UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

TC Ravenswood, LLC	)	
	)	
v.	)	**Docket No. EL10-70-000**
	)	
New York Independent System Operator, Inc.	)	
	)	

ANSWER OF THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.

In accordance with Rule 213 of the Commission's *Rules of Practice and Procedure* and with the Commission's June 10, 2010 *Notice of Extension of Time*, the New York Independent System Operator, Inc. ("NYISO") respectfully submits this answer to the *Complaint of TC Ravenswood, LLC* ("Complaint") in the above-captioned proceeding.

TC Ravenswood, LLC ("TCR") is seeking to recover $2,437,121.48 (plus interest) that it incurred during June, July, August, and September 2009 ("Summer 2009") pursuant to Section 4.1.7a of the NYISO's Market Administration and Control Area Services Tariff ("Services Tariff"), that is not properly recoverable under that provision. Simply stated, TCR has not shown that its claimed costs were "variable operating costs" that would not have been incurred "but for" its compliance with a specific New York State reliability rule. The costs are therefore not eligible for recovery under Section 4.1.7a. Moreover, TCR is attempting to revive claims for compensation that the Commission previously rejected, ignoring Commission mandates that any attempt to renew such claims begin in the NYISO stakeholder process, and arguing that it is entitled to greater compensation than Commission precedent or the Federal Power Act ("FPA")[1] require. TCR has therefore failed to carry its burden under Section 206 of

[1] 16 U.S.C. §§ 791 *et. seq.* (2006).

the FPA to demonstrate that the NYISO's rejection of its requests for compensation was unjust, unreasonable, or unduly discriminatory. TCR's Complaint should consequently be denied in its entirety.

I. COMMUNICATIONS

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II. BACKGROUND

A. The Minimum Oil Burn Rule

The New York State Reliability Council ("NYSRC")[2] establishes reliability rules for the New York State Power System, and the NYISO complies with them in its operations and in its administration of the electricity markets. Certain rules require the NYISO, the Transmission Owners,[3] and generators to take specific actions in particular Load Zones in defined circumstances. These are referred to by the NYSRC as "local reliability rules." One such rule, I-R3, the "Minimum Oil Burn Rule," states that:

[2] The NYSRC was created simultaneously with the NYISO, by the then six investor-owned New York Transmission Owners, the New York Power Authority and the Long Island Power Authority. Section 2.1 of the *Agreement between the NYISO and the NYSRC* requires the NYSRC to "develop Reliability Rules which shall he complied with by the ISO and all entities engaged in transactions on the NYS Power System."

[3] Capitalized terms that are not otherwise defined herein shall have the meaning specified in Article II of the Services Tariff.

> [T]he NYS Bulk Power System shall be operated so that the loss of a single gas facility does not result in the loss of electric load within the New York City or Long Island zones).[4]

Under this rule, Consolidated Edison Company of New York, Inc. ("Con Edison") and the Long Island Power Authority establish procedures pursuant to which specifically identified units that have dual fuel capability are required to utilize a minimum level of an alternative fuel, usually oil, when loads are expected to reach certain levels. Generators operating with at least a minimum of the alternative fuel will remain on-line should the loss of gas contingency occur.

TCR owns and/or leases three large steam units (Units 10, 20, and 30) at the Ravenswood complex that have the ability to burn both natural gas and oil, normally No. 6 fuel oil ("Fuel Oil"). TCR was subject to the Minimum Oil Burn Rule during Summer 2009 at times when New York City load was forecasted to exceed 9000 MW.[5]

B. Prior Commission Proceedings Addressing Minimum Oil Burn Costs

In February 2007, KeySpan-Ravenswood, LLC ("KSR"), the former owner of TCR's facilities, filed a Section 206 complaint against the NYISO demanding compensation for lost profits during the 2006 Summer Capability Period allegedly as a consequence of its compliance with the Minimum Oil Burn Rule. The NYISO explained that the requested compensation was not available under the then-effective version of its Services Tariff but added that it was developing tariff revisions to address the potential under-compensation of dual fuel generators.

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[4] Local Reliability Rule I-R3 codified an existing operating protocol of the New York Power Pool that was originally instituted as a result of a construction accident in 1989 near the Hellgate Station (Bronx, NY). The accident disrupted gas supplies to the New York City power generating stations and caused the loss of electricity to New York City consumers. All of the NYSRC's reliability rules, including l-R3, were adopted as NYS regulations by the New York Public Service Commission in February 2006.

[5] *See NYISO Technical Bulletin #159* <http://www.nyiso.com/public/webdocs/documents/tech_bulletins/tb_159.pdf> (September 2009). The NYISO's Technical Bulletin notes that during the Summer Capability Period, one of TCR's three dual-fuel ready units is required to burn Fuel Oil when Con Edison system forecasted loads exceed 9000 MW. When those forecasts exceed 10,500 MW then all three TCR units must burn Fuel Oil.

The Commission rejected KSR's complaint.[6]

In April 2007, the NYISO submitted its proposed tariff revisions. It described how dual fuel generators could be economically disadvantaged during periods when Fuel Oil was more expensive than natural gas if the Minimum Oil Burn Rule were triggered after the close of the Day-Ahead Market. In that scenario, the NYISO market rules would preclude a generator that had received a Day-Ahead schedule from incorporating the higher costs of Fuel Oil into its energy offer. Such generators could account for the higher Fuel Oil costs in their real-time market offers but only at the increased risk of not being selected to run. The then-effective version of the Services Tariff authorized the NYISO to reimburse higher operating costs that were not reflected in energy offers when the costs were incurred "to ensure local reliability." Such reimbursements could only be made, however, after crediting margins that the generator earned in the Day-Ahead and real-time markets during that day. The NYISO and a majority of its stakeholders agreed that it would be appropriate to establish a supplemental payment mechanism to address this situation.

Section 4.1.7a of the Services Tariff resolved the margin restoration issue by creating a special compensation rule under which generators would be eligible to recover the "variable operating costs" of burning an alternate fuel in compliance with the Minimum Oil Burn Rule when: (i) such costs are not reflected in the unit's reference level; (ii) the indexed alternate fuel cost, being burned pursuant to the Minimum Oil Burn Rule (typically Fuel Oil) is more than the indexed variable operating costs for natural gas; (iii) the Minimum Oil Burn was activated; and (iv) the variable operating costs would not have been incurred but for the requirement to burn the required alternate fuel for Minimum Oil Burn purposes. Importantly, the NYISO explained that

[6] *KeySpan-Ravenswood, LLC v. New York Independent System Operator, Inc.*, 119 FERC ¶61,089, at P 14 (2007), *reh'g denied*, 119 FERC ¶ 61,319 (2007).

Section 4.17a did not compensate generators "for the storage and delivery infrastructure required to be able to burn an alternative fuel at any given time." As the transmittal letter recounted:

> The NYISO and its stakeholders are still pursuing a design mechanism to capture these costs. Complicating this effort is that the capability to operate a unit using an alternative fuel provides economic opportunities when the primary fuel is unavailable or less economic than the alternative fuel. Design options such as compensating only the cost to maintain this equipment have been explored but no final solutions have been reached. The NYISO is committed to bringing this unresolved issue back to its stakeholders for further work over the next several months. The NYISO continues to consider this request in stakeholder meetings and will propose a recovery mechanism for fixed costs if and when it and its stakeholders agree on its necessity and its design.[7]

KSR protested the exclusion of both: (i) "storage and deliverability" costs incurred, as a result of being capable upon instruction, "to burn an alternative fuel at any given time. . . ."; and (ii) fixed costs associated with maintaining and investing in equipment required to enable a Minimum Oil Burn generator to switch to "an alternative fuel at any given time."[8] Among other things, KSR argued that its recoverable incremental storage and deliverability costs should include costs associated with "barge transportation." The Commission denied the protest and found Section 4.1.7a to be just and reasonable, notwithstanding the exclusion of these additional costs.[9]

KSR asserted on rehearing that it was unjust, unreasonable, and unduly discriminatory for the Commission to deny its claims for "incremental storage, delivery infrastructure, and related items necessary to maintain its fuel switching capabilities."[10] It again claimed that "barge transportation and lease arrangements" were incremental storage and delivery infrastructure costs

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[7] *New York Independent System Operator, Inc.*, Filing of Tariff Revisions to Establish Margin Restoration Payments, and Recovery Mechanisms, for Units Complying with a Specific Local Reliability Rule at 7, Docket No. ER07-748-000 (filed April 13, 2007) ("NYISO MOB Rule Tariff Filing").

[8] *New York Independent System Operator, Inc.*, 119 FERC ¶ 61,130 at P 14 (2007).

[9] *Id.* at P 17.

that should be recoverable under Section 4.1.7a on the same basis as incremental fuel oil commodity costs.

KSR also reiterated its prior claim that it was entitled to "some recovery" of the fixed capital and O&M costs "associated with facilities that enable generators to maintain their capabilities to respond to fuel-switching instructions under the Minimum Oil Burn Rule."[11] At the same time, it expressly did not seek rehearing of the Commission's denial of its request that the NYISO be directed to establish a fixed cost recovery mechanism.[12] The Commission denied KSR's Request for Rehearing, upholding its original decision and clarifying that there were "concerns that arise with respect to the costs of oil storage and delivery infrastructure that are not present with respect to the incremental variable costs of burning oil"[13] (the NYISO addresses these "concerns" *infra* in Section II.C). The Commission was clear that "barge transportation and lease payments" were the kinds of storage and delivery infrastructure costs that were subject to these concerns.[14] It went to say that the various "questions and concerns related to further compensation for the Rule I-R3 generators" for the costs of oil storage and delivery infrastructure would best be addressed through the NYISO stakeholder process because it had the potential to "formulate ways of answering these questions and addressing these concerns."[15] It observed:

> Ravenswood and other dual-fuel generators subject to Rule I-R3 may use the capability to burn oil for reasons other than complying with Rule I-R3.

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[10] *See New York Independent System Operator, Inc.*, Request for Rehearing of KeySpan Ravenswood at 7-12, Docket No. ER07-748-000 (filed June 11, 2007).

[11] *Id.* at n. 46.

[12] *Id.*

[13] *New York Independent System Operator, Inc.*, 121 FERC ¶ 61,039 at P 22 (2007).

[14] *Id.* at n. 16 (citing page 16 of KSR's request for rehearing in that proceeding which described the costs for which it sought recovery as barge transportation and lease payments).

[15] *Id.* at P 23.

> Ravenswood and other dual-fuel generators subject to Rule I-R3 may use the capability to burn oil of their own accord to earn greater Day-Ahead margins when natural gas is unavailable or when the price of oil is less than the price of natural gas.[16]

As a result, the Commission concluded that Section 4.1.7a was just and reasonable even though it did not provide for the recovery of "incremental costs for oil storage and delivery infrastructure" (or for fixed costs). If Ravenswood were "dissatisfied with the length of time that the stakeholder process takes [to address incremental costs for oil storage and delivery infrastructure] or with the results of the stakeholder process," it could raise its concerns in a complaint.[17]

On appeal, the United States Court of Appeals for the District of Columbia Circuit upheld all of the Commission's rulings. Among other things, the court agreed that it was reasonable for the Commission to conclude that "infrastructure compensation" implicated distinct concerns that were not relevant to the incremental variable costs of burning oil and, therefore, that Section 4.1.7a, was just and reasonable even though it did not provide for the recovery of those costs.[18]

C. Dual Fuel Capability Confers Significant Economic Advantages

TCR's Complaint focuses exclusively on the costs that it incurs under the Minimum Oil Burn Rule during periods when Fuel Oil is more expensive than natural gas. Left unmentioned is the fact that having, and maintaining, dual fuel capability confers various economic advantages on dual fuel capable generators, including TCR. The existence of these advantages, and the absence of a mechanism in the Services tariff to apportion the costs of dual-fuel capability between Minimum Oil Burn Rule compliance and other uses led the Commission to

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[16] *Id.* at P 22.

[17] *Id.* at P 23.

[18] *KeySpan-Ravenswood v. FERC*, No. 07-1278 Consolidated with 07-1517, 2009 U.S. App. LEXIS 10014, at 3 (D.C. Cir. May 7, 2009).

reject KSR's claims in 2007. These considerations should be of equal importance to the ultimate decision in this proceeding.

As the Commission has recognized, "the capability to operate a unit using an alternative fuel provides economic opportunities when the primary fuel [in this case, natural gas] is unavailable or less economic than the alternative fuel."[19] TCR tries to downplay this advantage by suggesting that "economic opportunities to burn Fuel Oil are virtually non-existent."[20] This is belied by TransCanada's own website, which notes that TCR's dual fuel capability "enables TransCanada to generate electricity with the most economic fuel mix to meet system demands."[21] It is also contradicted by TCR's acknowledgement that "Fuel Oil is procured and delivered to the Ravenswood site . . . ," for, among other things, "TC Ravenswood use for electric economic dispatch when Fuel Oil is less costly than natural gas . . . "[22] and for use during "actual gas system interruptions . . . ."[23]

While natural gas has, in recent years, often been less expensive than Fuel Oil, that has not always been so, and will not necessarily always be so in the future. According to the most recent *State of the Market Report* by the NYISO's independent market monitor ("IMM"), "[p]rior to 2006, [Fuel Oil] was often less expensive than natural gas, allowing oil-fired steam units to be relatively economic compared with gas-fired combined cycle units."[24] Even in the

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[19] *New York Independent System Operator, Inc.*, 121 FERC ¶ 61,039 at P 22 (2007).

[20] TCR Complaint at 14, n. 36.

[21] *See < http://www.transcanada.com/docs/About_Us/ravenswood.pdf>* ("The boilers in Units 10, 20, and 30 are all capable of burning both No. 6 fuel and natural gas, which enables TransCanada to generate electricity with the most efficient fuel mix to meet system demands.").

[22] TCR Exhibit No. TCR-11 at 3.

[23] TCR Exhibit No. TCR-1 at 24-25.

[24] *See* David B. Patton, Independent Market Advisor, 2008 State of the Market Report New York ISO, at 26 (September 2009) *available at* <http://www.potomaceconomics.com/uploads/nyiso_reports /NYISO_2008_SOM_Final_9-2-09.pdf>. *See also,* NYISO MOB Rule Tariff Filing at 6 ("During the initial years

last few years, Fuel Oil has sometimes been more economical than natural gas, as was the case on 16 percent of the days for all 2008[25] and 84 percent of days for January 2009.[26] Moreover, a generator with dual fuel capability may choose to burn oil even when it is more expensive than natural gas if the latter "is difficult to obtain on short notice or if there is uncertainty about its availability."[27] A generator with dual fuel capability also has the option of using oil as its fuel when its supply of natural gas is interrupted rather than derate its unit and leave the market completely.[28]

In addition, Con Edison has previously represented that dual fuel capability allows generators such as TCR to qualify for non-firm retail gas transportation service that is less expensive than firm delivery. Such capability may also entitle them to receive interruptible commodity service.[29] The NYISO's understanding is that these economic advantages continue to be available to TCR today.

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of NYISO operation, this issue did not arise because the cost of oil generally trailed natural gas by as much as 20 percent.").

[25] *Id.* at 27.

[26] *See, e.g.,* David B. Patton, Market Monitoring Unit, 2009 State of the Market Report New York ISO Electricity Markets, at 26 (April 2010) *available at* <http://www.potomaceconomics.com/uploads/ nyiso_presentations/2009_NYISO_SOM_Final_4-30-2010.pdf> ("2008 State of the Market Report"); *See also,* Exhibit No. TCR-11 at 14 (noting that in January 2009 Fuel Oil was burned for Ravenswood use and not I-R3 Orders).

[27] *Id.* Mr. Prestia's testimony likewise admits that Fuel Oil would be procured and delivered for actual gas system interruptions. TCR-11 at 3. The *2008 State of the Market Report* also pointed out that the presence of generators with dual fuel capability benefits the market as a whole. It stated that "[s]ince most large steam units can burn residual fuel oil (No. 6) or natural gas, the effects of natural gas price spikes on power prices are partly mitigated by generators switching to oil. 2008 State of the Market Report at 26.

[28] Unit derates for fuel unavailability, such as during a gas interruption, reduce the Unforced Capacity a unit is entitled to offer in the Installed Capacity market. Services Tariff at §5.12.6a, *see* also Installed Capacity Manual at § 4.5 (June 2010), *available at* <http://www.nyiso.com/public/webdocs/documents/manuals/ operations/icap_mnl.pdf>.

[29] *See New York Independent System Operator, Inc.*, Request for Leave to File Answer and Answer of Consolidated Edison Company of New York and Orange and Rockland Utilities, Inc., at 4, Docket No. ER07-748-000 (filed June 29, 2007).

Finally, the current version of the Demand Curve for the New York City capacity market specifically incorporates the capital costs that generators incur as a result of having dual fuel capability.[30] Generators that participate in that capacity market therefore receive compensation specifically directed at the fixed costs associated with that capability.

III. ANSWER

A. The Complaint Must Be Denied because it Collaterally Attacks Prior Commission Rulings Regarding the Scope of Section 4.1.7a

1. TCR Impermissibly Seeks to Recover Categories of Costs that the Commission Has Previously Deemed to Be Outside the Scope of Section 4.1.7a

TCR does not attempt to argue that Section 4.1.7a itself is unjust, unreasonable, or unduly discriminatory. Nor does it openly attempt to revive past claims that the Commission's orders accepting Section 4.1.7a were wrongly decided. There can thus be no question that the current version of Section 4.1.7a is just and reasonable, that it does not currently encompass oil and storage deliverability costs, and that it did not do so during Summer 2009.

TCR contends instead that the NYISO wrongly declined to pay it $2,437,121.48 (plus interest) for purported "variable operating costs" incurred during Summer 2009 that it alleges are recoverable given the "plain language" of Section 4.1.7a. These costs fall into three general categories (together, "Claimed Costs"): (i) TCR's *pro rata* share of monthly lease payments to have barges deliver Fuel Oil ("Barge Delivery Lease Payments");[31] (ii) TCR's *pro rata* share of lease payments for third-party off-site Fuel Oil tank and barge storage for days when it was

[30] *See, e.g., New York Independent Transmission System Operator, Inc.*, Tariff Revisions to Implement Revised ICAP Demand Curves for Capability Years 2008/2009, 2009/2010 and 2010/2011 at 8-9, Docket No. ER08-283-000 (November 30, 2007) ("The Consultants added the capital cost for dual-fuel capability to the hypothetical peaking unit in NYC, which added approximately $6.2 million to the capital costs of the LMS-100."); *See also, New York Independent System Operator, Inc.*, 122 FERC ¶ 61,064 (2008) (accepting the NYISO's tariff filing).

[31] The NYISO compensated TCR for its costs of actually purchasing the Fuel Oil under Section 4.1.7a.

required to provide Minimum Oil Burn Rule service ("Tank and Barge Storage Lease Payments"); and (iii) other charges associated with on-site Fuel Oil and delivery equipment ("On-Site Equipment Costs").[32] TCR alleges that all three categories are recoverable under the currently effective version of Section 4.1.7a and Commission precedent governing the compensation of generators that provide "reliability services."

It is clear, however, that each category of Claimed Costs either corresponds exactly to, or, at a minimum, overlaps substantially with, costs that the Commission previously found to be beyond the scope of Section 4.1.7a. Specifically, TCR has not explained how its Barge Delivery Lease Payments differ from the costs associated with "barge transportation and lease arrangements" that were rejected in 2007. Its claimed Tank and Barge Storage Lease Payments and On-Site Equipment Costs likewise appear to fall within the ambit of previously rejected "incremental storage and delivery infrastructure costs." Fundamentally, each category of Claimed Costs supports TCR's ability to comply with the Minimum Oil Burn Rule and to enjoy the economic advantages of dual fuel capability. The question of their possible recoverability therefore engenders the same questions that caused the Commission to reject claims to recover the same types of costs in the past.

Given the Commission's previous findings regarding the scope of Section 4.1.7a, the Complaint should be denied as an impermissible attempt to obtain retroactive relief under Section 206 of the FPA (which only provides for prospective relief)[33] and as a collateral attack

[32] *See* Complaint at 2.

[33] 16 U.S.C. § 824e(b) (stating that in a proceeding initiated under Section 206, the Commission can establish a refund effective date "not … earlier than the date of the filing of such complaint nor later than 5 months after the filing of such complaint."); *See also*, *Towns of Concord, Norwood and Wellesley v. FERC*, 955 F.2d 67, 71 n.2 (D.C. Cir. 1992) (providing that under the rule against retroactive ratemaking the Commission cannot adjust "current rates to make up for a utility's over or under-collection in prior periods.") (internal citations omitted); *KeySpan-Ravenswood v. FERC*, No. 07-1278 Consolidated with 07-1517, 2009 U.S. App. LEXIS 10014, at 3 (D.C. Cir. May 7, 2009) (stating that "its … holding in *City of Anaheim v. FERC*, 558 F.3d 521 (D.C. Cir. 2009), suggests … [that "(section 206(b) 'authorizes only retroactive refunds (rate decreases), not retroactive rate increases'".).

on earlier Minimum Oil Burn Rule precedent.[34] TCR is effectively asking the Commission to retroactively determine that Section 4.1.7a authorized the recovery of "incremental storage and delivery infrastructure costs" during Summer 2009 despite prior Commission rulings that it did not. Even if the Complaint were deemed not to constitute a claim for retroactive relief it still must be denied because TCR has not satisfied its burden of showing that its Claimed Costs differ from those that the Commission previously found were beyond the scope of Section 4.1.7a.

2. TCR Impermissibly Seeks to Recover Oil Storage and Deliverability Costs and Fixed Costs Without Having First Worked Through the Stakeholder Process

The Commission's earlier Minimum Oil Burn orders were clear that future questions concerning compensation for incremental Fuel Oil storage and delivery infrastructure costs (and for fixed costs) should be addressed through the stakeholder process in the first instance. The Commission correctly understood that the stakeholder process was the vehicle best suited to explore, and perhaps to resolve, the key question of whether costs that enabled generators to maintain an economically advantageous dual fuel capability ought to be eligible for compensation in the same way as costs incurred solely as a result of Minimum Oil Burn Rule compliance.

The October 2007 Order indicated that any party dissatisfied by the stakeholder process could seek redress through a complaint. Importantly, it did not invite any entity to resume litigation without first attempting to work through a stakeholder process.

In contravention of the October 2007 Order, TCR, like KSR before it, has not pursued tariff amendments to provide for the recovery of incremental Fuel Oil storage and delivery

[34] *See, e.g., Southern Co. Services, Inc.*, 129 FERC ¶ 61,253 at P 37 (2009) (stating that "collateral attacks on final orders and relitigation of applicable precedent, especially by parties that were active in the earlier case, impede the finality and repose in agency decisions that are essential to administrative efficiency, and are therefore

infrastructure costs. The NYISO is not aware of any effort by TCR to introduce such an amendment.[35] Given the history of Commission and judicial rulings on the recoverability of storage, barge, and deliverability costs it should have been apparent to TCR that attempting to work through a stakeholder process was a necessary pre-requisite to filing the Complaint.

TCR appears to recognize its vulnerability on this point. It suggests that its request to enter into an Expedited Dispute Resolution process with the NYISO was sufficient to comply with its obligation to exhaust alternative remedies before filing a complaint.[36] Of course, this contention ignores both the October 2007 Order and the Commission's general preference that aggrieved parties attempt to resolve their issues through the stakeholder process before resorting to litigation. TCR's complaint should therefore be denied.

B. The Complaint Must Be Denied Because the Claimed Costs Are Not "Variable Operating Costs" that Would Not Have Been Incurred But For the Minimum Oil Burn Rule

1. TCR's Definition of "Variable Operating Costs" Ignores the Commission's Minimum Oil Burn Precedent and Is Overbroad

TCR acknowledges that the Commission-approved Section 4.1.7a of the Services Tariff does not provide for the recovery of its fixed costs.[37] In addition, as was explained above, Section 4.1.7a has been found to be just and reasonable even though it does not cover

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strongly discouraged"), *citing, Entergy Nuclear Operations, Inc. v. Consolidated Edison Co. of New York, Inc.*, 112 FERC ¶ 61,117 at P 12 (2005) and *NSTAR Electric Co.*, 120 FERC ¶ 61,261 (2007)).

[35] *See also, TC Ravenswood, LLC,* Motion to Intervene and Protest of the New York Transmission Owners and the City of New York, at 4, Docket No. ER10-1359-000 (filed June 17, 2010) (stating that "Ravenswood never presented this specific proposal, whether in the form of a proposed amendment to the NYISO Services Tariff MOB provisions or otherwise, to any of the appropriate NYISO stakeholder committees. Rather, Ravenswood went straight to the Commission and thereby bypassed both the NYISO stakeholder process and the NYISO Services Tariff.").

[36] *See* Complaint at n. 17, *citing, Niagara Mohawk Power Corp. v. New York Independent System Operator, Inc.*, 114 FERC ¶ 61,098 at P 1 (2006).

[37] *See, e.g.,* Complaint at 11. *See also, TC Ravenswood, LLC*, Application of TC Ravenswood, LLC to implement a Minimum Oil Burn Service Cost of Service Recovery Rate Schedule, at 2 and 9, Docket No. ER10-1359-000 (filed May 27, 2010).

"incremental costs for oil storage and delivery infrastructure." Rather than openly challenging these established facts, TCR tries to circumvent them by arguing that the very types of costs that were previously found to be outside the ambit of Section 4.1.7a are nevertheless recoverable "variable operating costs."

Section 4.1.7a of the Services Tariff does not expressly define the term "variable operating costs." Neither does any other NYISO document nor the Commission's prior Minimum Oil Burn orders. TCR argues that the Commission should therefore mechanically apply definitions of fixed and variable costs taken from cost-of-service ratemaking decisions. According to TCR's interpretation, fixed costs are limited to those that do not vary with the amount of energy produced and variable costs are those which do. Variable costs would therefore "include, but are not limited to, costs that vary based on use, avoidable costs that would not have been incurred but for the production of energy, and incremental operation and maintenance costs that arise because of the use of equipment to produce energy."[38] By defining "variable costs" so broadly, TCR broadens the term to encompass all of its Claimed Costs. Even when so broadly defined, however, TCR fails in its attempt to show that Claimed Costs are recoverable "variable operating costs" because as Dr. Patton[39] illustrates in his affidavit, the lion's share of TCR's Claimed Costs cannot be classified as variable operating costs under Section 4.1.7a because they do not vary directly based on the volume of Fuel Oil burned in compliance with the Minimum Oil Burn Rule.

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[38] Complaint at 13, *citing Southern Co. Servs., Inc.,* 61 FERC ¶ 61,075 at 61,307 (1992), *reh'g denied,* 64 FERC ¶ 61,033 (1993). The Commission's cost-classification precedent is, however, not as absolute or susceptible to mechanical application as TCR claims. Even the precedent cited by TCR recognizes that past cases included numerous "*ad hoc* rulings on disputes over the correct classification of fixed and variable expenses in particular factual situations." *Southern Co. Servs., Inc* at 61,311. There is clearly room for the Commission to conclude that the Claimed Costs should be classified as fixed costs.

[39] Dr. David B. Patton is a Principle in Potomac Economics, the NYISO's Market Monitoring Unit.

2. TCR's Claimed Barge Delivery Lease Payments and Tank and Barge Storage Lease Payments Are Not Recoverable Under Section 4.1.7a

TCR's Barge Delivery Lease Payments and Tank and Barge Storage Lease Payments account for all but $78,637.51 of its Claimed Costs. Although a number (but not all) of these costs varied from month to month during Summer 2009, that variation was driven not by the number of barrels of Fuel Oil that TCR burned for Minimum Oil Burn Rule compliance *per se* but on TCR's usage relative to Con Edison's steam operations.

Specifically, the Complaint indicates that *pro rata* shares of Barge Delivery Lease Payments were determined by contractual arrangements between TCR, an affiliate, TC Ravenswood Services Corp. ("TC Services"), and Con Edison, which maintains significant regulated steam utility operations on and off the Ravenswood site that utilize Fuel Oil.[40] According to the Complaint, during Summer 2009, TC Services procured Fuel Oil on TCR's behalf and also sold it to Con Edison's steam operations pursuant to a long-term, cost-based Fuel Oil supply agreement.[41] Fuel Oil delivery and handling costs were reportedly allocated between TCR and Con Edison based on their respective monthly *pro rata* usage of Fuel Oil. Similarly, TCR states that its Tank and Barge Storage Lease Payments were divided between it and Con Edison's utility steam operations pursuant to an agreement that allocated 65% of off-site tank storage costs, and 35% of barge storage costs, to TCR.[42] The NYISO does not have access to any of the relevant contracts and thus can only rely on the Complaint's description of them at this time.

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[40] Complaint at 14-15.

[41] *See* TCR Exhibit No. TCR-11 at 3.

[42] *See* TCR Exhibit No. TCR-11 at 6.

With respect to the Barge Delivery Lease Payments, usage by TCR and Con Edison determined the *pro rata* allocations between them pursuant to their contract. Thus it was not TCR's usage alone, or even the usage for Minimum Oil Burn Rule purposes, but its usage relative to Con Edison's, that drove the variations in its Claimed Costs. As Dr. Patton explains, this variation in the allocation of a fixed cost does not convert the fixed cost into a variable cost and it does not matter that the amount of costs allocated between the two companies might vary depending on the number of days for which TC Services estimated it would need barges for the month.[43] Each company's total share of the costs still varied depending on the *proportionate* number of barrels each used each month.

With respect to the Tank and Barge Storage Lease Payments, TCR's allocated share for Minimum Oil Burn Rule compliance was effectively not dependent on the amount of Fuel Oil used for Minimum Oil Burn purposes but on its *pro rata* share of TCR's total Fuel Oil usage. In practice, in almost no month did this *pro rata* allocation vary with actual usage for Minimum Oil Burn Rule purposes. That is, in months in which the Minimum Oil Burn Rule was triggered, there typically was no other TCR use of Fuel Oil. Hence, the amount of Fuel Oil burned on a given day for Minimum Oil Burn Rule purposes had no effect whatsoever on the size of the Tank and Barge Storage Lease Payments allocated by TCR to Minimum Oil Burn Rule compliance. Whether TCR burned oil for its own purposes on a given day was at least as determinative of the amount of Tank and Barge Storage Lease Payments allocated to Minimum Oil Burn Rule compliance, as was the volumetric amount of Fuel Oil actually burned for Minimum Oil Burn Rule purposes.

[43] *See* Attached Affidavit of David B. Patton at P 13.

The total amount of the lease payment is a fixed infrastructure cost notwithstanding the fact that the cost is shared and that each company's portion may vary from month to month. As Dr. Patton states, for purposes of Section 4.1.7a "variable operating costs" should be those that vary directly with the quantity of Fuel Oil burned in compliance with the Minimum Oil Burn Rule -- without reference to uses by other entities.[44] By contrast, the per barrel charge to TCR for 1,000 barrels of Fuel Oil used to comply with Minimum Oil Burn Rule requirements could be as much as 0.5% of the monthly fixed costs if there was no use by Con Edison in that month but would drop to 0.25% of those costs if Con Edison used 500 barrels.

Moreover, unlike TCR's share of the Barge Delivery Lease Payments, it incurred its contractual share of the Tank and Barge Storage Lease Payments regardless of whether the Minimum Oil Burn Rule was invoked or not. Section 4.1.7a is clear that to be recoverable the cost must be incurred "only because Local Reliability Rule I-R3 . . . was invoked."[45] Since TCR would face its contractual share of the Tank and Barge Storage Lease Payments whether there was Minimum Oil Burn Rule activation in the month or not, TCR's share of these lease payments cannot properly be assigned to the Minimum Oil Burn Rule compliance.

Even though TCR asserts that it is only seeking to recover the portion of its Fuel Oil delivery, storage, and related infrastructure costs that it incurs to satisfy its Minimum Oil Burn compliance obligations, it also concedes that it incurs these types of costs in part to maintain its dual fuel capability.[46] As was detailed in Section II.C, there are potentially significant economic advantages that come from having dual fuel capability and that raise serious questions as to whether generators should be receiving additional non-market compensation for maintaining it.

[44] *See Id.* at P 23.

[45] Services Tariff § 4.1.7a.

[46] *See* TCR Exhibit No. TCR-11 at 3.

Therefore the same considerations that caused the Commission to deny KSR compensation under Section 4.1.7a for its Fuel Oil storage and deliverability militate against allowing TCR to recover the Claimed Costs now.

Finally, even if the Commission were to conclude that the Tank and Barge Lease Payment costs qualify as “variable operating costs” under the Services Tariff it should, at a minimum, exclude the portion of its barge storage costs incurred during the NYISO’s Winter Capability Period, *i.e.*, November 1 through April 30. The NYISO understands that in order to remain eligible for the favorable non-firm delivery rates offered under Con Edison’s retail gas tariff, TCR must maintain 45,000 barrels of Fuel Oil in its on-site tank storage and 55,000 barrels in barge storage. Therefore, during the Winter Capability Period, all lease payments associated with barge storage would be for uses unrelated to compliance with the Minimum Oil Burn Rule.

3. TCR’s Claimed On-Site Equipment Costs Are Not Recoverable Under Section 4.1.7a

TCR’s On-Site Equipment costs are not allocated between it and Con Edison in the same manner as its Barge and Delivery Lease Payment and Tank and Barge Storage Lease Payment costs. Nevertheless, based on the information provided in the Complaint these costs are not variable operating costs that would not have been incurred “but for” the Minimum Oil Burn Rule. TCR’s On-Site Equipment Costs pertaining to fuel handling and delivery, like other costs that the Commission previously found to be outside the scope of Section 4.1.7a, appear to directly support its general dual fuel capability as well as its ability to comply with the Minimum Oil Burn Rule.

C. The FPA Does Not Entitle TCR to Special Non-Market Based Compensation for Any and All Costs that it May Wish to Recover

1. The NYISO's Rejection of TCR's Claimed Costs Is Consistent with Both Commission and Judicial Precedent

The Complaint mischaracterizes the Commission's precedent on the extent to which independent generators that provide "reliability services" are entitled to recover their costs. According to TCR, the NYISO's determination that its Claimed Costs were unrecoverable is somehow a "violation of the most basic bedrock principles of rate regulation."[47] It implies that the NYISO is responsible for having market rules that guarantee generators' recovery of all of their costs.

In reality, neither the Commission's, nor the Supreme Court's, precedent establishes any such guarantee. Instead, the law requires only that generators have a "reasonable opportunity" to recoup their costs. This rule is derived from the *Hope* and *Bluefield* decisions which held that a traditional regulated utility "should be afforded the opportunity to recover its costs and earn a return commensurate with that earned by other enterprises of comparable risk."[48] The rule is understood to protect regulated utilities from receiving compensation at levels so low as to be confiscatory.[49] In the context of organized wholesale power markets, the *Hope and Bluefield*

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[47] Complaint at 11.

[48] Complaint at 9-10, *citing FPC v. Hope Natural Gas Co.,* 320 U.S. 591, at 603 (1944) and *Bluefield Water Works* & *Improvement Co.* v. *PSC,* 262 U.S. 679 (1923).

[49] *See, e.g., ISO New England Inc.,* 121 FERC ¶61,097, at P 32 (2007) (finding that "a just and reasonable rate, term or condition of service … is [not] confiscatory" *citing, Midwest Independent Transmission System Operator*, 109 FERC ¶61,157 at P 142-43 (2004); *FPC v. Texaco Inc.*, 417 U.S. 380 (1974) ("All that is protected against, in a constitutional sense, is that the rates being fixed by the Commission be higher than a confiscatory level."); *Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968) ("Any rate selected by the Commission from the broad zone of reasonableness permitted by the [Natural Gas] Act cannot properly be attacked as confiscatory."); *FPC v. Hope Natural Gas Co.,* 320 U.S. 591, 600-01 (1944) ("The fixing of prices, like other applications of the police power, may reduce the value of the property which is being regulated. But the fact that the value is reduced does not mean that the regulation is invalid."); *Southern Company Services, Inc*., 57 FERC ¶61,093 (1991) ("The Commission's action in this proceeding—ensuring that ratepayers are not charged an excessive, unjust and unreasonable rate—is not an unconstitutional taking, even though it may produce a rate less than the rate [commenters] would like to charge.")).

requirement is normally satisfied when the markets are deemed to be workably competitive.[50] The Commission has been clear that there can be "no basis for a generator operating under market-based rates authority to claim that for it to remain available in a competitive market, it must receive energy revenues equivalent to a full cost of service," since "in a competitive market, the Commission is responsible only for assuring that [a resource] is provided the *opportunity* to recover its costs."[51]

The NYISO-administered markets have consistently been found to be workably competitive.[52] Generators normally recover their marginal costs, and if they are infra-marginal, may recover a contribution to their fixed costs, from their sales in the energy markets. They also have the opportunity to recoup their legitimate going forward fixed costs through revenues received from the markets for Installed Capacity, Operating Reserves, and Regulation Service as well as from non-market revenue earned from providing Voltage Support Service.[53] In addition, as was noted above: (i) capacity market payments to New York City generators like TCR include

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[50] *See, e.g.,. ISO New England, Inc.*, 130 FERC ¶61,108, at P 32 (2010) (finding that "*Hope* reflects 'a superseded cost-of-service paradigm' that 'envisioned neither competition among service providers nor any opportunity for them to earn market-based rates.' … where there is a competitive market for capacity … 'unlike the regulated markets addressed in *Hope* …*,* competitive markets do not guarantee the opportunity for return of/on investment through cost-based rates. That opportunity is provided through authority to charge market-based rates for services."), *citing Pacific Gas and Electric Co.*, 91 FERC ¶63,008, at 65,111 (2000); *Bridgeport Energy, LLC*, 113 FERC ¶61,311 at P 29 (2005)); *see also, Bridgeport Energy, LLC*, 113 FERC ¶61,311 at P 47 (2005) (finding that "[i]t is reasonable and expected in a competitive market that there will be periods where full cost recovery is not realized. In a competitive market, the Commission does not have an obligation to guarantee cost recovery, especially for a highly efficient merchant generator, capable or earning a significant portion of available market revenues. Instead the Commission is responsible for assuring that … [an entity] is provided the opportunity to recover its costs.").

[51] *ISO New England Inc. and New England Power Pool Participants Committee*, 128 FERC ¶ 61,023 at P 34 (2009), *citing Bridgeport Energy, LLC*, 113 FERC ¶61,311 at P 29 (2005).

[52] *See, e.g.,* David B. Patton, Market Monitoring Unit, 2009 State of the Market Report New York ISO Electricity Markets (April 2010) *available at* <http://www.potomaceconomics.com/uploads/nyiso_presentations/2009_NYISO_SOM_Final_4-30-2010.pdf>

[53] *See, e.g., New York Independent System Operator, Inc.,* Filing Requesting Authority to Prospectively Apply New Mitigation Rules to Three Specifically Identified Generators, at Attachment B - Affidavit of Dr. David B Patton at PP 36-37 (filed September 4, 2009).

a component that helps them to recover the fixed costs associated with having and maintaining dual fuel capability; and (ii) compensation under 4.1.7a allows TCR to retain any Day-Ahead margin it may earn even when required to burn more expensive Fuel Oil.

In short, the NYISO is under no legal obligation to develop non-market-based mechanisms to ensure that TCR will recover any and all costs that it may incur in the course of its operations. By administering competitive electricity markets, the NYISO is fulfilling its obligation to ensure that generators have a "reasonable opportunity" to recover their costs. The fact that the NYISO previously concluded that a supplemental compensation mechanism was appropriate to ensure that generators could recover genuine variable operating costs that would not have been incurred but for the Minimum Oil Burn Rule does not alter this analysis. Nor does it give TCR a right to receive special payments for any cost that it may assert is related to its Minimum Oil Burn Rule obligations.

2. The Precedent Cited by TCR is Distinguishable and Does Not Support Its Position

TCR tries to buttress it argument by invoking the Commission's 2006 decision in *Independent Energy Producers Assn. v. California Independent System Operator Corp.* ("*IEPA*").[54] *IEPA* is, however, readily distinguishable from the facts and circumstances of this proceeding.[55]

IEPA involved the "must offer" obligation that was introduced in California as a result of the 2000-2001 energy crisis. Most generators serving California were compelled to offer all of their capacity in real-time during all hours when they were available and were not already

[54] 116 FERC ¶ 61,069 (2006).

[55] Of course, if *IEPA*, which was issued in 2006, truly mandated that generators were guaranteed recovery of any and all costs related to their provision of "reliability services" the Commission would not have found the current version of Section 4.1.7a to be just and reasonable in 2007.

scheduled to run through a bilateral agreement. The Commission found that the "must offer" rule had come to have perverse consequences, including suppressing Load-Serving Entities' incentives to engage in long-term contracting and driving real-time energy prices artificially low. Generators were also not receiving any day-ahead market compensation for capacity offered in real-time under the must-offer obligation. The Commission therefore concluded that significant changes had to be made to the must offer rule to ensure that California generators had the requisite "reasonable opportunity" to recover their costs. These factors are not present in this proceeding because the Minimum Oil Burn Rule impacts a comparatively smaller portion of the output of fewer generators and exists within the framework of the well-functioning NYISO-administered markets.

More generally, the Commission's approach in *IEPA* is in keeping with its policy disfavoring non-market-based compensation arrangements, such as "reliability must run" ("RMR") contracts. The Commission has consistently been reluctant to authorize those kinds of arrangements absent unusual circumstances, *e.g.,* when a generator that is deemed to be essential to the preservation of reliability cannot earn sufficient market revenue to continue operations unless it receives cost-based payments.[56] Even then, the Commission has normally insisted that non-market compensation rules are temporary stopgaps that may remain in place only until suitable market-based solutions can be introduced.[57]

[56] *See, e.g., Blumenthal v ISO New England, Inc.*, 117 FERC ¶61,038 at P 69 (2006) ("on several occasions we have stated our preference that generators not operate under RMR contracts and that RMR agreements should be a last resort. However, we must balance that preference with the concern that an inability to recover costs may prevent a generator from being available to provide reliability service in constrained areas."); *Bridgeport Energy, LLC*, 113 FERC ¶61,311 at P 27 (2005) (explaining that "RMR contracts are tools of last resort" because they may "understate the value of energy consumed and discourage efficient entry and demand response" and may "shift the risk of investment from investors back to consumers."); *Bridgeport Energy, LLC*, 118 FERC ¶61,243, at n. 34 (2007) (stating that "The Commission has repeatedly expressed dissatisfaction with these 'non-market' mechanisms and has adopted a 'last resort' policy when considering RMR agreements." (internal citations omitted).)

[57] *See, e.g., ISO New England, Inc. and New England Power Pool*, 118 FERC ¶61,018, at P 46 (2007); *Devon Power LLC*, *et al.*, 106 FERC ¶61,264, at P 28 (2004).

Unlike the California generators in *IEPA*, or the New England generators in the various RMR cases, there has been no demonstration that TCR requires additional cost-based compensation from the NYISO for its operations to remain viable, nor does it appear that TCR could plausibly make such a demonstration. Nor does there appear to be any possibility that the NYISO's denial of its Claimed Costs will impact TCR's revenues so severely as to implicate the concerns about confiscatory rates that animated *Hope* and *Bluefield.*

In short, Commission precedent on generator cost recovery, including *IEPA*, lends no support to TCR's contention that the "bedrock principles of rate regulation" compel the NYISO to pay its Claimed Costs. If anything, the Commission's discomfort with non-market based compensation mechanisms suggests that the definition of "variable operating costs" in Section 4.1.7a should be construed as narrowly as possible and supports the NYISO's view that it does not encompass TCR's Claimed Costs.

IV. CONCLUSION

The NYISO's position regarding the recovery of Minimum Oil Burn Rule costs has not changed since 2007. The NYISO has always believed that it is appropriate for generators with dual fuel capability to recover variable operating costs that they would not have incurred but for their compliance with the Minimum Oil Burn Rule, such as the commodity cost of burning more expensive Fuel Oil. The NYISO amended its tariff to provide compensation for those costs and paid them to TCR for Summer 2009. At the same time, the NYISO has consistently taken the position that Section 4.1.7 of the Services Tariff does not provide for compensation of oil storage and deliverability costs (including barge transportation lease costs). The Commission has found this exclusion to be just and reasonable.

The NYISO also believes that it might conceivably be just and reasonable to provide for some level of compensation for some portion of dual fuel generators' oil storage and deliverability costs in the future. As the Commission understands, however, the questions surrounding such compensation are complex and it may be, as a number of NYISO stakeholders appear to believe, that no additional payments are warranted. In keeping with the Commission's precedent on Minimum Oil Burn Rule compensation in New York, TCR should raise these issues through the NYISO stakeholder process rather than attempting to re-litigate old disputes.

WHEREFORE, for the foregoing reasons, the New York Independent System Operator, Inc., respectfully requests that the Commission deny the Complaint of TC Ravenwsood, LLC in its entirety.

Respectfully submitted,

/s/ Ted J. Murphy
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Counsel for the
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June 28, 2010

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, D.C. this 28[h] day of June, 2010

/s/ Vanessa A. Colón

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