UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent System Operator, Inc.) **Docket No. ER03-836-007**

MOTION TO TERMINATE PROCEEDINGS OF THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.

In conformance with Rule 212 of the Commission's Rules of Practice and Procedure,[1] the New York Independent System Operator, Inc. ("NYISO") respectfully moves to terminate the above-captioned proceedings. The only outstanding item is a 2005 Commission directive that the NYISO develop and file rules that would allow New York market participants to "self-supply" operating reserves. As is set forth in greater detail below, the NYISO's analyses have confirmed that there is no way to incorporate a self-supply option into the NYISO's market design without incurring costs that would far exceed any possible benefits. Years of experience have also demonstrated that creating such an option is not necessary to promote market efficiency or to mitigate market power in New York. Finally, the NYISO's stakeholders are united in agreement that a self-supply option should not be pursued at this time. Therefore, the NYISO respectfully requests that the Commission terminate these proceedings and not require any further action towards the development of a self-supply option.

[1] 18 C.F.R. § 385.212 (2010).

I. COMMUNICATIONS AND CORRESPONDENCE

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II. BACKGROUND

The issue addressed by this filing originated very soon after the inception of the NYISO. There were competitive issues in the NYISO-administered Eastern[2] non-spinning reserves ("NSR") market in 1999 that led to extensive proceedings before the Commission. Ultimately, the matter resulted in the imposition of a temporary bid cap and other NSR market power mitigation measures.[3] Among those was a directive that the NYISO establish a self-supply option, in large part as a check against possible future competitive problems in the Eastern NSR market.[4] The Commission's last specific pronouncement on the subject of a self-supply option

[2] In this context, the "Western" and "Eastern" portions of New York State are divided by the Central-East Interface.

[3] *New York Independent System Operator, Inc.; Niagara Mohawk Power Corp. v. New York Independent System Operator, Inc.*, 91 FERC ¶ 61,218 (2000).

[4] By July 1, 2003, the Commission had concluded that the NYISO's introduction of market power mitigation improvements for NSR suppliers, and other market enhancements, was significant enough to allow the lifting of the $2.52 NSR Bid cap that had been imposed in 2000. (The Commission remained concerned, however, that the lack of a self-supply option increased the likelihood that customers would be held captive to the NSR suppliers' market power.) *New York Independent System Operator, Inc.*, 104 FERC ¶ 61,002 (2003).

came in a March 2005 Order[5] that directed the NYISO to comply with a previously deferred obligation to submit a plan for establishing a self-supply option.

The NYISO made that compliance filing in late 2005.[6] The NYISO explained that it had resumed work with its stakeholders on the development of a self-supply option. It reported that its stakeholders had unanimously rejected the development of a "physical" self-supply model. Stakeholders agreed with the NYISO that a physical option would be fundamentally incompatible with the NYISO's reserves procurement and cost recovery systems and, consequently, would be extremely complex and time-consuming to implement. Among other things, the NYISO procures sufficient reserves to cover the largest single contingency through its Day-Ahead Market and allocates the total cost of these reserves to all Load-Serving Entities ("LSEs") based on the share of their withdrawals to all withdrawals in the NYCA (a load ratio share basis). LSEs do not have an individually determined NSR purchase obligation. The NYISO centrally procures reserves for the NYCA as a whole and assigns the costs equitably to all LSEs on a load-ratio share basis. The NYISO's stakeholder Management Committee therefore voted that the further exploration of physical self-supply options at that time would be "unproductive and unnecessary."[7]

The NYISO and its stakeholders preferred instead to further explore a financial self-supply option that would be more consistent with the NYISO's systems, software, and markets. Many design issues hinged on better understanding the differences between Western and Eastern reserves prices, and the feasibility of transmission optimization enhancements that would allow Western resources to meet Eastern requirements. The NYISO therefore proposed to take

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[5] *New York Independent System Operator, Inc.*, 110 FERC ¶ 61,287 (2005).

[6] *New York Independent System Operator, Inc.*, Compliance Filing, Docket No. ER03-836-007 (filed October 14, 2005) ("October 14 Filing").

[7] October 14 Filing at 4.

additional time to study these issues. Once the studies were complete the NYISO would either proceed to develop a financial self-supply option or, "[i]f the NYISO and Market Participants were to decide that no further enhancements were needed the NYISO would inform the Commission of this conclusion and seek further guidance . . . ."[8]

The Commission accepted the NYISO's compliance filing without comment in its April 2009 Order.[9]

Later in 2009, the NYISO staff completed an evaluation of East/West price differentials and West-to-East transmission availability.[10] It also finished an analysis of the feasibility, benefits, and costs of optimizing transmission capacity for reserves. Taken together the NYISO's work demonstrated that the economic benefits of implementing a financial self-supply option would be small, approximately $120,000 - $350,000 annually. At the same time, the costs of overhauling the NYISO's market software, settlement processes, and other systems to establish the new transmission optimization process necessary to support a financial self-supply option would be enormous. Resources committed to making transmission optimization improvements would, necessarily, be diverted from competing projects that enjoyed much greater stakeholder support and that are expected to bring much greater benefits.[11]

Consequently, the NYISO staff concluded that although it may be technically feasible to adjust the current reserve allocation from East to West based upon unused West to East transfer capacity in the Day Ahead Market, doing so would yield minimal benefits but require costs that

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[8] October 14 Filing at 5.

[9] *New York Independent System Operator, Inc.*, Letter Order, Docket No. ER03-836-007 (issued April 9, 2009) ("April 2009 Order").

[10] For additional information on the NYISO's analysis, s*ee Self Supply of Reserves,* Presentation for December 16, 2009 NYISO Management Committee meeting, which is attached hereto (Attachment I).

[11] These competing projects include Interregional Transaction Coordination, Congestion Management, Buy Through of Congestion, Disaggregated Virtual Trading, and many others.

could exceed one million dollars to implement. Moreover, taking on such a project would defer enhancements to improve market efficiency that are of higher value to the NYISO's Market Participants such as the NYISO's Broader Regional Markets initiatives.

NYISO staff also concluded that there did not appear to be any need for a new financial self-supply option given that the NYISO's existing rules already give LSEs two mechanisms to hedge against the risk of high reserve prices. Specifically, LSEs may: (i) bid (or contract for a generator to bid) into the reserve market; or (ii) enter into a contract for differences addressing reserve prices with a third party.

The NYISO's stakeholder Management Committee agreed with the NYISO staff's conclusions. It voted unanimously (with abstentions) that the NYISO should make a filing to terminate these proceedings, subject to the NYISO continuing to monitor the reserves market and consider re-opening the question if circumstances ever changed to an extent that made the development of a financial self-supply option worth pursuing.[12]

III. MOTION

In light of the Management Committee's decision, the NYISO respectfully asks that the Commission issue an order terminating these proceedings and relieving the NYISO of any compliance obligations that may remain in the aftermath of the April 2009 Order.

The NYISO's analysis, and the Management Committee vote endorsing it, has resolved the sole remaining issue in these proceedings to the satisfaction of all parties, including those utilities that favored a physical self-supply option a decade ago[13] and the exploration of

[12] See attached Management Committee Motion, *December 16, 2009 Meeting Agenda #07* (Attachment II).

[13] For example both Niagara Mohawk and LIPA were proponents of the self-supply option in 1999 and 2005, respectively, but both now support the Management Committee's decision.

transmission optimization mechanisms in 2005. The Commission has previously terminated proceedings when these conditions exist and should do so here.[14]

The NYISO and its stakeholders are united in the view that neither a physical nor a financial self-supply option is needed in the NYISO-administered markets at this time. There is likewise agreement that the costs of attempting to implement such an option would likely be prohibitive and that pursuit of such an option would require deferral of more pressing projects targeted to produce significantly more market value.[15] The NYISO has monitored NSR market conditions for the twelve months since the Management Committee voted and has detected no changes that warrant revisiting these determinations.

Experience has proven that even a financial self-supply option is not needed to mitigate potential exercises of reserves market power. Notwithstanding the absence of a new financial self-supply option there has been no recurrence of competitive problems in the Eastern NSR markets, as evidenced by years of analysis by the NYISO's independent Market Monitoring Unit.[16] Moreover, although the absence of a physical self-supply option distinguishes the

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[14] *See, e.g., California Independent System Operator Corp., et al.*, 120 FERC ¶ 61,159 at P7 (2007) (terminating proceeding where "there is nothing left to decide in these dockets"); *El Paso Natural Gas Co.*, 20 FERC ¶ 61,436 at 61,887 (1982) (terminating proceedings where no further controversy existed).

[15] For example, the NYISO's Broader Regional Markets ("BRM") initiatives will better coordinate transactions and internal dispatch to lower the costs of managing congestion and improve scheduling between markets. *See New York Independent System Operator, Inc.*, Supplemental Submission of Analysis of the Expected Impact of Buy-Through of Congestion Charges, Docket Nos. ER08-1281-004 and 004 (filed October 14, 2010).

[16] *See* Potomac Economics, *2009 State of the Market Report New York ISO* (September 2010) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/NYISO_2009_Full_Text_Final.pdf>; Potomac Economics, *2008 State of the Market Report New York ISO* (September 2009) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/NYISO_2008_SOM_Final_9-2-09.pdf>; Potomac Economics, *2007 State of the Market Report New York ISO* (August 2008) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/NYISO_2007_SOM_Final.pdf>; Potomac Economics, *2006 State of the Market Report New York ISO* (July 2007) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/2006_NYISO_SOM_Report_Final_7-31.pdf>; Potomac Economics, *2005 State of the Market Report New York ISO* (August 2006) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/2005_NYISO_SOM_Final.pdf >;Potomac Economics, *2004 State of the Market Report New York ISO* (July 2005) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/2004%20SOM%20Report_Final_Full%20Text.pdf >; Potomac Economics, *2003 State of the Market Report New York ISO* at (May 2004) *available at* <

NYISO-administered markets from regions governed by the Commission's *pro forma* Open-Access Transmission Tariff, it is just one of many such distinctions. In the time since the March 2005 Order the Commission has acknowledged and accepted many such ISO/RTO variations in ISO/RTO Order No. 890 compliance proceedings.[17] In this instance, the NYISO market provides alternative hedging features that give its market participants the flexibility that a self-supply option would provide in regions that do not have centralized reserves markets and obligations. Its markets and tariffs therefore provide a level of service consistent with or superior to the *pro forma* OATT model even in the absence of a self-supply option.

IV. CONCLUSION

For the reasons specified above, the New York Independent System Operator, Inc., respectfully requests that the Commission terminate the above-captioned proceedings and excuse the NYISO from any remaining compliance obligations that it may have.

Respectfully submitted,

/s/ Ted J. Murphy
Ted J. Murphy
Counsel for
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cc: Michael A. Bardee, Anna Cochrane, Jeffrey Honeycutt, Daniel Nowak, Gregory Berson, Jignasa Gadani, Michael Mc Laughlin, Rachel Spiker, Connie Caldwell, Lance Hinrichs, Kathleen E. Nieman

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http://www.potomaceconomics.com/uploads/nyiso_reports/2003%20State%20of%20the%20Market%20Report_Final_Full%20Text.pdf>; Potomac Economics, *2002 State of the Market Report New York ISO* at (June 2003) *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/2002%20Annual%20Report_Full%20Text.pdf>; Potomac Economics, *2001 Annual Report on the New York Electricity Markets* at (June 2002), *available at* < http://www.potomaceconomics.com/uploads/nyiso_reports/2001%20annual%20report_final%20full-text.pdf>.

[17]For example, the NYISO OATT does not include *pro forma* Schedules 4 (Energy Imbalance Service) and 9 (Generator Imbalance Service), and does not include Order No. 890 *pro forma* OATT revisions regarding penalties for unreserved transmission use, conditional firm service, or rollover rights. The Commission has found such deviations to be consistent with or superior to the *pro forma* OATT. *See, e.g., New York Independent System Operator, Inc.*, 123 FERC ¶ 61,134 at P 13 (2008) and *New York Independent System Operator, Inc.*, 125 FERC ¶ 61, 274 at P 13 (2008).

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the foregoing document to be served on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, DC, this 22nd day of December, 2010.

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ATTACHMENT I

NEW YORK INDEPENDENT SYSTEM OPERATOR

Self-Supply of Reserves

Shaun Johnson
Manager, Energy Markets Products
New York Independent System Operator

Management Committee
Krey Corporate Center
December 16, 2009

Self Supply of Reserves

- ✓ Background – How we got here
- ✓ Reserve Optimization Concept
- ✓ Cost /Benefit Analysis
- ✓ Conclusion

Draft – for discussion purposes only

Physical Self-Supply

- FERC ordered the NYISO to produce a schedule for providing Market Participants an opportunity to physically procure their own non-synchronous reserves (physical self-supply)
- In October, 2005, the Management Committee voted to move forward by advising the FERC that physical self supply was not suited to the NY financial market model and that the NYISO should, instead, analyze a financial self supply option
  - *FERC accepted the response and directed the NYISO to provide a schedule for developing a financial solution*

Draft – for discussion purposes only

Background

- The NYISO buys all its reserves in the Day-Ahead market
- Half of the ten-minute spinning reserves it procures Day-Ahead needs to be procured from Eastern resources
- The current tariff provides two mechanisms which provide LSEs the ability to hedge against high reserve prices
  - *Bidding (or contracting for a generator to bid) into the reserve market.*
  - *Entering into a contract for reserve price differences with a third party*
- The NYISO included an evaluation of the feasibility, costs and benefits of optimizing transmission capacity for reserves
- Around other priority projects, the NYISO has been designing and carrying out an evaluation of the feasibility, costs and benefits of optimizing transmission capacity for reserves

Draft – for discussion purposes only

Background

- *Analyzing the feasibility, benefits and costs of optimizing transmission capacity for reserves*:
  - Studies of East/west price differentials and west-to-east transmission availability in both the DAM and the RT markets were performed
  - The remainder of this discussion presents estimates of the **actual benefits** likely to be realized by further transmission optimization

Draft – for discussion purposes only

Reserve Optimization Concept

Utilize unused DAM west to east transfer capacity to shift additional eastern reserve to more economic western resources

- **Would require an additional dispatch step to move Eastern Reserve requirements to Western resources when:**
  - The SCUC dispatch solution results in unused west to east transfer capacity ***and*** the eastern 10 minute reserve price exceeds the western price (hereinafter referred to as "active hours")
- **The NYISO has limited its optimization analysis to the DAM, at present:**
  - NYISO purchases all reserves in the DAM
  - Most RT reserve prices are very low (often $0) yielding very limited benefit.
  - RT optimization would at minimum add substantial complexity with its attendant performance impact and financial cost

Draft – for discussion purposes only

Benefit Estimating Method

- *All days in May, June and July 2009 were examined for active hours*
- *50 of the 93 days contained active hours*
- *23 of the 50 identified days were selected as a representative profile*
- *The 23 evaluated days include a total of 184 active hours*
- *All active hours in these candidate days were modified to reflect new reserve and transfer limits. SCUC was re-run for each candidate day and results compared with the initial schedule to determine production cost benefits*

Draft - for Discussion Purposes Only

Cost Benefit Analysis

- The potential economic benefits of pursuing an additional optimization for reserves:
  - *Range from $120,000 to $350,000 annually*
  - *Benefits appear to be limited in two ways:*
    1. Much of the time when east to west capacity is available to support such a transfer, West-east price differentials are minimal obviating the benefit to a transfer. Out of 93 analyzed days only 50 had 1 or more active hours
    2. When the active hours are then re-dispatched with reduced eastern reserve minimums the average actual reserve transfer (east-to-west reserve transfer found to be economic) is only about 23% of the total available to be transferred in that hour

Draft - for Discussion Purposes Only

Cost Considerations

- **While detailed cost estimates have not been compiled, it would be safe to categorize this as a MAJOR initiative**
  - A thumbnail view of potential costs suggests fairly costly impacts of:
    - *SCUC processing and structural changes (data and process)*
    - *Settlements processing and structural changes (data and process)*
    - *General effort to avoid creating additional structural causes for DAM/RT and RTC/RTD price differentials*
    - *Development of rules and processes to govern re-shifting western reserves to eastern resources when this is desirable in real-time operation*
  - In addition to financial costs these efforts will occupy many resources which are already in high demand for other important projects.
    - This initiative would compete with the same resources that are needed for: Interregional Transaction Coordination (all phases), Congestion Management, Buy Through of Congestion, Disaggregated Virtual Trading, Rest of State Reliability Mitigation, and many others

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Conclusion

- **Financial Self Supply (Analysis Results Review)**
  - The difference between Eastern and Western Non-Synchronous Reserves Prices is *de minimus.* That, combined with a more liquid non-synch market now than in 2001, makes it appear that a hedging mechanism is unnecessary for non-synchronous reserves
  - The NYISO has completed the analysis of the ten minute market and makes the following observations and recommendations as directed by the Management Committee
    1. *It appears **technically feasible** to adjust the current reserve allocation from East to West based upon unused west to east transfer capacity in the DAM*
    2. *Pursuing ten minute reserve optimization appears to yield minimal actual economic benefit and the probability of high implementation cost*
    3. *Given the lack of substantive benefit demonstrated by testing the most likely optimization method against recent actual DAM historical results it can be concluded that **no actual need exists for additional hedging mechanisms** beyond the two currently provided by the NYISO tariff*

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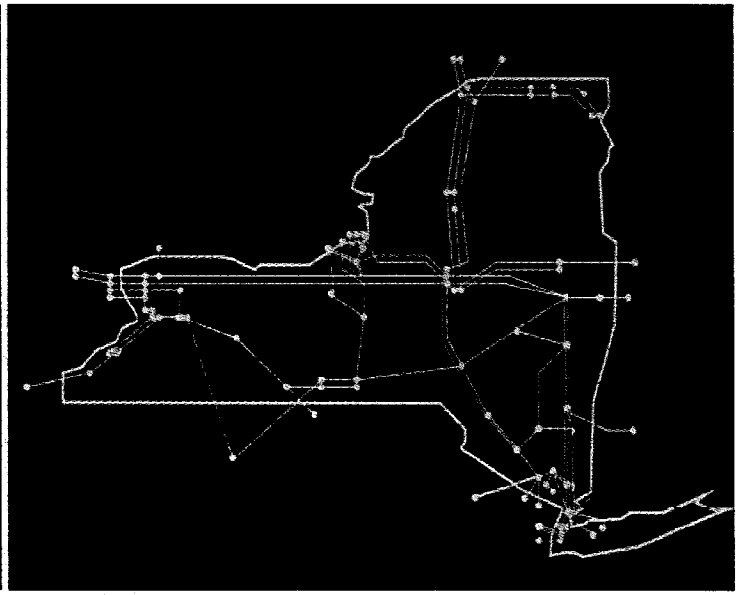
The New York Independent System Operator (NYISO) is a not-for-profit corporation that began operations in 1999. The NYISO operates New York's bulk electricity grid, administers the state's wholesale electricity markets, and conducts comprehensive planning for the state's bulk electricity system.



www.nyiso.com

ATTACHMENT II

Management Committee
December 16, 2009 Meeting
Agenda #07

Motion:

WHEREAS: The NYISO has completed the analysis called for in the October 2005 Management Committee resolution

WHEREAS: It appears technically feasible to pursue ten minute reserve optimization by adjusting the current reserve allocation from East to West based upon unused west to east transfer capacity in the DAM, it appears to yield minimal actual economic benefit and the probability of high implementation cost

WHEREAS: It also appears that the process required to complete design and implementation of the transmission optimization enhancement concept tested would be prohibitively costly given the limited estimated benefit

WHEREAS: The lack of substantive benefit demonstrated by testing the most likely optimization method against recent actual DAM historical results leads to the reasonable conclusion that no actual need exists for additional hedging mechanisms beyond the two currently provided by the NYISO tariff

NOW, THEREFORE, IT IS MOVED THAT the Management Committee:
1. Concurs with the conclusions of the NYISO analysis with respect to current market conditions
2. Approves a filing with the FERC to close this docket (ER03-836-000)
3. Further recommends that the NYISO continue to monitor the reserves market and if there are any significant changes in market conditions, perform an updated cost/benefit analysis and provide it to the Business Issues Committee for consideration.