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December 21, 2010

Honorable Kimberly D. Bose, Secretary
Federal Energy Regulatory Commission
888 First Street, NE
Washington, DC 20426

Re: New York Independent System Operator, Inc., Docket No. ER10-xxx-000, Proposed Tariff Revisions to Enhance Shortage Pricing

Dear Secretary Bose:

In accordance with Section 205 of the Federal Power Act and Part 35 of the Commission's regulations, the New York Independent System Operator, Inc. ("NYISO") respectfully submits proposed revisions to its Market Administration and Control Area Services Tariff ("Services Tariff").[1] With this filing, the NYISO is proposing to improve shortage pricing for its Regulation Service and Operating Reserves products by modifying the existing demand curves applicable to those products to better reflect the value of energy during shortage conditions and to improve the consistency between tariff provisions and operational practices. If approved, these revisions will enhance market efficiency. The NYISO also expects that these proposals will improve reliability, and will provide a greater energy market price incentive for generator performance, generator location, demand response, and transmission expansion.

These tariff changes are the result of an ongoing review by the NYISO of the existing Ancillary Services shortage-pricing mechanisms. The changes proposed here represent the outcome of the first phase of this review; the NYISO and its stakeholders are continuing to consider and discuss further possible enhancements. The amendments proposed in this filing received unanimous approval of the NYISO's Management Committee, with abstentions, and approval of the NYISO's independent Board of Directors.

[1] Capitalized terms used in this filing and not defined here shall have the meaning given to them in the NYISO Services Tariff.

I. Documents Submitted

1. This filing letter;

2. A clean version of the proposed revisions to the NYISO's Services Tariff ("Attachment I"); and

3. A blacklined version of the proposed revisions to the NYISO's Services Tariff ("Attachment II").

II. Background and Issue

Enhanced Shortage Pricing

Effective shortage pricing rules improve reliability, promote the entry of new demand response and generation resources, and promote innovation. In its October 2008 Final Rule on Wholesale Competition in Regions with Organized Electric Markets ("Order 719"), the Commission directed ISOs and RTOs to modify their market rules governing price formation during periods of operating reserve shortage to ensure that the market price for energy accurately reflects the value of such energy during shortage periods.[2] Order 719 suggested four methods for compliance, including the option of establishing:

> [A] demand curve for operating reserves, which establishes a predetermined schedule of prices according to the level of operating reserves. As operating reserves become shorter, the price increases.[3]

The NYISO has used such demand curves since 2005 to ensure that the market price for energy reflects the value of energy during an Operating Reserve shortage. Thus, in its Order 719 Compliance Filing, the NYISO explained that its tariff design already met the requirements of Order 719.[4] The Commission accepted the NYISO's response, but noted that it expected the "NYISO to continue to work with its stakeholders to improve scarcity pricing rules where possible."[5]

[2] Order No. 719, 73 Fed. Reg. 64, 100 (Oct. 28, 2008), FERC Stats. &. Regs. ¶ 31,281 (2008), 125 FERC ¶ 61,071 (2008).

[3] Order No. 719 at ¶221.

[4] New York Independent System Operator, Inc., *Compliance with Order No. 719*, Docket No. ER09-1142-000, 11-13 (May 15, 2009).

[5] New York Independent System Operator, Inc., Order on Compliance Filing, Docket No. ER09-1142-000, 129 FERC ¶ 61,164, ¶ 51 (Nov. 20, 2009).

Since their implementation, the levels of the NYISO Ancillary Services demand curves have remained unchanged. However, in its ongoing effort to refine and improve price signals during shortage conditions, the NYISO recently reviewed its existing shortage-pricing mechanisms and explored possible enhancements to its current approach. As a result of the first phase of this review, the NYISO now proposes to modify the pricing points for its Regulation Service Demand Curve and for two of the Operating Reserve Demand Curves, the Total 10-Minute Reserves demand curve for the NYCA and the 30-Minute Reserves demand curve for Long Island. [6]

Regulation Service:

The current Regulation Service Demand Curve is composed of two segments. Each segment has a distinct pricing point, $250 for up to 25 MWs of shortage and $300 for 25 MWs or more of shortage. This approach does not adequately conform to actual operating practices. In practice, system operators treat shortages of a few MWs as a trade-off of Regulation Service for energy MWs since these shortages are typically of short duration. Unless the system is short at least the number of MWs that could be provided by a gas turbine unit ("GT"), the system operator will not commit such resources to provide energy to meet a shortage in real-time. Therefore, the NYISO proposes changing the Regulation Service Demand Curve from two to three segments to better reflect these operations. The first segment will be for a shortage up to 25MWs with the price of $80; this pricing point represents a small shortage traded off for energy and is priced consistent with the historic value of energy. The second segment will be for a shortage of at least 25MWs but fewer than 80MWs with the price of $180. The third segment will be for a shortage of 80MWs or greater with the price of $400. 80MWs represents the point at which operators would consider activating GTs, and the $400 price point reflects the average cost of starting and operating a GT for an hour. The $180 price point for the middle MW value is an interpolation of the other two dollar-values.

Total 10-Minute Reserves:

The current value of the demand curve for NYCA total 10-minute reserves is $150. This value is less than the cost of starting a GT. Operational practices indicate that when this category of Operating Reserves is short, the ISO should start a 30-minute GT to back down an on-line flexible resource and create the 10-minute reserve product. In order to achieve this desired outcome, the NYCA 10-minute reserves demand curve should be increased to $450 to reflect the cost of starting a GT (similar to the Regulation Service Demand Curve proposal). This value differs from the proposed Regulation Service value to indicate an operational preference for 10-minute Operating Reserves and to ensure the market solution does not have any undesirable trade-offs of 10-minute reserves for Regulation Service.

[6] The NYISO Services Tariff Rate Schedule 4 defines an Operating Reserve Demand Curve for each Operating Reserves requirement. This includes demand curves for "Total 10-Minute Reserves" and "Long Island 30-Minute Reserves."

30-Minute Reserves:

The 30-Minute Reserves demand curve for Long Island, currently set at $300, serves little purpose as currently constructed. The $300 value is similar to the cost of starting a quick start resource. However, no resources need to be committed to meet this requirement, since it is satisfied by both spinning and non-spinning resources on Long Island. Therefore, the NYISO proposes to reduce this value to $25 to reflect a more accurate market value for this product.

In the course of its deliberations with stakeholders, the NYISO tested the new proposed values for these Operating Reserves and Regulation Services products against actual data from 2009 real-time cases. The NYISO's analysis showed that use of the proposed demand curve pricing rules would result in more efficient commitments of GTs, an annual reduction in uplift by approximately $100,000, and a decrease in overall production costs of up to $2 million annually.

III. Tariff Modifications

The proposed changes to the NYISO Services Tariff are located in Rate Schedules 3 and 4. The NYISO proposes to modify section 15.3.7 of Rate Schedule 3 to provide that:

> The ISO shall establish and post a target level of Regulation Service for each hour, which will be the number of MW of Regulation Service that the ISO would seek to maintain in that hour. The ISO will then define a Regulation Service demand curve for that hour as follows:
>
> For quantities of Regulation Service that are less than or equal to the target level of Regulation Service minus 80 MW, the price on the Regulation Service demand curve shall be $400/MW.
>
> For quantities of Regulation Service that are less than or equal to the target level of Regulation Service minus 25 MW but that exceed the target level of Regulation Service minus 80 MW, the price on the Regulation Service demand curve shall be $180/MW.
>
> For quantities of Regulation Service that are less than or equal to the target level of Regulation Service but that exceed the target level of Regulation Service minus 25 MW, the price on the Regulation Service demand curve shall be $80/MW.
>
> For all other quantities, the price on the Regulation Service demand curve shall be $0/MW. However, the ISO shall not schedule more Regulation Service than the target level for the requirement for that hour.

At Rate Schedule 4, subsection d of section 15.4.7, the NYISO proposes changes to the Total 10-Minute Reserves demand curve to provide that:

> d) Total 10-Minute Reserves. For quantities of Operating Reserves meeting the total 10−minute reserves requirement that are less than or equal to the target level for that requirement, the price on the total 10−minute reserves demand curve shall be $450/MW.

For all other quantities, the price on the total 10−minute reserves demand curve shall be $0/MW.

At subsection i of section 15.4.7, the NYISO proposes changes to the Long Island 30-Minute Reserves demand curve to provide that:

(i) Long Island 30−Minute Reserves. For quantities of Operating Reserves meeting the Long Island 30-Minute Reserves requirement that are less than or equal to the target level for that requirement, the price on the Long Island 30−Minute Reserves demand curve shall be $25/MW. For all other quantities, the price on the Long Island 30−Minute Reserves demand curve shall be $0/MW.

IV. Effective Date

The NYISO requests an effective date of March 15, 2011.

V. Stakeholder Approval

These amendments were unanimously approved by the NYISO Management Committee, with abstentions, on September 29, 2010. The NYISO's Board of Directors approved this filing on November 16, 2010.

VI. Communications and Correspondence

All communications and service in this proceeding should be directed to:

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VII. Service

The NYISO will electronically send a link to this filing to the official representative of each of its customers, to each participant on its stakeholder committees, to the New York Public Service Commission, and to the electric utility regulatory agency of New Jersey. In addition, the complete filing will be posted on the NYISO's website at www.nyiso.com. The NYISO will also make a paper copy available to any interested party that requests one. To the extent necessary, the NYISO requests waiver of the requirements of Section 35.2(d) of the Commission's Regulations (18 C.F.R. § 35.2(d) (2007)) to permit it to provide service in this manner.

VIII. Conclusion

Wherefore, for the foregoing reasons, the New York Independent System Operator, Inc. respectfully requests that the Commission accept for filing proposed the tariff revisions attached hereto with an effective date of March 15, 2011.

Respectfully submitted,

/s/ Elizabeth A. Grisaru
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