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## **PRELIMINARY STATEMENT**

Multiple Intervenors, an unincorporated association of over 50 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State, hereby submits its Initial Comments on Phase II Issues in Case 06-M-1017.<sup>1</sup>

On August 28, 2006, the New York State Public Service Commission (“Commission”) issued an Order Instituting Proceeding and Notice Soliciting Comments (“August 28<sup>th</sup> Order”) in this proceeding. In the August 28<sup>th</sup> Order, the Commission solicited comments from interested parties on electric utility hedging and supply portfolio management practices. Numerous parties, including Multiple Intervenors, submitted comments in response to the August 28<sup>th</sup> Order.

On April 19, 2007, the Commission issued an Order Requiring Development of Utility-Specific Guidelines for Electric Commodity Supply Portfolios and Instituting a Phase II to Address Longer-Term Issues (“April 19<sup>th</sup> Order”) in this proceeding. In the April 19<sup>th</sup> Order, the Commission: (a) resolved certain issues pertaining to utility hedging practices; and (b) instituted a second phase of this proceeding to examine “long-term contracting, resource planning, energy efficiency, and environmental issues” raised by certain parties in comments submitted in response to the August 28<sup>th</sup> Order. (See April 19<sup>th</sup> Order at 5.) Specifically, the Commission noted that while some parties advocated for the adoption of a statewide integrated resource planning (“IRP”) process, other parties called for

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<sup>1</sup> 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.

increased reliance on long-term supply contracts “for diversified supply portfolio management (e.g., to maintain appropriate generating fuel diversity) or to provide a financial basis to support the provision of new capacity.” (Id. at 29; footnote omitted.)

The April 19<sup>th</sup> Order solicits initial comments and reply comments on a series of questions posed by the Commission. Multiple Intervenors’ responses to those questions, and positions on the issues raised therein, are set forth below.

**MULTIPLE INTERVENORS’ RESPONSES TO THE  
QUESTIONS POSED IN THE APRIL 19<sup>TH</sup> ORDER**

**Question No. 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? What processes should be adopted, if any, to ensure that resource 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:**

Multiple Intervenors’ position as to whether a statewide IRP process to examine long-term electricity resource needs should be established depends entirely on the purpose and the design of such a process. As detailed below, the Commission should avoid establishment of an IRP process that is duplicative of, or conflicts with, existing planning efforts. The Commission also should refrain from implementing any IRP process unless its primary purpose is to reduce electricity prices paid by New York consumers while maintaining reliable service.

As the Commission recognized in the April 19<sup>th</sup> Order, the New York Independent System Operator, Inc. (“NYISO”) already engages in extensive planning efforts aimed at maintaining the reliability of the State’s bulk electric system. (April 19<sup>th</sup> Order at 32-33.) As part of the NYISO’s reliability planning process, the State’s existing and projected future resources and demands are evaluated over a ten-year period, and current and future reliability needs, if any, are identified. The process relies initially on market-based responses to identified reliability needs, but also provides for regulatory-based projects or solutions (which could include long-term supply contracts) if the market does not respond adequately. Additionally, as a result of Order No. 890 issued by the Federal Energy Regulatory Commission (“FERC”),<sup>2</sup> the NYISO is developing for future implementation an economic planning process, which likely will focus on the identification of congestion-related costs and rely primarily, if not exclusively, on the market to advance solutions to perceived economic needs.

Thus, inasmuch as the NYISO currently employs a comprehensive reliability planning process, and soon may implement some form of economic planning process, a new IRP process instituted by the Commission may be duplicative of – and possibly contradictory to – existing planning efforts.<sup>3</sup> In determining whether a mandatory IRP process is

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<sup>2</sup> See FERC Docket Nos. RM05-17-000 and RM05-25-000, Preventing Undue Discrimination and Preference in Transmission Service, Order No. 890 (issued February 16, 2007).

<sup>3</sup> It also is not clear how a proposed IRP process would be coordinated with the existing Renewable Portfolio Standard (“RPS”) and the recently-proposed Energy Efficiency Portfolio Standard. See, e.g., Case 03-E-0188, Proceeding on Motion of the Commission Regarding a Renewable Portfolio Standard, Order Regarding Retail Renewable Portfolio Standard (issued September 24, 2004), and Case 07-M-0548, Proceeding on Motion of the

necessary, the Commission also should consider whether the incremental benefits that might be gained by establishing another planning process would justify the substantial resources that would need to be allocated to the process.

Assuming, arguendo, that the Commission determines to adopt an IRP process, its primary purpose should be clear – the reduction of electricity prices paid by New York consumers, without jeopardizing reliable service. As detailed, infra, the average retail electricity price in New York is significantly above the national average, and this competitive disadvantage has a large, negative impact on the State’s economy. Despite the plethora of generic proceedings instituted by the Commission in recent years, none of them has focused on how to solve the statewide problem of non-competitive energy rates.<sup>4</sup> An IRP process focused on reducing electricity prices to consumers should: (a) first examine whether, and to what extent, long-term contracts executed by utilities truly are needed to increase supply capacity in the State; and (b) if long-term contracts are found to be needed, focus on how such contracts can be entered into at the lowest possible cost, and risk, to consumers. The process also should consider where additional generation is needed and the appropriate duration of long-term contracts. Competitive bidding, using broadly-targeted requests for proposals (“RFPs”), should be employed as a means of obtaining the most favorable pricing options for long-term contracts. Finally, in choosing between two or more generation proposals competing for a long-term supply contract, the lowest-price proposal should be selected.

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Commission Regarding an Energy Efficiency Portfolio Standard, Order Instituting Proceeding (issued May 16, 2007).

<sup>4</sup> To the contrary, many of the generic proceedings actually exacerbate the problem by resulting in higher energy rates and bills.

**Question No. 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:**

To the extent the Commission requires or encourages utilities to enter into long-term electricity contracts, the primary purpose of such contracts should be to reduce energy and/or capacity prices for end-use consumers. In response to the questions posed, Multiple Intervenors advances the following positions, each of which is addressed in more detail below: (a) the Commission should proceed cautiously with respect to increased reliance on long-term contracts; (b) long-term contracts may be required to ensure that an optimal amount of generation is developed in the foreseeable future due to circumstances unrelated to wholesale market price levels, which are very high; (c) to the extent long-term contracts are pursued, the primary goal of such efforts should be to reduce prices to consumers while maintaining reliability; and (d) long-term contracts generally should not be pursued for the primary purpose of adding particular types of new generation, improving fuel diversity, or furthering environmental policies.

**A. The Commission Should Proceed Cautiously With Respect to Increased Reliance on Long-Term Contracts**

New York's history of relying on utility-executed, long-term supply contracts to promote certain favorably-perceived electric generation projects (e.g., cogeneration) has been an economic nightmare for consumers. Between the ill-fated "Six-Cent Law" and

reliance on what turned out to be wildly-inaccurate long-run avoided cost estimates, over the past decade the State's consumers have paid billions and billions of dollars in "out-of-market" or "stranded" costs. Indeed, a number of these costly contracts remain in existence today and continue to plague consumers. Before embarking down a similar road, the Commission should exercise extreme caution before adopting policies reliant on new, long-term supply contracts. Fundamentally, long-term contracts may be appropriate if their purpose is to reduce prices for consumers, and the use of such contracts to pursue other societal objectives should be discouraged. As the late philosopher George Santayana observed: "Those who cannot remember the past are condemned to repeat it."

One of the touted benefits of transitioning to competitive electricity markets was that the risks associated with the construction and the operation of potentially-uneconomic generation projects would be borne by developers, not consumers. Reliance on long-term supply contracts likely would shift at least some of that risk back to consumers. Notwithstanding the best efforts of the Commission, its staff, and the State's electric utilities, the prospect of predicting wholesale electricity prices over 5 years, 10 years, 15 years or longer is fraught with tremendous uncertainty. For instance, there may be market and/or technological changes in the coming years that are not capable of being predicted at this time. As detailed below, Multiple Intervenors recognizes that some, limited reliance on long-term contracts may be necessary to ensure that: (a) adequate generation capacity is available to maintain reliability; and/or (b) energy and capacity prices are reduced. These uses of long-term contracts would be justified if they are designed to lessen the competitive disadvantage faced by New York consumers due to extremely-high wholesale and retail electricity prices. However, based on the concerns raised above, Multiple Intervenors urges

the Commission to proceed very cautiously before adopting policies dependent upon long-term supply contracts.

**B. Some Reliance on Long-Term Contracts May Be Appropriate to Reduce Prices or Ensure Reliability**

Notwithstanding historically-high wholesale electricity prices, the recent adoption of new scarcity pricing market rules more favorable to generators, and the implementation of installed capacity (“ICAP”) Demand Curves resulting in more stable and higher ICAP prices, there is a paucity of new generation being developed in New York. According to some market participants, notably generators, long-term supply contracts now are necessary to finance the construction of new generation projects.

Initially, it is important for the Commission to recognize that wholesale and retail electricity prices in New York State are extremely high, and the lack of market-driven generation projects can be explained, at least in part, on a number of factors unrelated to price levels, including: (a) the expiration of the Article X siting law and the failure to enact any successor, “one-stop-shopping” siting process; (b) the likelihood of increased public opposition to the siting of new generation, particularly in certain regions of the State; (c) difficulties in obtaining financing for energy projects following the Enron debacle; (d) many generation companies – which often form separate subsidiaries for each project – lack the capitalization and credit strength of regulated utilities; (e) more stringent environmental laws and regulations; and (f) the possibility that the construction of new projects by generators already in the New York market may harm the economics of their existing projects. Thus, there are a number of factors contributing to the absence of the anticipated, vibrant generation market, and easy solutions are not forthcoming.

As a result of these and other factors, it has become apparent that, absent utility-executed long-term supply contracts, there may be very little development of new generation projects in the coming years. Consequently, it may be necessary and appropriate to rely, to some limited extent, on long-term contracts to ensure that: (a) adequate generation capacity is available to maintain reliability; and/or (b) energy and capacity prices paid by consumers are reduced to more competitive levels.

**C. The Primary Goal of Any Increased Reliance on Long-Term Supply Contracts Should Be to Reduce Energy Prices Paid By Consumers While Maintaining Reliable Service**

High electricity prices are having a crippling effect on New York's economy. To the extent the Commission requires or encourages utilities to enter into long-term supply contracts to foster the development of new generation, the primary goal of such an undertaking should be to reduce electricity prices paid by consumers.

According to the Energy Information Administration, which publishes the official energy statistics of the United States Government, the average retail price of electricity in New York in February, 2007 was 14.19 cents per kWh.<sup>5</sup> That price was over 62 percent higher than the national average price of 8.74 cents per kWh.<sup>6</sup> Unfortunately, the disparity between New York and national average electricity prices appears to be increasing. For instance, for February, 2006, New York's average retail electricity price of 13.49 cents

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<sup>5</sup> Energy Information Administration, Average Retail Price of Electricity to Ultimate Customers by End-Use Sector, by State, Electric Power Monthly with Data for February 2007 (issued May 11, 2007) ([http://www.eia.doe.gov/cneaf/electricity/epm/table5\\_6\\_a.html](http://www.eia.doe.gov/cneaf/electricity/epm/table5_6_a.html)).

<sup>6</sup> Id. Only Connecticut, Hawaii and Massachusetts had a higher average electricity price than New York.

per kWh was approximately 60 percent higher than the national average price of 8.43 cents per kWh.<sup>7</sup>

There can be no dispute that New York's non-competitive electricity prices are hurting the State's economy. Indeed, the Commission's primary goal in the coming years should be to reduce the disparity between electricity prices paid by New York consumers and those paid by consumers in other states. The Commission should not require or encourage utilities to enter into long-term supply contracts unless it is convinced that such contracts will reduce retail electricity prices in the State in both the short-term and the long-term. If and when utilities issue RFPs for long-term contracts and evaluate responses received thereto, the primary – if not the exclusive – consideration in evaluating contract proposals should be to reduce prices paid by New York consumers while maintaining reliable service.

**D. Long-Term Contracts Should Not Be Pursued For the Purpose of Adding Particular Types of New Generation, Improving Fuel Diversity, or Furthering Environmental Policies**

Question No. 2 posed by the Commission in the April 19<sup>th</sup> Order solicited comments on, inter alia, whether utilities should be required or encouraged to enter into long-term supply contracts to pursue a number of perceived societal objectives. As detailed below, long-term contracts should not be pursued for the primary purpose of adding particular types of new generation, improving fuel diversity, or furthering environmental policies.

Initially, to the extent new generation is needed, the goal of the Commission should be to reduce energy prices paid by consumers, not to pursue the construction of a

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<sup>7</sup> Id.

certain type of generation that may result in higher prices. In response to any RFP for new generation, different forms of generation should compete against each other, with the contract, if any, being awarded to the least-cost resource.<sup>8</sup> If particular types of generation are excluded from or favored in RFPs, the resulting contract price may be higher than necessary (i.e., the bidding process should be open to all forms of generation bidding on an equal basis).

Long-term electricity contracts should not be required or encouraged for the purpose of improving fuel diversity. New York already enjoys a very diverse fuel mix. For instance, according to the NYISO's website, New York's 2005 energy production by fuel type was as follows:

Nuclear	27%
Natural Gas & Oil	27%
Hydro	19%
Coal	15%
Natural Gas	9%
Other	2%
Oil	1% <sup>9</sup>

Additionally, the Commission recently adopted an RPS, intended to subsidize the development of additional renewable resources.<sup>10</sup>

Thus, New York's fuel mix already is very diverse. Significantly, however, due to the current structure of the NYISO's wholesale electricity markets, gas-fired generation sets the market clearing price in the vast majority of hours throughout the year.

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<sup>8</sup> Such RFPs could include demand response/energy efficiency projects, but, similar to more traditional forms of generation, adequate safeguards would need to be incorporated into the contract to ensure that the offered reductions actually are achieved.

<sup>9</sup> See [www.nyiso.com/public/company/about\\_us/index.jsp](http://www.nyiso.com/public/company/about_us/index.jsp).

<sup>10</sup> See Case 03-E-0188, *supra*, Order Regarding Retail Renewable Portfolio Standard.

Consequently, notwithstanding the existence of substantial nuclear, hydro and coal generation, wholesale energy prices often are based on the bids of gas-fired facilities, whose bids typically reflect volatile natural gas prices. Absent major structural changes to the wholesale electricity markets administered by the NYISO, the most effective means of reducing this correlation is for additional baseload generation to be added to the State's fuel mix. Such efforts, if undertaken, should focus on increasing generation capacity at the lowest possible cost to consumers. There is little point in attempting to reduce the correlation between gas prices and wholesale energy prices if an even more expensive resource displaces gas-fired facilities on the margin.

Finally, Multiple Intervenors does not believe that the Commission should require or encourage utilities to enter into long-term supply contracts for the primary purpose of furthering environmental policies. New York's environmental policies are embodied in statutes and regulations, some of which are applicable to the construction of new electric generating facilities. To the extent a proposed project is in compliance with those statutes and regulations, it is (or should be considered) consistent with State environmental policy. Therefore, rather than attempting to favor one form of generation over another, the primary purpose of any reliance on long-term supply contracts should be to procure new generation at the lowest possible cost to consumers, while maintaining reliability.<sup>11</sup>

**Question No. 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

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<sup>11</sup> The Commission should not forget the lessons of the ill-fated Six-Cent Law, which involved required long-term supply contracts intended to promote a then-preferred form of generation (i.e., cogeneration). New York consumers still are paying for the premiums that were approved for those contracts in the form of stranded costs and above-market contracts.

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:**

To the extent the Commission requires or encourages major regulated utilities to enter into long-term electricity contracts, other load serving entities (“LSEs”) that compete with utilities to provide retail commodity service – such as energy service companies (“ESCOs”) – should be accorded the option (but not be mandated) to participate in RFPs. Upon information and belief, the Commission does not possess the requisite jurisdiction over the New York Power Authority (“NYPA”) and the Long Island Power Authority to require or mandate that those public authorities to enter into long-term supply contracts.

NYPA currently plays a unique role in promoting much-needed economic development within New York through allocations of competitively-priced electricity, and will continue to do so. In particular, NYPA allocations of hydropower are especially important in retaining businesses that are very large employers in the State. It also is anticipated that other beneficial NYPA programs, such as Power For Jobs and Economic Development Power, will be extended or reconstituted to benefit those employers. In short, NYPA plays a critical role in economic development in the State, and much of how that role is fulfilled is controlled by legislation, not Commission policy.

Nevertheless, in response to the Commission’s question, to the extent NYPA is encouraged to enter into new long-term power supply contracts, an overriding policy should be that those contracts not increase the price of existing NYPA allocations. Rather, the incorporation of future power supply contracts into NYPA allocations should be limited to: (a) new allocations; and (b) existing allocations only to the extent recipients thereof elect

to participate in such contracts. Importantly, existing NYPA customers should not be forced to subsidize or participate in new long-term electricity contracts, particularly if such contracts are more expensive than the price of existing allocations.

While ESCO participation in long-term electricity contracts should be facilitated (to the extent such contracts are pursued), the Commission should refrain from mandating – or attempting to mandate – that ESCOs enter into long-term supply contracts. To the extent ESCOs desire, they should be accorded an opportunity to participate in RFPs for long-term supply contracts. Significantly, however, ESCOs must serve the needs of their customers, and customers will contract with an ESCO only if they believe the prices offered truly are competitive. Therefore, ESCOs must retain the flexibility to forego participating in long-term contracts if they determine it is in their best business interests to do so.

**Question No. 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:**

See Multiple Intervenors' Response to Question No. 1.

**Question No. 5:**

What barriers, if any, exist that discourage long-term contracts for development of new electricity resources? What other barriers exist, if any, for the development of new electricity resources? 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? How could those incentives be structured consistent with the goal of acquiring the most cost-effective resources?

**Response to Question No. 5:**

There are numerous barriers that exist that discourage long-term contracts for the development of new electricity resources. Those barriers include, but are not necessarily

limited to: (a) the significant expense associated with such contracts; (b) the significant risk associated with such contracts, particularly given high market price volatility; (c) issues concerning cost recovery; (d) the lack of LSEs that, individually, serve load sufficient to warrant execution of a long-term contract adequate to cause the development of a new generation facility; (e) consumer reluctance to commit to long-term contracts or hedges; and (f) the lack of a developed, forward market for electricity. These barriers are substantial, and form the basis for Multiple Intervenors' recommendation that the Commission proceed very cautiously before requiring or encouraging increased reliance on long-term supply contracts.

There also are numerous barriers for the development of new electricity resources. Some, but not all, of those barriers are identified in subsection B of Multiple Intervenors' Response to Question No. 2, supra, and need not be repeated here.

Notwithstanding the above-mentioned barriers, the Commission should not create any new incentives "to encourage entry into long-term contracts generally, or to foster the development of any particular type of resource." Initially, as the Commission is aware, the State's electric utilities already are obligated to advance regulated solutions (e.g., long-term supply contracts) in response to reliability needs identified by the NYISO where adequate, market-based solutions are not forthcoming. More problematically, the cost of "new incentives" simply would increase the cost of electricity to New York consumers which, for the reasons noted earlier, is exactly the wrong policy direction.

**Question No. 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:**

To the extent the Commission requires or encourages utilities to enter into long-term supply contracts, it should refrain from imposing any constraints with respect to the resource types eligible for such contracts. As noted earlier, imposing constraints will yield higher prices. Rather, the Commission's primary goal should be to facilitate open, fair bidding for the construction of new generation and/or the utility's contracting for electricity supplies at the lowest possible cost to consumers while maintaining reliability.

With respect to contract terms and/or other contract conditions, the Commission's primary focus should be on price, and minimizing risks to consumers. While contract term limitations have some appeal to minimize risk, it probably is premature to establish such limitations now, without the benefit of more knowledge regarding the relationship between contract term and contract price. The Commission should, however, require that all long-term supply contracts include enforceable performance guarantees to ensure that the generator or supplier honors the contract, regardless of whether or to what extent the contract price falls below prevailing market prices.

With respect to the final question posed – “What steps should be taken to limit any anti-competitive impacts long-term contracts might create?” – it is not at all clear that long-term contracts create any anti-competitive impacts that need to be addressed. New York's wholesale electricity markets were designed specifically to accommodate bilateral contracts, which for many years have been a large part of the total market. Moreover, all purchasers and developers of existing generation facilities assumed the regulatory and business risks that steps may be undertaken to facilitate the development of new generation projects. Finally, if, as Multiple Intervenors advocates, any RFP issued for a long-term

supply contract for new generation is open to all potential bidders – and not limited by fuel type or other criteria – generators should not be heard to complain that the process somehow is anti-competitive.

**Question No. 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:**

As the first guideline, long-term contracts only should be pursued if they offer the strong likelihood of near-term and long-term savings for consumers.<sup>12</sup> For the reasons detailed, supra, price should be the primary – if not exclusive – criteria in evaluating contract offers. Solicitations for long-term supply contracts should not be limited to particular resources or fuel types.

The second guideline should attempt to minimize consumer risks by limiting the duration of long-term contracts as much as possible. Given the enormous market price uncertainty going out into the future, the duration of supply contracts should not be any longer than is necessary to ensure the desired development of new generation capacity. Whether the appropriate maximum duration is ten years or less is not certain at this time; absent guaranteed savings to consumers, Multiple Intervenors would advocate that the maximum contract duration be set at ten years.

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<sup>12</sup> Multiple Intervenors recognizes that it may not be possible to guarantee a certain level of savings (unless the contract is based on market prices minus some percentage discount). However, based on the best available projections, the contract price should provide a strong level of confidence that material consumer savings will be achieved. Absent such level of confidence, the Commission should refrain from requiring or promoting the contract.

The third guideline should attempt to minimize consumer risks by limiting the amount of energy and capacity subject to long-term contracts. Absent identified reliability needs and/or market power concerns caused by inadequate available generation, there is little reason why a utility should allocate a substantial portion of its supply portfolio to long-term contracts.

A final guideline would be to require security from the winning generator to ensure performance.

**Question No. 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?

**Response to Question No. 8:**

To the extent regulated utilities enter into long-term electricity contracts, the costs of such contracts should be recovered solely from the utilities' commodity customers. If a customer procures commodity supply from an alternative provider, such as an ESCO, it should not be required to pay the utility for acquiring supply that it does not need. In particular, the long-term contracting process should not create any new delivery charges or non-bypassable or stranded costs that are imposed on delivery customers.

Pursuant to prior Commission decisions, large customers purchasing electric commodity from utilities are generally subject to mandatory hourly pricing tariffs. If such customers are precluded from participating in the hedges provided by mandated long-term contracts, then they should not have to bear any of the costs associated with such contracts. In any long-term supply contract, payments are made for the provision of energy and/or

capacity – to the extent a customer does not want, or is ineligible for, a portion of that supply, it should not have to pay any portion of the contract costs.

**Question No. 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?

**Response to Question No. 9:**

To the extent regulated utilities are authorized to enter into long-term contracts, cost recovery generally should be permitted where the price, the quantity, the term, and the other material provisions of the contract are demonstrated by the utility to be prudent. Consistent with long-standing Commission policy, under no circumstances should utility recovery of contract costs be pre-approved.

The law is well-settled that where a utility is seeking to modify existing rates, the burden of proof is on the utility to demonstrate that the proposed rates are just and reasonable.<sup>13</sup> For many years, the Commission has declined utility requests to pre-approve the prudence of proposed contracts, including commodity supply contracts. There is no compelling reason why the Commission should modify that policy at this time.

In Case 90-E-0775, pertaining to electric power purchase contracts between multiple New York utilities and Hydro Quebec, the Commission declined to pre-approve the contracts as prudent, ruling that:

As to the implementation of these contracts, utility managements are expected to make power supply decisions prudently, and are compensated accordingly. They may not sit on their hands and decline to make decisions in the absence of prior regulatory

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<sup>13</sup> See, e.g., N.Y. Pub. Serv. Law § 72.

determinations of prudence. New York’s statutory structure, sound regulatory practice, and our limited staff resources preclude such an approach.<sup>14</sup>

The ruling could not be more clear that utility managements – and not the Commission – must decide whether an electricity supply contract is prudent in the first instance. The Commission should not micro-manage utilities, and utilities must be responsible for the prudence of their decisions.<sup>15</sup>

The Commission has affirmed its policy of not pre-approving the prudence of power supply contracts repeatedly, and as recently as 2003. In Case 02-E-1656, Consolidated Edison Company of New York, Inc. (“Con Edison”) sought a Commission declaration that the utility’s contract costs arising out of a request for proposals for 500 MW of new electric generating capacity will be recovered in rates.<sup>16</sup> The Commission denied Con Edison’s request, ruling that:

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<sup>14</sup> Case 90-E-0775, Consolidated Edison Company of New York, Inc., Long Island Lighting Company, and Orange and Rockland Utilities, Inc. – Joint Petition for Approval of Long-Term Hydro Quebec Firm Power Purchase Contracts, Order Accepting Contracts for Filing and Denying Petition, 1990 N.Y. PUC LEXIS 54, at 10 (issued December 10, 1990). See also *id.* at 42 (holding that: [a] “Utilities should plan their power purchases ... to timely meet future electricity needs at optimum prices and reliability”; [b] “Utility managers make analogous purchasing decisions routinely, and should be no less able to do so in the marketplace for capacity and energy”; and [c] utility managers “are well-compensated for shouldering this type of decision-making and the risk it entails”).

<sup>15</sup> If, *arguendo*, the Commission elects to modify its long-standing policy and starts pre-approving power supply contracts for prudence, such a significant reduction in utility business risk should be reflected in substantially lower authorized rates of return on equity.

<sup>16</sup> Case 02-E-1656, Consolidated Edison Company of New York, Inc. – Petition for a Declaratory Ruling With Respect to Cost Recovery of Payments For Capacity and Associated Energy To Be Made As a Result of a Recently-Issued Request For Proposal Soliciting 500 MW of New Electric Capacity, Declaratory Ruling on Cost Recovery (issued January 24, 2003) at 9.

When one balances the benefit to Con Edison of the Commission acting on its request against the administrative burden of doing so, it becomes clear that our longstanding policy against prior approval of specific contract prices should continue. Granting Con Edison's ratemaking request would not assure the utility recovery of the contract costs in question because ratemaking is rulemaking, and one commission can neither bind future commissions nor relieve future commissions of their duty to balance ratepayer and shareholder interests when setting "just and reasonable" rates.<sup>17</sup>

In discussing the administrative burden associated with the proposed pre-approval of contracts, the Commission noted that: "Utilities enter into many contracts, often involving confidential terms. The review of these terms can be both delicate and time-consuming."<sup>18</sup>

Thus, utilities should be accountable for the prudence of any contracts entered into for which cost recovery is sought from consumers.

**Question No. 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 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:**

Long-term contracts for energy and/or capacity already are consistent with New York's wholesale electricity markets – there is no need for the Commission (or the NYISO) to adopt any special rules or other mechanisms to "harmonize" them. Since the inception of the NYISO, bilateral contracts between LSEs (including utilities) and generators

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<sup>17</sup> Id. at 9-10 (footnotes omitted).

<sup>18</sup> Id. at 10.

have been an integral part of the State's wholesale electricity markets. Indeed, upon information and belief, approximately 50 percent of the wholesale electricity transacted in New York is through bilateral contracts. Thus, to the extent the Commission elects to require or encourage utilities to enter into long-term supply contracts as a means of facilitating new generation projects, such contracts can be accommodated under the existing market structure and need not be "harmonized" in any particular manner.

Moreover, there is no compelling reason why the NYISO's rules should be modified as a result of this proceeding. Even after a generic policy ruling is issued on the questions posed in the April 19<sup>th</sup> Order, it likely will not be possible to predict, with any degree of certainty, the number or size of long-term contracts that actually will be consummated between utilities and generators resulting in the development of new projects. To the extent any such contracts are executed, the resulting generation likely will not be added to the State's supply mix for a number of years. Thus, it would be premature to decide now that specific market rules should be adopted or modified to account for the results of this proceeding.

Furthermore, although generators may argue that they need some form of financial protection from the impact of new, long-term supply contracts, there are several reasons why no such relief should be granted. First, such relief likely would come at the expense of consumers, thereby resulting in even higher electricity prices in New York. Second, generators presumably will be accorded an opportunity to participate in RFPs and, therefore, may have an opportunity to benefit from an increased reliance on long-term contracts. Third, when existing generators purchased or constructed their facilities, they did so assuming a certain level of regulatory and business risk that includes, inter alia, the

adoption of new policies by the Commission and/or the construction of additional generation projects.<sup>19</sup> In short, generators should not get to be shielded from the impacts, if any, of regulatory policies designed to ensure that adequate generation is developed in New York.

**Question No. 11:**

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

**Response to Question No. 11:**

Multiple Intervenors has no response to this question, other than to emphasize again that the Commission's primary goal in this proceeding should be to reduce energy prices and rates to end-use consumers while ensuring that reliability is maintained. New York's wholesale and retail energy prices are among the highest in the nation and continue to have a significant, negative impact on the State's economy. The Commission should refrain from adopting any policy that would cause energy prices to rise, either in the short-term or the long-term.

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<sup>19</sup> Many generators have benefited from changes in regulatory policy. For instance, ICAP prices have risen since the Commission led the charge within the NYISO stakeholder process to adopt ICAP Demand Curves. Additionally, existing generators with no desire to develop new projects in New York arguably have benefited by the absence of a successor to the expired Article X siting process, which has contributed to the dearth of new projects, thereby helping to maintain electricity prices at very high levels.

## CONCLUSION

For all the foregoing reasons, Multiple Intervenors urges the Commission to resolve the issues identified in the April 19<sup>th</sup> Order in accordance with these Initial Comments on Phase II Issues.

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Respectfully submitted,

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