STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 06-M-1017 – Proceeding On Motion Of The Commission As To The Policies, Practices And Procedures For Utility Commodity Supply Service To Residential And Small Commercial and Industrial Customers.

COMMENTS OF CONSOLIDATED EDISON SOLUTIONS, INC. AND CONSOLIDATED EDISION ENERGY, INC.

I. BACKGROUND

As part of its April 19, 2007 *Order Requiring Development of Utility-Specific Guidelines for Electric Commodity Supply Portfolios and Instituting a Phase II to Address Longer Term Issues* ("April 19, 2007 Order") in the above captioned case, the Public Service Commission ("Commission") initiated an inquiry into longer term purchases of commodity supply and related planning and acquisition practices and invited interested parties to address a series of questions relating to various aspects of the electric infrastructure planning and analysis process. In response to the specific questions raised in the April 19, 2007 Order, Consolidated Edison Solutions, Inc. ("CES") and Consolidated Edison Energy, Inc. ("CEE") submit the following comments:

II. PRELIMINARY STATEMENT

The April 19, 2007 Order requests input on a series of policy initiatives that have the potential to impact the market structure and corresponding investment behavior within New York. By proposing the use of a centralized regulatory planning structure to meet future resource needs, the Commission could be jeopardizing the ability of market solutions to satisfy the required resource needs and potentially usurp the existing reliability backstop mechanism

built into the Reliability Needs Assessment ("RNA") process conducted annually by New York Independent System Operator ("NYISO"). Therefore, CEE and CES urge the Commission to proceed cautiously and only consider the use of long term contracts: (i) to pursue clearly defined public policy objectives like the Clean Coal Initiative or (ii) solely as a measure of last resort when there is compelling evidence that market solutions are not likely to be implemented. In either instance, the implementation of long-term contracts should be done in a competitively neutral manner with any difference between the prevailing market price and the costs associated with the contract collected from or credited to all customers either through a mechanism like the current systems benefit charge or through a non-bypassable surcharge / credit on the utilities' delivery charge. Because of the long-term nature of such contracts, there are likely to be both sustained periods when the cost of the contract is above the prevailing market price AND sustained periods when the contract cost is below the prevailing market price. In the absence of a competitively neutral mechanism to collect and credit back the differences to all ratepayers, the utility's costs would diverge from the prevailing market price and could create artificial boom-bust cycles for competitive retail ESCOs.

III. RESPONSE TO QUESTIONS POSED BY THE COMMISSION

1. Should there be a statewide integrated resource planning process to examine long term electricity resource needs? [To what extent or in what manner would a statewide integrated resource planning process build on or parallel existing reliability planning processes?] What time frame should be examined in such a process and what issues should be considered? What is the role of the utilities and other interested parties in the process? How should the process differ from any previous integrated resource planning processes? What processes should be adopted, if any, to ensure that resources portfolios at the utility and statewide level satisfy overall planning objectives and public policy considerations? How should immediate concerns and long range considerations be addressed?

Response to Question No.1:

CEE and CES currently participate with other market participants in the NYISO's RNA process which examines whether long-term reliability needs are being addressed and can result in the NYISO directing appropriate transmission owners to invest in new resources (either transmission, generation or demand response) to meet reliability needs that are not addressed by market forces. In addition, in response to Order 890 from the Federal Energy Regulatory Commission ("FERC"), the NYISO is working on a revision to its transmission planning process that will add additional transparency into the transmission planning process and include reliability and economic considerations. CEE and CES recommend that the Commission first consider whether these NYISO processes provide a sufficient examination of long-term resource needs. To the extent that the Commission identifies gaps, CEE and CES suggest that the Commission Staff work with the NYISO and its stakeholders to amend either the RNA or the transmission planning process to eliminate those gaps. Alternatively, the Commission could develop a supplemental process that leverages and builds on the ongoing NYISO efforts. If a supplemental effort is pursued, CEE and CES would recommend that the overall process be updated periodically so that recommendations and/or study conclusions can be validated and/or updated as market conditions and long-term forecast assumptions (that are inherently hard to predict) change.

2. Should major regulated electric utilities be required or encouraged to enter into long-term contracts, with existing generators, proposed generators, and other entities, that facilitate the construction of new generation, the development of additional energy efficiency, the development of additional renewable generation resources, the re-powering of existing generation, or the relief of transmission congestion? Should such

contracts be entered into for the purposes of improving fuel diversity, mitigating market power, or furthering environmental policies?

Response to Question No. 2:

CEE and CES are concerned about the use of long-term contracts because of the potential for: (i) adverse impacts on investment decisions and (ii) rate impacts if the cost of the contracts deviates from the prevailing market price. Currently there are several major market-transforming events planned and contemplated including the pending Regional Greenhouse Gas Initiatives ("RGGI"), as well as the potential for structural changes to the existing NYISO capacity markets that are likely to come from either a NYISO-initiated stakeholder process or a FERC order in the pending ER07-360 case. Combined, these initiatives will have significant and evolving impacts on the New York electricity markets and could make it difficult to identify the optimal long term investment(s). Therefore, CEE and CES suggest that long-term contracts be viewed as a tool of last resort.

3. Should Load Serving Entities other than utilities including the New York Power Authority and the Long Island Power Authority be required or encouraged to enter into long-term contracts as described above? What role, if any, might entities other than Load Serving Entities play in such resource procurement?

Response to Question No. 3:

CEE and CES strongly believe that it would be imprudent to require competitive load-serving entities (either retail ESCOs or wholesale LSEs) to enter into long-term commodity or capacity contracts. Such a policy would either impose significant financial risks on these competitive entities or force them to abandon the New York market. Ultimately, the supply

portfolio of a competitive entity should be structured to support the types of products it sells to its individual customers rather than based on a regulatory mandate.

As discussed in the response to Question No. 2, above, long-term contracts should only be implemented in limited circumstances but could be implemented by a number of different entities including a state agency such as the New York State Energy Research and Development Authority ("NYSERDA").

4. Should resource procurement, as described in Question 1, be coordinated on a statewide basis? What regulatory oversight, if any, would be appropriate?

Response to Question No. 4:

If a resource procurement process is needed, it would be appropriate to utilize a single statewide competitive procurement process. Two examples of such processes are the NYISO's capacity auctions and NYSERDA's RPS program procurement. As with the existing NYISO capacity auctions and the New Jersey BGS auction, a coordinated state-wide process could still accommodate different evaluations, and, if appropriate, award volumes based on differing needs within individual utility service territories.

5. 1. What barriers, if any, exist that discourage long-term contracts for development of new electricity resources? 2. What other barriers exist, if any, for the development of new electricity resources? 3. Should incentives beyond what exist today be created to encourage entry into long-term contracts generally, or to foster the development of any particular type of resource? 4. How could those incentives be structured consistent with the goal of acquiring the most cost-effective resources?

Response to Question No. 5:

CEE and CES are not aware of any barriers that discourage long-term contracts. Regarding the development of new electricity resource, Leslie Biddle, Managing Director of Goldman Sachs, testified at the May 8, 2007 FERC Conference on Competition in Wholesale

Power Markets that there are new power plants being built with financing in the five to seven year range.[1] Similarly, there are numerous reports of lenders entering into financial arrangements with the owners of existing resources to refinance or otherwise restructure the ownership of the facilities.

6. Should constraints be imposed that would, under certain circumstances, restrict the resource types eligible for long-term contracts, limit the length of contract terms or establish the content of other contract conditions? [What steps should be taken to limit any anti-competitive impacts long-term contracts might create?]

Response to Question No. 6:

If long-term contracts are used to achieve public policy objectives, then it would be appropriate to limit the eligible resource types to those that clearly meet the policy objective(s).

7. Should restrictions or guidelines be imposed on the resource procurement practices employed in selecting the resources that would be acquired under the long-term contracts?

Response to Question No. 7:

Yes, restrictions should be imposed such that long-term procurement is only implemented for specific criteria such as to meet a clearly defined public policy objective or when there is significant evidence of an uncorrectable market failure.

8. How should long-term contract costs be recovered from customers, and should different recovery mechanisms be developed based on the type of resource that is acquired under the contract, the length of the contract, or other factors?

1 See transcript at page 134, lines 7-18 "The two power plants, two greenfield power plants that are being built are Plum Point and Longview, and neither of those were built with 20 year PPAs from industrials, or the authorities ... And that way that those contracts are actually being established in the market right now is that they're going in and stepping in for almost like a bridge contract, where it's five to seven years.…."

Response to Question No. 8:

The implementation of long-term contracts should be done in a competitively neutral manner with any difference between the contract cost and the prevailing market price collected from / credited to all utility customers either through a mechanism like the current systems benefit charge or through a non-bypassable surcharge / credit on the utilities' delivery charge.

9. What procedures should be followed in reviewing a long-term contract and in establishing its qualification for cost recovery? Under what circumstances, if any, should recovery of contract costs be pre-approved?

Question No. 9 Response:

The cost of long-term procurement contracts required either to meet a clearly defined public policy objective or in the event that there is significant evidence of an uncorrectable market failure should be fully recoverable and should be eligible for pre-approval by the Commission.

10. Can long-term contracts (energy and/or capacity) be harmonized with existing NYISO rules for energy and capacity markets, and with potential NYISO forward capacity markets? If so, how can they best be harmonized? What changes to NYISO market rules, if any, would be necessary or appropriate for the purpose of accommodating long-term contracts? Should NYISO market rules recognize or ameliorate the impact, if any, of long-term contracting on the NYISO capacity prices paid existing generators, or, if amelioration is appropriate, should it be accomplished through non-NYISO mechanisms?

Response to Question No. 10:

Currently both the ISO New England ("ISO-NE") and PJM wholesale markets have adopted forward capacity markets that will procure local and regional resources to meet their annual reliability needs for the delivery year three years into the future. In addition, the ISO-NE

design allows new entrants that clear the market to obtain an escalating price guarantee (providing them an assured revenue stream) for up to five delivery years. By providing new resources with 5 years of price certainty, the ISO-NE Forward Capacity Market was designed to provide an appropriate price signal to attract and retain the resources necessary to maintain reliability and help new resources overcome the risk premium associated with a capital intensive investment by providing an initial five year period of price certainty.

As discussed above, the NYISO is considering alternatives to its capacity construct. If it adopts a forward market design along the lines of ISO-NE's Forward Capacity Market, that may provide a market mechanism to attract new resources. Such a market mechanism, coupled with the concurrent investment in energy efficiency and demand response measures, may be sufficient to obviate the need for mandated long-term contracts and other non-market solutions.

11. Are there any other creative solutions that might be considered to address the issues identified herein?

Response to Question No. 11:

Investments in energy efficiency and demand response measures will likely mitigate the need for future supply-side resources. The recently initiated Commission proceeding in Case 07-M-0548 is anticipated to develop programs and/or incentives to help reduce state-wide electricity usage by 15% by 2015. If these reductions are concentrated in resources-constrained regions, the need for new supply-side resources could be significantly deferred.

IV. CONCLUSION;

CEE and CES appreciate the opportunity to address the important issues raised in this proceeding and respectfully request that the Commission approach the issue of long-term contracts cautiously and consistent with the views and recommendation expressed herein.

Respectfully submitted,

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