation that will attract and retain needed infrastructure and thus promote long-term reliability while neither over-compensating nor under-compensating suppliers.

23. Ravenswood further asserts that the price suppressive impacts of uneconomic activity need to be incorporated into the capacity mitigation measures or the Commission needs to ensure that the Demand Curve reset process[19] takes into account uneconomic energy entry such that market prices are not subject to market power for three years until the next Demand Curve capacity price reset is made. Also, appropriate risk factors may also be required when evaluating the Demand Curve reset and the potential exercise of load-side market power.

24. Ravenswood states that if a reliability unit remains uneconomic because the market is not providing an adequate price signal, then a viable reliability-must-run agreement process is required that does not require retirement as a trigger.[20]

25. To provide for a balanced market design, Ravenswood suggests mitigation of supply-side market power using flexible thresholds that increase with the frequency of reliability mitigation events. Ravenswood states that to the extent a unit is frequently mitigated as a reliability unit, its offer threshold should be increased and the unit meeting the reliability need should at a minimum be paid its long run average cost, as would occur in a reliability-must-run agreement.

26. Ravenswood maintains that payments made to the suppliers that are required to operate to maintain reliability will still be subject to a just and reasonable standard and not permitted to rise to usurious levels. Ravenswood asserts that, assuming for argument's sake that market power exists, the exercise of market power should be judged by determining whether the returns are usury, not simply by blindly applying energy mitigation without regard to other market issues and the real costs that affect actual returns.

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[19] According to section 5.14.1.2 (Demand Curve and Adjustments) of the NYISO Services Tariff, NYISO conducts a triennial review of its Installed Capacity Demand Curve for the next three capability years. NYISO files the proposed ICAP Demand Curves with the Commission, as approved by the NYISO Board of Directors, no later than November 30 of the year prior to the year in which the ICAP Demand Curves would apply. *See New York Independent System Operator*, 113 FERC ¶ 61,271 (2005).

[20] Ravenswood September 3, 2010 Protest at 11; *see also* IPPNY September 3, 2010 Comment at 11-12 (citing Shanker Affidavit at P 12, 37).

### C. Answers

27. In their answer to EPSA's protest, the NYTOs state that the protestors are repeating the same cost recovery arguments that the Commission addressed in the May 20, 2010 Order and found to be unrelated and outside the scope of the mitigation proceeding. The NYTOs assert that the instant filing is focused solely on mitigating market power and the establishment of a fixed cost recovery mechanism is not a relevant issue in this proceeding.

28. NYISO, in its answer, asserts that, contrary to protestors' claims, the proposed mitigation rule is not expected to significantly impact compensation to reliability-committed generators located outside of New York City. NYISO states that the protests include no evidence to support the contention that applying tighter mitigation thresholds to reliability-committed rest-of-state generators will prevent this class of generators from recovering their fixed costs in the markets that NYISO administers. In total, NYISO explains that there are 264 generators and more than 26,600 MW of capacity located outside the New York City Constrained Area. According to NYISO, the protests are attacking a proposed mitigation rule that might significantly impact the revenues received by five to seven rest-of-state generators if those generators are offered in a manner that is not consistent with their marginal operating costs.

29. NYISO states that since its inception in 1999, it has evaluated the potential reliability impacts of numerous generator retirements. In each case, NYISO determined that the generator could retire without harm to the reliability of electric service in New York. While it is true that the NYTOs and/or the NYISO commit generators "for reliability" as DARUs or via SRE, NYISO explains that the committed generators vary from day-to-day and are determined based on system conditions including transmission facility outages (planned or unplanned), and the need to support a transmission owner's local distribution system. NYISO states that it is not accurate, or even reasonable, to simply assume that a NYTO would need to execute a reliability-must-run agreement with any of the generators that were committed for reliability over the past year if it proposed to retire.

30. NYISO disagrees that the generators committed for reliability are providing a "unique service" that is entitled to additional, or distinct, compensation. NYISO states that unforced capacity suppliers in New York are expressly required by the NYISO tariffs to offer their generator into the day-ahead market so it is available for DARU commitment, and are required to submit bids in response to an SRE request.[21] Hence, responding to reliability related commitments is already a clear and express component of

[21] NYISO September 23, 2010 Answer at 9-10 (citing sections 5.12.1.6 and 5.12.1.10 of the Services Tariff).

an unforced capacity supplier's obligation in New York; it is part-and-parcel of the unforced capacity product that a supplier sells.

31. NYISO states that the protestors' comments regarding compensation for frequently mitigated units fails to take differences between the NYISO and PJM markets into consideration. NYISO states that Dr. Shanker's proposal to increase the mitigation thresholds are inadequately justified and lack the specific detail needed to be implemented. NYISO states that the compensation rule proposed by IPPNY and Ravenswood fails to require a showing that a generator is not already fully recovering its going-forward costs. According to NYISO, protestors' proposed compensation also provides incentives for economic withholding. NYISO states that the proposed measures will consequently harm the New York markets by forcing New York to pay higher prices for rest-of-state reliability constraints and by decreasing the number of generators offering economically.

32. NYISO asserts that Ravenswood improperly reached the conclusion that the State of the Market Reports have historically indicated that market returns are insufficient to recover costs. NYISO references multiple quotes from previous State of the Market Reports regarding sufficient investment incentives for resources. NYISO attributes insufficient revenues in 2008 and 2009 to the recession and states that the fact that NYISO's markets accurately reflected 2009 economic conditions in New York does not indicate a deficiency that needs to be remedied, nor does it show that New York generators are being denied an adequate opportunity to recover their going forward fixed costs in the markets that NYISO administers.

33. NYISO states that while it may be possible in some instances to model and price reliability constraints that require the commitment of rest-of-state generators, the appropriateness of NYISO's proposed mitigation measure does not turn on whether a particular constraint is, or is not modeled. NYISO contends that a generator that must be committed to address a reliability constraint will possess market power in either case. NYISO states that even if it were to model rest-of-state reliability constraints in the manner EPSA suggests, the vast majority of reliability commitments would not set price because they are committed at their minimum generation level and do not set price in LBMP markets for their minimum generation megawatts. NYISO states that modeling the constraint will shift the impact of exercising market power from guarantee payments to LBMPs and will expand the potential market impact of that supplier's ability to exercise market power.

34. In NYISO's answer, Dr. Patton addresses Dr. Shanker's characterization of constraints that result in DARU and SRE commitments, that Dr. Shanker frames as "invisible" constraints that do not allow for infra-marginal rents.[22] Although generators

[22] *Id.*, Attachment A at 8.

that are committed for reliability do not earn infra-marginal rents in some cases, Dr. Patton explains that they are not unique in this regard from other locational pricing markets that are all uniform price auctions. According to Dr. Patton, an important feature of the uniform price auction market design is that suppliers have an incentive to offer at marginal cost. This allows the market to commit and dispatch resources efficiently. One implication of this design, states Dr. Patton, is that the marginal generator usually receives little or no infra-marginal rents to contribute toward the recovery of its fixed costs. According to Dr. Patton, when constraints involve small areas where there are relatively few generators, each generator is more likely to be marginal, but such units are not prevented from earning additional energy and ancillary services revenues when prices rise above the marginal costs of the generator, particularly during shortage pricing events. Therefore, asserts Dr. Patton, whether a reliability constraint is "invisible" and not reflected in prices, or modeled and included in prices does not materially change the market power the supplier possesses or the appropriateness of the proposed mitigation.

35. In response to Ravenswood's arguments regarding uneconomic entry by wind generation, NYISO believes that given federal and state policy, its role is to do its best to reliably incorporate wind resources into its markets. While it might be reasonable to assume that the recent influx of wind generators has had some effect on rest-of-state capacity and energy prices, NYISO asserts that Ravenswood has not shown that its broad policy concerns regarding government subsidies to wind generators are closely tied to the market power concern that is the sole focus of the proposed mitigation measure.

36. NYISO states that the provisions of Attachment Y contemplate that developers of a non-transmission regulated reliability project, including a Gap Solution, may receive "full recovery of all reasonably incurred costs" as determined under state law.[23] NYISO believes that providing a pre-determination of reliability need will only serve to encourage generators that are needed for reliability to announce their "retirement" if the supplier believes that the generator will earn more under cost-based rates than it can earn in the NYISO's markets under current market conditions. NYISO states that the Commission's orders addressing reliability commitments in ISO-New England recognize the danger that permitting generators to "toggle" between market- and cost-based compensation methods presents.[24] NYISO is willing to consider and discuss stakeholder-proposed solutions that would prevent toggling between cost- and market-based rates.

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[23] *Id.* at 19-20 (citing sections 31.2.5.9 and 31.4.4 of Attachment Y of NYISO's OATT).

[24] *Id.* at 14 (citing *ISO New England Inc. and New England Power Pool,* 125 FERC ¶ 61,102, at P 45-46 (2008) ("We agree with ISO-NE that it is not reasonable to allow a resource that will remain in the capacity market in future years to toggle between cost-based and market-based compensation since a resource that could receive market prices when they exceed its costs and cost-based prices in the other years would

37. In response to IPPNY's request that generators be informed when they are needed for reliability in advance of submitting their bids so that the generator can be sure to bid below the applicable threshold(s), NYISO states that the Commission rejected these arguments in the May 20, 2010 Order and stated that generators should bid competitively at all times.[25] NYISO further explains that rest-of-state generators that let their day-ahead bids expire will receive a request to submit bids in response to an SRE request from the transmission owner and will know their bids may be used to commit the generator for reliability. NYISO states that because a DARU designation means that a generator is guaranteed to be committed, if the NYISO or a transmission owner tells the generator in advance that it is the subject of a DARU request, then the generator will be subject to the mitigation; if the generator is not informed in advance and the generator is competitively committed, the proposed mitigation measure will not apply.

38. NYISO disagrees with IPPNY's assertion that mitigation measures applying to a generator's operating parameters should only be subject to mitigation if the generator changes these parameters. NYISO states that a generator including an unreasonable parameter in its bid that causes NYISO to unnecessarily extend the generator's reliability commitment for several additional hours should not be able to rely on the fact that a physical parameter, such as minimum run time, has been included in its bid for some time.

39. Dr. Patton disagrees with IPPNY's assertion that NYISO's provisions are unnecessary when the generator is one of several generators capable of satisfying the reliability need.[26] Dr. Patton explains that even if the owner of a generator does not know the reason for a DARU or SRE instruction, a generation owner that frequently receives DARU and SRE instructions can determine that it likely has local market power. According to Dr. Patton, the generation owner will make a profit-maximizing decision under uncertainty that balances (a) the probability of higher revenues from raising its offers above the competitive levels against (b) potential losses from foregone sales if it is economic and does not have local market power. In most circumstances, Dr. Patton believes that such an owner would not offer competitively unless it estimated a very low probability of having local market power.

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be virtually guaranteed to earn revenues above costs over time. Providing a resource with a cost-based backstop would also blunt incentives for the resource to minimize its costs."); *Bridgeport Energy, LLC,* 118 FERC ¶ 61,243, at P 66 (2007); *Bridgeport Energy, LLC,* 113 FERC ¶ 61,311 (2005)).

[25] *Id.* at 26 (citing May 20, 2010 Order, 131 FERC ¶ 61,169 at P 78-79).

[26] *Id.*, Attachment A at 12.

## IV. Commission Determination

### A. Procedural Matters

40. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2010), the notice of intervention and the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

41. Pursuant to Rule 214(d) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214(d) (2010), the Commission will grant Constellation's and Alliance Utilities' late-filed motions to intervene given their interest in the proceeding, the early stage of the proceeding, and the absence of undue prejudice or delay.

42. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2010) prohibits an answer to a protest or to an answer unless otherwise ordered by the decisional authority. We will accept the answers filed in this proceeding because they have provided information that assisted us in our decision-making process.

### B. Substantive Matters

43. The proposed rest-of-state mitigation measures of NYISO's August 13, 2010 Filing, with a few adjustments, are essentially the same and accomplish the same purpose as applied to all rest-of-state generators as those accepted for the Specified Generators in the May 20, 2010 Order. For the same reasons that we accepted those measures, as discussed below, we accept these mitigation measures to be effective on October 12, 2010, subject to the conditions discussed below. As the rest-of-state mitigation measures apply to all rest-of-state generators, we direct NYISO to submit a compliance filing within 15 days of the date of this order to remove section 23.8 (Generator-Specific Mitigation Measure) from Attachment H of the Services Tariff.

44. In the May 20, 2010 Order, the Commission determined that the proposed mitigation of the three Specified Generators in that proceeding was justified under the specifically defined circumstances where the three generators had market power when used for reliability and engaged in bidding conduct in such circumstances that breached the conduct and impact thresholds of section 3.2.3 of the tariff. The Commission noted its concern over the absence of a generally-applicable mitigation measure to address the exercise of market power in those instances where a specific generator is the only solution to a reliability need.[27] As was the case for the three Specified Generators mitigated by the May 20, 2010 Order, NYISO has shown here that generators meeting the conditions specified in its proposed mitigation measures have market power as a consequence of too few or no competitive alternatives.[28] Thus, the mitigation principles

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[27] May 20, 2010 Order, 131 FERC ¶ 61,169 at P 101.

articulated by the Commission in the May 20, 2010 Order apply to rest-of-state generators in a similar position as the Specified Generators. The Commission also stated that it may be appropriate for NYISO to eliminate the inherent delay in mitigating individual generators under the existing provisions of section 3.2.3 of the tariff that require an investigation and section 205 filing in each instance where NYISO finds a market participant meets the conduct and impact thresholds of that section. The August 13, 2010 filing also addresses this timing concern. In addition, NYISO proposes to apply the consultation guidelines of Attachment H to this generally-applicable mitigation measure, which it is already applying to the three Specified Generators under section 23.8 of the Services Tariff.[29] As such, we find their use here to be appropriate as well.

45. We disagree with IPPNY that NYISO should inform a supplier whether it could be subject to mitigation before the supplier submits its bid in order to inform a generator's bidding behavior. As the Commission clarified in the May 20, 2010 Order, competitive behavior only requires that a generator be able to determine its marginal cost, which is defined as its reference price level, so that it can bid at that level.[30] The Commission found that, as a general matter, a generator can be expected to bid at its marginal cost level in a competitive market. Mitigation is meant to ensure competitive offers even when competitive conditions are not present.[31] We find that even though a supplier might not know which particular days or hours they will be committed to meet reliability needs, they will know that bidding above marginal cost is potentially subject to mitigation.

46. We disagree with IPPNY that if generators are the sole unit available to meet a reliability need and submit bids within the greater of the 10 percent or $10/MWh range of the bid reference level under proposed section 23.3.1.2.3.3, then these generators have complied with the NYISO's tariffs and will not be subject to market power allegations under any provisions of NYISO's tariffs. We agree that if a generator bids within these thresholds, then it should be able to avoid market power allegations related to economic withholding; however, the same generator may not necessarily be within the thresholds regarding physical withholding. In this regard, we find that generators submitting bids or bid components within NYISO's proposed thresholds should still be held accountable for the section 23.3.1.1 physical withholding thresholds and any other applicable mitigation

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[28] *Id.* P 78.

[29] The Commission accepted the use of the Attachment H consultation guidelines by delegated letter in Docket No. ER10-2158-000 on September 20, 2010.

[30] May 20, 2010 Order, 131 FERC ¶ 61,169 at P 78.

[31] *Id.* P 69.

measures that are also necessary to evaluate whether generators have departed from competitive conduct.

47. We also disagree with IPPNY that a unit receiving a DARU out-of-merit request must be the only unit that can respond to a reliability need in order for NYISO to apply the proposed mitigation measures. By definition, a DARU is needed to meet the reliability needs of a transmission owner's local system or the reliability requirements of the New York Control Area.[32] As was the case with the Specified Generators, a DARU could be expected to be committed for reliability needs and thus bid at levels above its marginal cost with that expectation in mind. The DARU is committed outside of economic merit for reliability and thus is put in a position where few or no competitive alternatives exist. As NYISO explains in its answer, a generator that is the subject of a DARU request is guaranteed to be committed in the day-ahead market and, for this reason, has market power.

48. Additionally, we disagree that a supplier is not in a position of market power when multiple generators are capable of solving a reliability need, but NYISO only receives bids from one market party. As NYISO provides in its answer, a generator bidding in response to an SRE request knows they are needed for reliability and thus may be in a position to exercise market power. Regardless of whether there is only one generator or multiple generators available to address a reliability need, when NYISO receives bids from a single market party in response to a reliability need, NYISO does not have an ability to evaluate competing offers. Accordingly, mitigation should apply anytime a non-competitive offer must be taken.

49. We reject IPPNY's contention that section 23.3.3.3.1.3.3 should memorialize that generator operating parameters are only subject to mitigation when the generator has changed its operating parameters. Consistent with the May 20, 2010 Order and the section 3.2.3 conduct threshold, we do not agree that generators need to actually change their bid components in response to being committed for reliability in order for the bids to be mitigated; only that the bid components should exceed a reference level.[33] As determined in the May 20 Order, "[w]hether a submitted bid is a change from a prior bid is irrelevant, because the analysis should properly focus on the bid compared to the reference level, and not on what a generator bids one day compared to another day."[34]

50. As discussed in the May 20 Order, market power mitigation is a market design mechanism to ensure competitive offers even when competitive conditions are not present.[35] Competitive offers are expected to cover only the generator's marginal costs.[36]

[32] *See* section 2.4 of the NYISO Services Tariff.

[33] May 20 Order, 131 FERC ¶ 61,169 at P 74.

[34] *Id.*

As discussed below and in the May 20, 2010 order, the issue of fixed cost recovery is outside of the scope of this proceeding, which is focused on market power mitigation.

51. As stated in the May 20, 2010 Order, generators needed mainly for reliability have other opportunities to receive compensation above their marginal costs.[37] During periods of market-wide scarcity, given the nature of NYISO's markets, the market clearing price will typically exceed the marginal costs of virtually all generators, thereby allowing all such generators to receive revenues that contribute to fixed cost recovery.[38] In addition, generators can receive revenues to contribute to the recovery of their fixed, i.e., capacity, costs from the capacity market. While generators that are needed for reliability may have fixed cost recovery issues that need to be addressed, these generators must remain subject to NYISO's market power mitigation measures, the application of which is the only issue in this proceeding.[39]

52. Ravenswood asserts that the exercise of market power should be judged by determining whether the returns are usury, not simply by mitigation without regard to other market issues and the real costs that affect actual returns. According to Ravenswood, pursuit of cost recovery opportunities, including a return of and on investment, is not an abuse of market power in competitive or regulated markets where a resource is required for reliability. We disagree. As we found in our May 20, 2010 Order, market power exists during periods when generators are needed for reliability, are committed out of the market, and are able to recover bids that exceed their marginal costs.[40] When such generator is required out-of-merit for reliability, there is no dispute that it possesses market power, and thus that mitigation may be required.[41] The desire for full cost recovery does not justify the exercise of market power.[42]

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[35] *Id.* P 69.

[36] *Id.* P 73.

[37] *Id.* P 81.

[38] *Id.* P 81 (citing *New York Independent System Operator, Inc.,* 106 FERC ¶ 61,111, at P 1, 41-45 (2004)). *See, e.g*., scarcity pricing provisions in the Services Tariff, Rate Schedules 3, 4, and 5 and Attachment B.

[39] *Id.*

[40] *Id.* P 72.

[41] *Id.* P 78.

[42] *Id.* P 81.

53. Commenters raise a number of fixed cost recovery concerns that we find do not impact our decision to accept the rest-of-state mitigation proposal that we address here. These issues were also raised in the proceeding leading to the May 20, 2010 Order. Referring to the May 20, 2010 Order, where the Commission stated that fixed cost recovery issues were not within the scope of that proceeding and may be addressed in other appropriate proceedings,[43] parties state that the instant proceeding is the appropriate forum.

54. We disagree. This proceeding, similar to the proceeding addressed by our May 20, 2010 Order, is only concerned with NYISO's proposed mitigation measures that will apply to generators that are able to exercise market power when committed for reliability. Because fixed cost recovery issues do not go to whether NYISO's mitigation proposal is in itself just and reasonable, this proceeding is not the appropriate forum in which to raise such issues. Further, commenters do not present factual evidence that demonstrates that market participants generally will be unable to recover their costs due to application of the proposed mitigation provisions. We note, however, that the NYISO Board of Directors, in its July 29, 2010 decision on the appeal of the NYISO Management Committee's adoption of the instant mitigation proposal, directed NYISO management to work with stakeholders to examine the generation owners' claims that existing cost recovery mechanisms are inadequate and to review the process that evaluates permanent solutions to reliability problems. Accordingly, we believe the better course is to await the outcome of the stakeholder process as directed by the NYISO Board of Directors. In this regard, we direct NYISO to file status reports every 180 days beginning 180 days from the date of this order for informational purposes only.[44]

<u>The Commission orders</u>:

(A) The Market Mitigation Measure for rest-of-state generators required for reliability is hereby accepted to be effective on October 12, 2010, subject to the conditions of this order.

(B) NYISO is hereby directed to submit a compliance filing within 15 days of the date of this order to remove section 23.8 (Generator-Specific Mitigation Measure) from Attachment H of the Services Tariff, as discussed in the body of this order.

(C) NYISO is hereby directed to submit status reports on its stakeholder progress within 180 days from the date of this order and every 180 days thereafter until the stakeholder process on fixed cost recovery is complete, as discussed in the body of

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[43] *Id.* P 82.

[44] The Commission does not intend to issue public notices, accept comments, or issue orders on such informational filings.

this order.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,
Deputy Secretary.