UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Astoria Generating Company, L.P. and	)	
TC Ravenswood, LLC	)	
	)	
v.	)	**Docket No. EL11-50-___**
	)	
New York Independent System Operator, Inc.	)	

REQUEST FOR REHEARING, AND
REQUEST FOR EXPEDITED CLARIFICATION AND REQUEST FOR SHORTENED NOTICE AND COMMENT PERIOD ON REQUEST FOR CLARIFICATION,
OF THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.

Pursuant to Rules 212 and 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212 and 713, the New York Independent System Operator, Inc. ("NYISO") requests rehearing of several rulings in the September 10, 2012 *Order on Complaint* ("September Order") in this proceeding.[1] Specifically, as discussed in Section II, below, the Commission should reverse its: (i) interpretation of section 23.4.5.7.2 of the NYISO's Market Administration and Control Area Services Tariff ("Services Tariff"), or, at a minimum, modify its holding that the NYISO "violated" that provision; (ii) requirement that the NYISO use an October 2010 "analysis reference date" instead of a reasonable "going forward date" for the Astoria Energy II LLC ("AEII LLC") generation project ("AEII"); (iii) ruling regarding AEII's shared facilities costs; and (iv) holding regarding AEII's capital costs. Correcting these rulings is important to ensuring that the NYISO's buyer-side capacity market mitigation rules do not result in over-mitigation. Misapplying the rules has the potential to harm consumers, the markets, and reliability by deterring investment and impairing competition.

[1] *Astoria Generating Co., et al. v. New York Independent System Operator, Inc.,* 140 FERC ¶ 61,189 (2012) ("September Order").

In addition, the NYISO also requests expedited clarification to confirm that certain rulings from the June 22 Order in Docket No. EL11-42-000 ("June 22 Order") are applicable to the exemption re-determinations that the September Order required for AEII and the Bayonne Energy Center ("BEC"). The NYISO also requests expedited clarification regarding the applicability of the September Order's ruling regarding AEII's cost of capital to determinations made under the current New York City ("In-City") buyer-side market power mitigation measures (the "BSM Rules").[2] The NYISO is working diligently to complete one such analysis, *i.e.,* the exemption redetermination for Hudson Transmission Partners, LLC's merchant transmission project ("HTP Project"), by the Commission's November 13 deadline.[3] Expedited clarification confirming that the NYISO is taking the correct approach on these issues will help to provide market certainty and to avoid future disputes.

I. REQUEST FOR REHEARING

A. The NYISO's Issuance of Exemption Determinations Prior to the End of the Class Year for AEII and BEC Before the Completion of the Class Year Did Not "Violate" the Pre-Amendment Rules

1. The NYISO's Interpretation of Section 23.4.5.7.2 Was Reasonable, Consistent with Commission Precedent, the Principles Underlying Buyer-Side Mitigation, and the Informed Opinion of the Independent Market Monitoring Unit

The September Order concluded that the NYISO's issuance of exemption determinations for AEII and BEC before completion of the Attachment S Class Year process "violated"

[2] The BSM Rules are set forth at section 23.4.5.7 of Attachment H to the NYISO's Services Tariff, and are also referred to as the "Post-Amendment Rules." The September Order, and the determinations that are the subject of that proceeding, were made under the Pre-Amendment Rules, which are also referred to in EL11-50 and ER10-3043 as the "In-City Mitigation Measures" or "In-City BuyerSide Mitigation Measures".

[3] *Notice of Extension of Time*, Docket No. EL11-42-000 (issued September 25, 2012).

section 3.4.5.7.2 of the Pre-Amendment Rules."[4] The Commission should reverse this finding on rehearing because the most reasonable reading of section 23.4.5.7.2 is that it authorized the NYISO to issue the AEII and BEC determinations when it did. If the Commission nevertheless concludes that its interpretation of section 23.4.5.7.2 was more reasonable, it should reverse its ruling that the NYISO's interpretation constituted a "violation" of the tariff.

The September Order recites,[5] but does not substantially address, the NYISO's key arguments demonstrating that section 23.4.5.7.2 gave it discretion to issue final determinations before the completion of the Class Year interconnection cost allocation process. As the NYISO explained, section 23.4.5.7.2 expressly states that developers could request that the NYISO "make" an exemption determination "upon" the execution of an Interconnection Facilities Study Agreement. It appears that the Commission read this language as limited to defining the moment when a developer could first ask for a determination. The Commission apparently read other language as requiring that the actual determination wait until much later. The Commission also seems to have believed that certain other steps had to be taken before the NYISO could make a determination.

Under the Pre-Amendment Rules, section 23.4.5.7.2 was a complex provision. Although it is possible to read the provision as the September Order did, the NYISO has already explained that such a reading would not be reasonable.[6] Similarly, the independent Market Monitoring

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[4] September Order at P 63.

[5] *Id*. at PP 56-59.

[6] *See Answer of the New York Independent System Operator, Inc. to Comments and Protests* at 7-12, Docket No. EL11-50-000 (August 11, 2011) (explaining, that adopting such an interpretation would be "inconsistent with the plain language of the Services Tariff, with the rationale underlying the development of the In-City Buyer-Side Mitigation Measures, with the Commission's August 2, 2011 order in Docket Nos. ER10-3043-002 and -004."); *see also* Public Version - *New York Independent System Operator, Inc. Request for Leave to Submit Answer and Answer to Pleadings Opposing Exemptions and Answer to Motion to Lodge* at 10-18, Docket No. EL11-50-000 (filed October 12, 2011)

Unit for the NYISO ("MMU"), Potomac Economics, Ltd., stated that it never understood section 23.4.5.7.2 to have the meaning ascribed to it by the September Order.[7] Contrary to the September Order, the Pre-Amendment Rules did not provide that "it was only 'as soon as practicable after completion of the relevant Project Cost Allocation or Revised Project Cost Allocation that [the NYISO] could make the exemption determination.'"[8]

Among other things, the September Order overlooks the critical point that the NYISO's interpretation of section 23.4.5.7.2 was consistent with the Commission's February 2, 2011 Order.[9] It similarly ignores a key rationale for modifying the Pre-Amendment Rules and the formulation of the BSM Rules, including specifically the adoption of the "Three Year Rule."[10]

("October 2011 Answer") (arguing that such an interpretation of section 23.4.5.7.2 would be inconsistent with its plain meaning, the August 2 Order in ER10-3043-002 and -004, the overall structure of the buyerside mitigation measures, which focus on determining whether entry decisions were reasonable at the time that they were made, and contrary to the reasonable expectations of AEII and BEC).

[7] *See* October 2011 Answer at *Supplemental Affidavit of Dr. David B. Patton* at n. 12 (stating that "I have also reviewed Complainants' and NRG's argument that the Pre-Amendment Rules did not allow the NYISO to issue an exemption determination before the conclusion of a new project's Class Year. This was never my understanding of the Pre-Amendment Rules and I do not believe that it is a reasonable interpretation. Among other things, that interpretation would have the potential to unnecessarily subject economic entrants to mitigation for extended periods of time solely based on the timing of the NYISO stakeholder Operating Committee decisions and the interconnection process that are beyond an entrant's control") ("Patton Affidavit").

[8] September Order at P 62.

[9] *See New York Independent System Operator, Inc.*, 134 FERC ¶ 61,083 at P 23 (2011) (accepting the NYISO's proposed Three-Year Rule because "it is more transparent, predictable and less prone to manipulation by the project developer" than the Reasonably Anticipated Entry Date Rule) ("February 2011 Order"); *see also New York Independent System Operator, Inc.*, 136 FERC ¶ 61,077 at P 38 (2011) ("August 2011 Order").

[10] *See Answer of the New York Independent System Operator, Inc. to Comments and Protests* at 8-9, Docket No. EL11-50-000 (August 11, 2011) ("August 2011 Answer") (explaining that "a principal objective of the changes to the Pre-Amendment Rules was to more closely align the mitigation exemption and the Class Year cost allocation processes and to establish that exemption determinations would be made in tandem with the latter", *citing, Proposed Enhancements to In-City Buyer-Side Capacity Mitigation Measures, Request for Expedited Commission Action, and Contingent Request for Waiver of Prior Notice Requirement* at 9-10, 13-14, Docket No. ER10-3043-000 (filed September 27, 2010)). Note that the Commission directed that the NYISO utilize the "Reasonably Anticipated Date Rule" instead of the "Three Year Rule" for the HTP Project along with any other Class Year 2008 projects. *See* February 2011 Order at P 25; *see also* August 2011 Order at P 7.

Those changes were meant to address the fact that the Pre-Amendment Rules were not as closely tied to the Class Year cost allocation timetable as the September Order assumes. The Pre-Amendment Rules provided developers with the flexibility to request and receive, and the NYISO with the flexibility to make, final buyer-side mitigation rule determinations before the Class Year process was complete. That flexibility was consistent with the "overall structure of the buyer-side mitigation measures, which focus on determining whether entry decisions were reasonable at the time that they were made."[11]

In particular, the August 2011 Order held that the Pre-Amendment Rules required that exemption determinations be made "prior to when the project accepts its cost allocation and enters the capacity market."[12] The September Order recognizes that it would not be appropriate to require these entrants to wait until after they are in the market to receive a buyer-side mitigation determination. It also states that granting a waiver of section 23.4.5.7.2 was consistent with the August 2011 Order. However, it fails to acknowledge that its own interpretation of section 23.4.5.7.2 is what necessitated a waiver in the first place, and does not ensure that exemption determinations occur pre-entry. The NYISO's interpretation is free from this defect.

The NYISO identified the potentially inconsistent and harmful consequences of the interpretation that was later adopted by the September Order. It informed the Commission that:

[11] *See* October 2011 Answer at 12; *see also* August 2011 Answer at 12 (asserting that "Under the Pre-Amendment Rules the decision on a project was to be made before making significant financial commitments. In AEII's and BEC's case this point was reached well before the Initial Decision Period in their respective Class Year analyses"). Certain provisions of the BSM Rules were designed to establish the specific time frames for issuing determinations. That specificity did not exist in the Pre-Amendment Rules which, as is clear in the record in this proceeding allowed the NYISO to issue determinations before the completion of the Class Year process. *Id*.

[12] August 2011 Order at P 27.

> Imposing an Offer Floor on all new entrants until the completion of their Class Year project cost allocation process would impose an Offer Floor on economic entrants for reasons beyond their control, and give their competitors an undue economic advantage by affecting the price at which the new entrant may offer. It would also subject them to the influence of their competitors that could take actions in an effort to delay the Class Year project cost allocation process.[13]

The NYISO's conclusion that the Pre-Amendment Rules permitted it to make exemption determinations before the end of the Class Year process was consistent with the August 2011 Order and with the nature of the "Unit Exemption test."[14] The analysis is a forward-looking projection that can accommodate the inclusion of reasonably anticipated costs including estimated, but not yet final, Class Year costs.[15]

To the extent that the Commission believed that other language in section 23.4.5.7.2 conflicted with the NYISO's interpretation, it should have sought to resolve the contradiction in a manner that was consistent with the purpose and design of the Pre-Amendment Rules. The September Order, however, interpreted section 23.4.5.7.2 in a way that the Commission itself acknowledges was inconsistent with the "originally-stated intent that the developer would have its exemption determination in hand before it would have to decide whether or not to accept its cost allocation." On rehearing, the Commission should reconsider the NYISO's interpretation of section 23.4.5.7.2. It is reasonable, consistent with both precedent and, as the Commission

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[13] October 2011 Answer at 17-18.

[14] *See* September Order at n. 30.

[15] *See* Public Version - *Confidential Supplemental Answer of the New York Independent System Operator, Inc.*, Docket No. EL11-50-000 at Affidavit of Dr. David Patton at PP 10-11 (filed September 8, 2011) ("September 2011 Answer") (stating that "it is critical that the [mitigation exemption test] MET evaluation consider only the expected costs and future market conditions that existed at the time the investor decided to move forward with the investment" and "[t]he MET evaluations require the NYISO to make reasonable projections of a number of factors that are subject to uncertainty, which is entirely consistent with the assessment that a rational investor must make before determining that a particular project is likely to be economic"); *see also* October 2011 Answer at Patton Affidavit at n. 12 (explaining that the MMU never understood the tariff as restricting the NYISO's ability to issue a determination prior to the conclusion of the Class Year).

acknowledged, with the intent of the provision. The NYISO's interpretation also did not require a tariff waiver to avoid conflicts with section 23.4.5.7.2's intent. Neither the Complainants,[16] nor any other party that challenged the NYISO's and the MMU's interpretation, met their burden under section 206 of the Federal Power Act ("FPA") of demonstrating that it was contrary to section 23.4.5.7.2, or otherwise unjust and unreasonable.

2. Even if FERC Determines that its Interpretation of Section 23.4.5.7.2 Is More Reasonable, It Should Not Have Found that the NYISO "Violated" that Provision by Issuing the Determinations When it did

In the alternative, if the Commission upholds the September Order's interpretation of section 23.4.5.7.2, the Commission still should not have held that the NYISO "violated" its tariff. The very rationale that led the Commission to waive section 23.4.5.7.2 demonstrates that it should not have found a NYISO "violation" in the first place. The Commission waived the provision because it took an "inordinately long time"[17] for the Class Year process to conclude. It also recognized that "[t]o be an effective deterrent to uneconomic entry, the mitigation and offer floor determinations should at least be provided before the unit enters into the capacity market, not after."[18] To find that the NYISO "violated" section 23.4.5.7.2 is to say that the NYISO should have waited for months after AEII entered the market to issue a determination, which is the very outcome that the September Order rejects. In short, it is unreasonable to conclude that there was a tariff violation, when the NYISO's interpretation was reasonable, supported by the

[16] The Complainants are Astoria Generating Company, L.P. and TC Ravenswood, LLC.

[17] The September Order's statement at P 64 that "it took an inordinately long time for NYISO to complete the final project cost allocation for the 2009 and 2010 class years . . ." could be read as implying that the NYISO was somehow at fault. To the extent that the Commission's finding of a tariff "violation" was based in part on such an assumption, the NYISO would note that there were many factors affecting the NYISO's ability to complete these determinations earlier that were beyond its control. These included the status of the on-going proceedings on the NYISO's compliance tariff modifications to implement deliverability in Docket No. ER04-449, *et. al.*

[18] September Order at P 63.

independent entity charged with monitoring its markets (the MMU), and consistent with both Commission precedent and the intent and implementation of the buyer-side market power mitigation rules.

B. The NYISO Correctly Used Information from the Time that "Going Forward" Decisions Were Made in its Exemption Analyses

The September Order held that it was not consistent with the Pre-Amendment Rules for the NYISO to base determinations on a project's "going forward" date.[19] It observed that the use of a going forward date is not expressly referenced in the tariff. It commented that if the Pre-Amendment Rules actually were intended to require that exemption analyses be conducted using information available as of that date then it was a "very significant omission."[20] The Commission also expressed concern that the use of going forward dates was an overly subjective exercise.

It is true that the Pre-Amendment Rules did not specify an "analysis reference date." But Commission precedents and earlier NYISO filings clearly established the principle that the analyses should be conducted using information available as of the time that developers decided to proceed with an investment.[21] The intent of the mitigation measures is to mitigate only conduct where a developer enters the market uneconomically in order to depress capacity prices. Therefore, it is essential to utilize the information the developer would have had available when it decided to enter.[22] If market conditions subsequently change, causing the investment to be

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[19] *Id*. at P 81.

[20] *Id*.

[21] *See* August 2011 Order at P 38 and August 2011 Answer at 10-11 (arguing that the determination should be made on a forward looking basis).

[22] October 2011 Answer at Patton Affidavit P 17 (stating that "the NYISO had to establish an initial decision point corresponding to when the developers made the decision to proceed with the investment so that it could utilize the market information from that timeframe to evaluate whether the developer was knowingly entering uneconomically").

more or less economic, that should not change the interpretation of the developer's conduct or the determination regarding whether mitigation is warranted.

The NYISO previously argued at length, with the MMU's support,[23] that July 2008 was a reasonable "analysis reference date" for AEII under the Pre-Amendment Rules. AEII LLC had taken many steps by that time which demonstrated that it was proceeding with its project. By July 2008, AEII LLC had signed a contract with the New York Power Authority (and would have incurred significant costs for violating it), "ordered major pieces of equipment such as turbines and heat recovery steam generators, and began to incur significant engineering expenses."[24] The selection of the July 2008 date should be considered both reasonable and fully supported by the record.

The September Order noted, consistent with the position taken by the NYISO's expert,[25] that projects can have multiple going forward dates. However, the Commission did not engage those arguments. The September Order's ruling that the NYISO must use an October 2010 analysis reference date for AEII is wholly inconsistent with the principle of using information from the time that an investment decision was made. The September Order states that the Default exemption test is not just made in "contemplation of" a project's construction but must also consider the timing of market entry.[26] But the Commission's analysis reference date

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[23] *See* October 2011 Answer at Patton Affidavit P 18 (re-emphasizing argument from earlier Patton Affidavit that "it was appropriate for the NYISO to use July 2008 as the initial decision point when performing the price projections for AEII's MET because . . ." that was when AEII "committed contractually to the project by entering into the PPA with NYPA" and when "AEII began to make significant financial commitments to the project that would not be sensible unless it had already decided to move forward").

[24] October 2011 Answer at 22-23.

[25] *See* October 2011 Answer at 22 (stating that "[t]he NYISO is not contending that there is only one possible go-forward investment decision date that might have reasonably been chosen", *citing* September 2011 Answer at Affidavit of Christopher Ungate at P 18).

[26] *See* September Order at P 81.

requires the NYISO to use information from a time when the construction of AEII was substantially complete.[27] Using such a date is not compatible with what is supposed to be a forward-looking analysis tied to the timing of investment decisions. Neither the Complainants, nor the other parties that challenged the use of the July 2008 date made any showing that would justify, nor does the record support, an October 2010 analysis reference date for AEII.

Even if the Commission disagreed that the July 2008 date was reasonable and fully supported by the record, it ignored potential alternate reference dates that are far more reasonable than October 2010. For example, AEII closed on financing in July 2009.[28] The September Order forces an absolute and complete separation between all of the energy and capacity market assumptions used in the buyer-side mitigation analysis from the information that was actually available at the time that AEII LLC's investment decision was made.

The NYISO agrees that the use of a "going forward" date requires a significant degree of judgment which has the potential to lead to disputes and to raise other issues. That is why the NYISO proposed, and the Commission accepted, tariff revisions to incorporate clearer and more objective requirements in the BSM Rules.[29] This does not mean, however, that the use of a "going forward" date was impermissible under the Pre-Amendment Rules.

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[27] *See Complainants' Answer to Supplemental Answer of the New York Independent System Operator, Inc.* at 2, Docket No. EL11-50-000 (filed September 23, 2011) ("Complainants EL11-50 Answer").

[28] October 2011 Answer at Affidavit of Christopher Ungate at P 18 (stating that "AEII achieved financial close on July 2, 2009"); *see also* Complainants EL11-50 Answer at Affidavit of Mark D. Younger at P 69.

[29] *See* August 2011 Order at P 38.

C. The NYISO Properly Excluded Shared Facilities Costs from the AEII Determination Notwithstanding the Reference to "Embedded Costs" in the Definition of Unit Net CONE

The September Order held that the NYISO should not have excluded from the Unit Net CONE value used in the AEII exemption analysis, a payment that AEII LLC made to compensate an affiliate, Astoria Energy LLC ("Astoria I"), for AEII's use of shared facilities.[30] The Commission focused on the fact that the Pre-Amendment Rules defined Unit Net CONE as the "localized levelized embedded costs of a specified Installed Capacity supplier, including interconnection costs..... net of likely projected annual Energy and Ancillary Services revenues."[31] According to the September Order, the "common meaning of the term 'embedded costs' includes all costs that have been incurred in the past," without reference to factors that economists look to when evaluating investment decisions, such as "whether or not the associated assets have any opportunity costs or market values."[32]

The September Order cites three secondary sources that recite traditional utility definitions of "embedded costs" in the context of accounting for historic costs. Even within the cited sources, however, there is no true "common meaning." The first definition in the September Order describes embedded costs as including all costs that "have already been incurred and cannot be varied."[33] The second definition of embedded costs includes the "total costs of all assets and ongoing charges incurred in providing and maintaining a supply of energy."[34] An energy industry textbook provides more clarity on the "embedded cost" aspect of the Unit Net CONE definition. The *Power Distribution Planning Reference Book* states that

[30] September Order at P 121.

[31] *Id. citing* section 23.2.1 of the Services Tariff.

[32] September Order at P 121.

[33] September Order at n. 153.

[34] *Id*.

"embedded costs" may vary "[d]epending on the application" and may "include all or portions of the initial fixed cost and all or parts of the variable costs."[35] This definition and those cited by the Commission indicate that the term "embedded costs" sometimes includes and sometimes excludes a variety of costs. The September Order focused on one aspect of the definition to the exclusion of other potential applications that more reasonably relate to the use of "embedded costs" in a buyer-side mitigation analysis.

In any case, even if "embedded costs" has a "common meaning" in the traditional costof-service ratemaking context, that does not dictate that the same meaning must apply in fundamentally different settings, in particular, a competitive energy market. Using a regulatory utility "accountant's" version of the term may make sense for backward-looking analyses to set traditional cost-based rates. It does not make sense in the context of a prospective analysis focused on evaluating the economic decisions of private investors. Cost measures employed by economists are highly relevant to Unit Net CONE determinations under both the Pre-Amendment Rules and the current BSM Rules because they are prospective evaluations of investment decisions in a competitive market. The costs defined by economists include opportunity costs and other non-accounting costs because it is these costs that determine the incentive of a business to make an investment.

Thus, despite the September Order's suggestion that the term "embedded costs" is clearly defined, the reality is that its meaning is ambiguous when it is used outside the context of traditional cost-of-service ratemaking and in the context of buyer-side mitigation rules. Commission precedent holds that a tariff is ambiguous where it is "susceptible to different constructions and interpretations" and where such ambiguity is found it "must be resolved by

[35] WILLIS, H. LEE, POWER DISTRIBUTION PLANNING REFERENCE BOOK 138-139 (2nd Ed. 2004).

reference to the … tariff as a whole … [and] extrinsic evidence may be considered to prove a meaning to which the tariff language is reasonably susceptible."[36] Further, the principle of construction known as *noscitur a sociis* ("it is known from its associates") provides that the meaning of an unclear word or phrase should be determined by the words immediately surrounding it.[37] Therefore, the fundamental purpose of the buyer-side mitigation rules - *i.e.,* to determine whether an investment is uneconomic - cannot be ignored. Ignoring economic costs in favor of accounting costs will lead to inaccurate exemption test results and unreasonable applications of buyer-side mitigation.

There is no extrinsic evidence suggesting that the traditional utility definition of embedded costs was meant to be applied in the market-based analyses that are part of buyer-side mitigation determinations. There is no indication of such an intent in the various NYISO filings establishing the Pre-Amendment Rules. Dr. David B Patton, the President of the MMU, who proposed the original buyer-side mitigation rules that evolved into the Pre-Amendment Rules,[38] strongly supported the exclusion of the shared facilities transfer payments in the AEII

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[36] *See Duquesne Light Co.,* 122 FERC ¶ 61,039, at P 85, *clarified*, 123 FERC ¶ 61,060 (2008) (interpreting PJM's Reliability Pricing Model ("RPM") tariff procedures "based on the intent and structure of the RPM"); *see also Consolidated Gas Transmission Corp. v. F.E.R.C.*, 771 F.2d 1536, 1545 (D.C. Cir., Sep 17, 1985) (finding when a tariff provision is ambiguous "[t]he purposes for which a tariff was imposed should be considered when interpreting the tariff, for 'to decide the question of the scope of [a] tariff without consideration of the factors and purposes underlying the terminology employed would make the process of adjudication little more than an exercise in semantics'" *(citing United States v. Western Pacific Railroad*, 352 U.S. 59, 67(1956)).

[37] *See Black's Law Dictionary* 1349 (9th ed. 2009); s*ee e.g., Union Power Partners, L.P.,* 123 FERC ¶ 61,191, at P 21 (2008) (applying the doctrine).

[38] October 2011 Answer at Patton Affidavit at P 5 (stating that "I have been and continue to be one of the principal proponents of BSM measures in the NYISO's market and in other organized markets. The current BSM provisions are largely based on the initial proposal I made in 2007 to address uneconomic entry", *citing Compliance Filing of the New York Independent System Operator, Inc. Regarding the New York City ICAP Market Structure*, Attachment 1, Affidavit of David B. Patton filed in Docket No. EL07-39-000 (October 4, 2007)).

determination.[39] Dr. Patton has also authorized the NYISO to state his opinion that the September Order's holding on this issue is unreasonable and may lead to erroneous mitigation determinations. Even those parties that opposed the NYISO's exclusion of shared facilities costs in the AEII analysis did not argue that those costs must be included on the grounds that the tariff incorporated the traditional ratemaking definition of "embedded costs."[40]

It is the NYISO's understanding that no other Independent System Operator ("ISO") or Regional Transmission Organization ("RTO") has adopted (or proposed) to incorporate the traditional utility ratemaking definition of "embedded" costs into its own buyer-side capacity market mitigation analyses. The PJM Interconnection's ("PJM's") Minimum Offer Price Rule ("MOPR") allows sell offers below the normal minimum offer level when a supplier can demonstrate that its "competitive, cost-based, fixed, net cost of new entry" falls under it. To qualify for this exception to the MOPR, the supplier must provide documentation to support the "fixed development, construction, operation, and maintenance costs of the planned generation resource, as well as estimates of offsetting net revenues." Notably, "[s]uch documentation also shall identify and support any sunk costs that the Capacity Market Seller has reflected as a reduction to its Sell Offer."[41]

Although there are a number of important distinctions between the NYISO and PJM rules, neither is intended to unnecessarily mitigate entrants whose decision to enter was economically reasonable at the time that it was made. There does not appear to be any valid economic reason why legitimate sunk costs should be excluded from the buyer-side mitigation

[39] *See* October 2011 Answer at Patton Affidavit at section IV (including at PP 30-40).

[40] It therefore cannot be said that Complainants, or any other party that objected to the exclusion of AEII's shared facilities costs, met their burden of demonstrating that the exclusion of shared facilities costs violated the tariff or was otherwise unjust and unreasonable under section 206 of the FPA.

[41] *See PJM Interconnection LLC's Open Access Transmission Tariff,* Attachment DD at Section 5.14(h)(5)(ii) (emphasis added).

analysis in PJM but automatically included by the NYISO in its analysis. The Commission should not interpret the NYISO's buyer-side mitigation rules to require the NYISO to assume that reasonable investors would consider sunk costs in their investment decisions when economic theory is clear that they would not.

Consequently, on rehearing, the Commission should avoid an overly formalistic interpretation of the NYISO's tariff. Instead, the Commission should hold that the NYISO definition of Unit Net CONE does not incorporate a traditional utility ratemaking concept of embedded costs to the extent that it is alien to the purpose and intent of the buyer-side mitigation rules. It should also confirm that the NYISO's exclusion of shared facilities costs from the AEII exemption analysis was appropriate for the reasons specified above and in the NYISO's earlier pleadings in this proceeding.

D. The NYISO Should Not Be Required to Use the ICAP Demand Curve Proxy Unit's Capital Costs in the AEII Exemption Analysis Because Even if AEII Was Selected Through a "Discriminatory" RFP Process its Actual Capital Costs Were Not Unreasonable

The September Order erred when it found that the NYISO was required to apply the rationale underlying its determination in a November 2011 order on PJM's Minimum Offer Price Rule[42] ("PJM Rationale") when determining the cost of capital for AEII. The November 2011 MOPR Order held that "PJM and its Internal Market Monitor must exercise discretion in assessing whether 'competitive cost advantages' are legitimate and determine whether there are 'irregular or anomalous' cost advantages or sources of revenue that 'do not reflect arm's-length transactions, or that are not in the ordinary course of [business]."[43] The September Order translated the PJM Rationale to the context of the New York capacity markets. It found that the

[42] *PJM Power Providers Group v PJM Interconnection, L.L.C.*, 137 FERC ¶ 61,145 (2011) ("November 2011 MOPR Order").

[43] September Order at P 134, *citing* November 2011 MOPR Order at P 249.

NYISO should use the ICAP Demand Curve proxy unit's cost of capital on the theory that AEII's financing costs were reduced by virtue of its being selected through a "discriminatory" RFP process that gave it an "irregular or anomalous" advantage.[44]

This directive should be reversed on rehearing. It was unreasonable to not consider potential differences between the facts in the PJM case and those here.

The PJM Rationale is based on a different approach to buyer-side mitigation. It was developed in response to compliance tariff language proposed by PJM that permitted entrants that failed its buyer side market power screens to seek individual exceptions from mitigation. It gave PJM and its Independent Market Monitor ("IMM") discretion to evaluate the "cost justifications submitted by resources whose sell offers have been mitigated."[45] The November 2011 MOPR Order rejected a request that would have taken away this discretion by requiring that proxy capital costs be used in all of the case-by-case analyses. By contrast, the September Order would deprive the NYISO of its ability to exercise discretion by prescribing the use of the ICAP Demand Curve proxy unit's capital costs even when there is good cause to believe that actual costs would be more reasonable.

This proceeding is an example of such a situation. Even if the RFP process that selected the AEII project truly was "discriminatory," it does not mean that AEII's capital costs were necessarily unreasonable or inconsistent with competitive markets. The November 2011 Order recognized that an absolute requirement to use proxy costs "would not allow PJM to recognize the lower financing costs of sellers that are especially creditworthy or that have negotiated contracts that have enabled them to secure favorable credit terms."[46] The September Order

[44] *Id*. at PP 134-135.

[45] November 2011 MOPR Order at P 212.

[46] *Id*. at P 249.

ignored the evidence in the record showing that NYISO and its MMU, reasonably determined that it was appropriate to use AEII's actual cost of capital because it was consistent with what was available to other developers that had a PPA with a creditworthy counterparty.[47] As further explained by the MMU, using AEII's cost of capital was proper because "[s]uch PPAs and other long-term contracts are not uncommon" and "it is rational for such developers to enter into long-term contracts, which also improves the developer's access to capital by lowering its default risk."[48] The September Order also did not refute the MMU's assertions that the existence of such a PPA is neither a subsidy nor evidence that a project is uneconomic.[49] Neither the Complainants, nor any other party that challenged the NYISO's and the MMU's assessment of AEII's capital costs, met their burden under section 206 of the Federal Power Act ("FPA") of demonstrating that it was contrary to section 23.4.5.7.2, or otherwise unjust and unreasonable. Thus, the Commission should reverse on rehearing the September Order's requirement that the NYISO use the proxy unit's cost of capital for AEII.

Finally, the September Order's application of the PJM Rationale is problematic to the extent that it will require the NYISO to discern the intent of New York State entities that issue RFPs for energy or capacity resources. It is logically inconsistent for the September Order to simultaneously specify that the NYISO should not engage in "overly subjective" determinations and then instruct it to make them.[50] This is especially true in light of Commission precedents

[47] September 2011 Answer at Patton Affidavit at PP 44-47.

[48] *Id*. at P 44.

[49] *Id*. at P 45.

[50] September Order at P 84 (finding that the NYISO's interpretation that the tariff required the use of a project's going-forward date was unreasonable because that would require "an imprecise and subjective determination, which tends to cause contentious debate").

confirming that ISOs/RTOs should not second guess the legitimacy of state policy determinations or state interests.[51]

II. REQUEST FOR EXPEDITED CLARIFICATION

The proceedings in Docket No. EL11-50-000 were limited to the application of the Pre-Amendment Rules.[52] Similarly, the proceedings in Docket No. EL11-42-000 were confined to the application of the current version of the BSM Rules.[53] There are certain rulings in the June 22 Order and the September Order, however, that would logically seem to be "universally" applicable because there is no apparent reason to restrict them to the context of the Pre-Amendment Rules or the BSM Rules. For example, as is explained below, the NYISO does not see any difference between the Pre-Amendment Rules and the BSM Rules that would make the June 22 Order's directives regarding inflation adjustments inapplicable to redeterminations under the Pre-Amendment Rules.

The NYISO believes that it should follow this kind of broadly applicable Commission guidance in all of its buyer-side mitigation determinations (and redeterminations) regardless of whether they are conducted under the Pre-Amendment or the BSM Rules. It is foreseeable, however, that some parties may contend that a ruling made in the context of the Pre-Amendment Rules should not apply to a determination under the BSM Rules (or vice versa). The NYISO is therefore seeking confirmation that it is acting consistent with the Commission's intent when it

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[51] *See e.g.*, *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000-A, 139 FERC ¶ 61,132 at P 318 (2012) (stating that "we are not placing public utility transmission providers in the position of being policymakers or allowing them to substitute their public policy judgments in the place of legislators and regulators") and PP 327-328 (clarifying that "it is not the transmission providers' function to decide on the merits of … federal or state requirements…."); *New York State Independent System Operator, Inc.*, 131 FERC ¶ 61,170 at P 137 (2010) (stating that "it is not [the Commission's] intent to interfere with state programs that further specific legitimate policy goals").

[52] September Order at P 3.

[53] *New York Independent System Operator, Inc.*, 139 FERC ¶ 61,244 at P 8 (2012).

applies: (i) one ruling from the September Order to determinations under the BSM Rules; and (ii) several rulings from the June 22 Order to the redeterminations required by the September Order.

The NYISO is in the process of performing buyer-side mitigation analyses consistent with the foregoing assumptions. This includes its redetermination for the HTP Project under the BSM Rules, which is to be complete by November 13. The issuance of an order clarifying that the NYISO's assumptions are correct before the HTP Project redetermination is issued would help to promote confidence in the validity of the redetermination and thus market certainty. Clarifying that the NYISO's approach to these issues is correct now could also help to avoid (or reduce the scope of) later litigation. The NYISO therefore requests that the Commission act expeditiously on these requests for clarification and take whatever procedural steps it deems appropriate, *e.g.,* establishing a shortened period for answers or protests, to permit expedited action consistent with due process. Because the points that the NYISO is asking the Commission to confirm are clearly defined and relatively narrow in scope they should lend themselves to expedited treatment.

A. The Commission Should Confirm that, if the NYISO is Required to Apply the PJM Rationale to AEII's Cost of Capital, it Should Also Apply to Determinations Under the BSM Rules When the Facts Warrant

As is discussed above, the September Order held that the NYISO's use of AEII's actual cost of capital was not consistent with the rationale of the November 2011 MOPR Order. It found that the NYPA "contracting process that awarded the power purchase agreement to Astoria II was discriminatory - because the process was limited to new resources - and thus, the resulting lower financing costs do not reflect competitive market processes."[54] Accordingly, the

[54] September Order at P 135.

Commission believed that the financing costs available to AEII as a result of its power purchase agreement provided "irregular or anomalous" cost advantages.[55] It therefore required that the NYISO "use the proxy reference unit's cost of capital as of the date the analysis for [AEII] was performed in 2010."[56]

Because this ruling was made in Docket No. EL11-50-000, its scope is formally limited to the Pre-Amendment Rules. The NYISO does not believe, however, that to the extent that the PJM Rationale is to be applied in New York,[57] that there would be any justification for not applying the same principle to determinations, and redeterminations,[58] under the current BSM Rules. Thus, to the extent that other power purchase agreements have been, or may in the future be, awarded to projects under RFP processes that are "limited to new resources" the NYISO would use an appropriate proxy cost of capital in its analysis. The NYISO requests that the Commission grant expedited clarification to confirm that this interpretation is correct.

B. The Commission Should Confirm that the June 22 Order's Holdings Regarding Escalation Factors and Inflation Adjustments Are Applicable to the Redeterminations Required Under the September Order

The June 22 Order made a number of rulings and offered extensive guidance on the use of inflation and escalation factors in the various calculations under the current BSM Rules. The NYISO believes that the adjustments using escalation factors and inflation rates dictated by the

[55] *See id*.

[56] *Id*.

[57] *See* Section I.D above.

[58] As explained in the NYISO's request for clarification and rehearing in EL11-42, HTP is the only project as of that time for which the NYISO is required to make a redetermination. *See Request for Expedited Clarification, and Alternative Request for Rehearing, of the New York Independent System Operator, Inc.* at 4-7, Docket No. EL11-42-002 (filed July 23, 2012) ("EL11-42 Request for Clarification or Rehearing"); *see also Compliance Filing* at n. 8, Docket No. ER12-2414-000 (filed August 6, 2012) ("ER12-2414 Compliance Filing"). However, if the Commission does not rule expeditiously before the next set of determinations must be made, there may be a need to make additional redeterminations.

June 22 Order should also be applied if a redetermination for AEII and BEC required by the September Order results in an Offer Floor.

The June 22 Order's rationale for the escalation factor and inflation rate to be used was that comparing "the Unit net CONE amount stated in one year's dollars to demand curve prices stated in dollars of three to six years in the future … [made] it necessary to restate, *i.e.*, inflate the Unit net CONE value in order to render a valid comparison in constant 'real' dollar terms."[59] The Pre-Amendment Rules' Unit exemption test is in all relevant respects the same as in the BSM Rules. It is therefore reasonable that the NYISO apply the escalation factor and inflation rate adjustments to the redeterminations for AEII and BEC under the Pre-Amendment Rules. Further, the NYISO believes that those adjustments should be calculated in the same manner specified in its pending Request for Clarification of the June 22 Order and its proposed tariff revisions filed in compliance with that order.[60]

It is similarly reasonable to adjust Offer Floors for inflation after an entrant is in the market, regardless of whether that Offer Floor was set using the BSM Rules or the Pre-Amendment Rules. The June 22 Order held that the annual adjustment to the Offer Floor is necessary because "it maintains the originally determined offer floor in 'real' terms while at the same time making such values comparable to the prices in the year in which the mitigation occurs. Without an inflation adjustment, a static offer floor would understate Unit net CONE over time."[61] Offer Floors set under the Pre-Amendment rules would also remain static if not adjusted for inflation, thus it is appropriate to adjust them consistent with the June 22 Order's

[59] June 22 Order at P 60.

[60] *See* EL11-42 Request for Clarification or Rehearing at 4-7; *see also* ER12-2414 Compliance Filing at 5-9.

[61] June 22 Order at P 73.

direction.[62] As explained in its Request for Clarification of the June 22 Order, the NYISO would apply inflation to the Offer Floor for these redeterminations: (1) based on annual net CONE rather than Unit Net CONE;[63] and (2) inflated or deflated as applicable based on each specific project's entry date.[64]

Therefore, the Commission should clarify that the NYISO is correct to apply the escalation factor and inflation rate for the AEII and BEC redeterminations, as directed in the June 22 Order's holdings, and as described by the NYISO in its Request for Clarification of the June 22 Order.

III. SPECIFICATIONS OF ERRORS AND STATEMENT OF ISSUES

In accordance with Rule 713(c), 18 C.F.R. § 385.713(c), the NYISO submits the following specifications of error and statement of the issues on which it seeks rehearing of the September Order:

- The September Order's finding that the issuance of exemption determinations for AEII and BEC before completion of the Attachment S Class Year process "violated" section 23.4.5.7.2 of the Pre-Amendment Rules does not reflect reasoned decision-making, because the NYISO's interpretation of that section was reasonable, consistent with Commission precedent, the principles underlying buyer-side mitigation and the view of the NYISO's MMU. *See New York Independent System Operator, Inc.*, 134 FERC ¶ 61,083 (2011); *New York Independent System Operator, Inc.*, 136 FERC ¶ 61,077 (2011).

[62] *Id*.

[63] *Id*. at 8 (explaining that the Commission should grant clarification that in applying the inflation adjustment to the Offer Floor, the NYISO should adjust the Default Offer Floor (which is an annual number) for inflation rather than Unit Net CONE (which is a three-year average of annual net CONE values over the Mitigation Study Period)).

[64] *Id*. at 9 (explaining that the Commission should grant clarification that "if an entrant initially offers UCAP after the first year of the Mitigation Study Period, the NYISO's understanding of the June 22 Order is that it should adjust the Offer Floor for inflation in the Capability Year that the entrant first offers UCAP [such that where] an entrant initially offers UCAP prior to the first year of the Mitigation Study Period, the NYISO believes that it is required to adjust for early entry and deflate the Offer Floor for inflation").

- The September Order's finding that the NYISO should not have used information from the time of a project's going forward decision in its exemption analyses does not reflect reasoned decision-making because Commission precedent and earlier NYISO filings clearly established that the analysis reference date should be tied to the timing of the investment decisions and the date that the NYISO selected was reasonable. *See New York Independent System Operator, Inc.*, 136 FERC ¶ 61,077 (2011).

- The September Order's finding that the NYISO should have used an analysis reference date of October 2010 instead of July 2008 (or an alternate reference date based on the record) for AEII does not reflect reasoned-decision making because that date is wholly inconsistent with the principle of using information from the time that an investment decision is made and would require the NYISO to conduct a forward-looking analysis for AEII using information from a time when its construction was substantially complete.

- The September Order's finding that the NYISO should not have excluded the transfer payment from AEII LLC to AEII from the Unit Net CONE value used in its exemption analysis does not reflect reasoned decision-making because: (1) the definition of the term "embedded costs" can vary depending on its application to a particular context; (2) even if the term has a common meaning in the cost-of service ratemaking context, it would be unreasonable for the Commission to formalistically apply that definition when to the extent that it is alien to the purpose and intent of the buyer-side mitigation rules and the meaning ascribed by the Commission was never meant to be incorporated in or applied to the tariff; (3) the Commission disregarded principles of tariff interpretation that it has applied in other cases and overlooked extrinsic evidence indicating that the utility cost of service ratemaking version of the definition should not be applied in the context of this proceeding; and (4) there does not appear to be any valid economic reason why the Commission would allow legitimate sunk costs to be excluded from PJM's buyer-side mitigation analyses while requiring the NYISO to include them. *See Duquesne Light Co.,* 122 FERC ¶ 61,039, at P 85, *clarified*, 123 FERC ¶ 61,060 (2008); *Consolidated Gas Transmission Corp. v. F.E.R.C.*, 771 F.2d 1536, 1545 (D.C. Cir., Sep. 17, 1985).

- The September Order's finding that the NYISO must apply the rationale from the Commission's November 2011 order on PJM's Minimum Offer Price Rule to the cost of capital for AEII, does not reflect reasoned decision-making because: (1) the Commission failed to consider the differences between the facts in PJM and in this proceeding; (2) there is good cause, and record evidence, supporting the NYISO's determination that AEII's actual capital costs were reasonable; and (3) the September Order's directive would require the NYISO to discern the intent of New York State entities that issue RFPs for energy and capacity resources in contravention of Commission precedents finding that ISOs/RTOs should not second guess the legitimacy of state policy determinations or state interests. *See e.g.*, *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000-A, 139 FERC ¶ 61,132 (2012); *New York State Independent System Operator, Inc.*, 131 FERC ¶ 61,170 (2010).

IV. CONCLUSION

WHEREFORE, for the foregoing reasons, the New York Independent System Operator, Inc., respectfully requests that the Commission grant clarification, or in the alternative rehearing, of the rulings and statements in the June 22 Order that are described above.

Respectfully submitted,

/s/ Ted J. Murphy
Counsel for the
New York Independent System Operator, Inc.

Date: October 10, 2012

cc: Travis Allen
Michael A. Bardee
Gregory Berson
Anna Cochrane
Jignasa Gadani
Morris Margolis
Michael McLaughlin
Joseph McClelland
Daniel Nowak

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the foregoing document to be served upon each person designated on the official service list compiled by the Secretary in this proceeding in accordance with the requirements of Rule 2010 of the Commission Rules of Practice and Procedure, 18 C.F.R. § 385.2010 (2011).

Dated at Washington, D.C. this 10th day of October, 2012.

/s/ Catherine Karimi

Catherine Karimi
Hunton & Williams LLP
2200 Pennsylvania Ave., NW
Washington, DC 20037
Tel: (202) 955-1500
Fax: (202) 778-2201
E-mail: ckarimi@hunton.com