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June 25, 2007

**VIA HAND DELIVERY**

Honorable Jaclyn A. Brillling  
Secretary  
New York State Public Service Commission  
Three Empire State Plaza  
Albany, New York 12223

Re: 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

Dear Secretary Brillling:

Pursuant to the New York State Public Service Commission's April 19, 2007 Order in the above-referenced case, enclosed please find an original and ten copies of New York State Electric & Gas Corporation's and Rochester Gas and Electric Corporation's Reply Comments.

Respectfully submitted,

  
Scott J. Mueller

Enclosures/97000

cc: Active Party List in Case 06-M-1017 (via First Class Mail and e-mail)

STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

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Proceeding on Motion of the Commission as to Policies, :  
Practices and Procedures for Utility Commodity Supply Service : Case 06-M-1017  
to Residential and Small Commercial and Industrial Customers : Phase II  
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REPLY COMMENTS OF  
NEW YORK STATE ELECTRIC & GAS CORPORATION  
AND  
ROCHESTER GAS AND ELECTRIC CORPORATION

I. Introduction

New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation (respectively, "NYSEG" and "RG&E" and collectively, the "Companies") hereby submit their reply comments on the Phase II issues in the above-captioned proceeding.<sup>1</sup> Like most of the market participants commenting in Phase II (including electric utilities, ESCOs and generators) the Companies agree that there is no reason or justification for returning to a utility-specific, centralized resource planning model, such as that proposed in Staff's Initial Comments. Rather than instituting a multi phase IRP process, which includes annual filings and reviews for each electric utility, the state should rely and build upon the NYISO's comprehensive planning process to implement the state-wide policies for integrated resource planning. New York should build upon and support the competitive energy markets rather than return to the individual utility IRP regime that in the past contributed to some of the highest energy prices in the country. Similarly, the Companies, like many commentators, urge the Commission not to require electric distribution utilities to enter into long-term contracts nor prohibit the use of utility-owned generation to meet electric utility's supply obligations.

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<sup>1</sup> These reply comments are filed pursuant to the Order Requiring Development of Utility-Specific Guidelines for Electric Supply Portfolios and Instituting a Phase II to Address Longer-Term Issues, issued on April 19, 2007 (the "Order").

## II. Summary of Initial Comments

A majority of the initial comments voiced significant concerns about, or clear opposition to, adoption of a traditional IRP process for individual utilities.<sup>2</sup> Commentators noted that the utility specific IRP process had failed in the past, was inconsistent with the competitive markets and would be duplicative of the Comprehensive Reliability Planning Process (“CRPP”) conducted by the New York Independent System Operators (“NYISO”). Many commentators supported use of the NYISO CRPP process to address the issue of inadequate resources and promote other state-wide energy policies.

In stark contrast to the majority of comments opposing utility-specific IRPs, the Staff of the Department Public Service (“Staff”) proposes a return to command and control regulation for resource planning and procurement by electric utilities.<sup>3</sup> Under Staff’s three part proposal, Staff would first develop an interim resource plan based upon an analysis of every Commission and CRPP initiative adopted by each utility to date. Following implementation of the interim plan, Staff proposes a two-track Dynamic Energy Planning Process. In Track I, Staff would develop and submit to the Commission a state-wide plan every three years which evaluates long-term strategic options and recommends specific policy directives over a 15-20 year planning horizon. Under Track II of Staff’s proposal, electric utilities would submit to Staff an annual IRP, including a progress report, to identify resource needs and strategies for meeting those needs over a five years planning period. The annual Track II IRPs would be subject to review by Staff

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<sup>2</sup> See e.g. Comments of the New York Suppliers (AES Eastern Energy, L.P.; Dynergy Power Corp., Inc.; Energy Nuclear Power Marketers, LLC; The Mirant Parties and U.S. Power Generating Company, LLC), p. 17 (June 5, 2007) (the “NY Suppliers Comments”); Comments of Constellation Energy Commodities Group, Inc. and Constellation New Energy, Inc., pp. 3-9 (June 5, 2007) (the “Constellation Comments”); Initial Comments of Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc., pp. 5-8 (June 5, 2007) (the “ConEd Comments”).

<sup>3</sup> Staff Initial Comments, pp. 4-8 (June 5, 2007) (the “Staff Comments”).

and approval by the Commission. Staff would also serve as a centralized information resource in development of the IRPs, and would monitor implementation of the various planning efforts.

On the issue of long term contracts, a large number of market participants (including some merchant generators) oppose requiring electric utilities to enter into mandatory long-term contracts.<sup>4</sup> While many commentators believe that appropriately structured long-term contracts should be an option available to electric utilities, they caution against mandatory long-term contracts that could increase prices for customers, create new stranded costs and undermine development of the competitive market. Like NYSEG and RG&E, commentators also noted that utility-owned generation should be considered as an alternative to long-term contracts.<sup>5</sup>

Many commentators also expressed views regarding the process to be followed by the Commission in considering the Phase II issues. There is widespread support for coordinating any state-wide resource planning with the NYISO in order not to duplicate on-going efforts and to adopt policies that are consistent with the competitive wholesale market.<sup>6</sup> Some commentators suggest that the Phase II proceeding in this docket be consolidated with the Commission's consideration of related issues in other generic proceedings, such as retail access and energy efficiency. Other commentators encourage the Commission to conduct a comprehensive investigation of the Phase II issues, including hearings and opportunity to present testimony.

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<sup>4</sup> See e.g. Initial Comments of the Energy Association of New York, pp. 2-3 (June 5, 2007) (the "Energy Assoc. Comments"); Initial Comments of the Retail Energy Supply Association and the Small Customers Marketer Coalition, p. 3 (June 5, 2007) (the "RESA/SCMC Comments"); Initial Comments of SUEZ Energy, North America, Inc., p. 3 (the "SUEZ Energy Comments"). In contrast, New York City advocates the use of long-term generation and transmission contracts to address unique issues and constraints in New York City.

<sup>5</sup> See e.g. Energy Assoc. Comments at 3.

<sup>6</sup> See e.g. ConEd Comments at 5-6; NY Suppliers Comments at 14-19.

### III. Reply Comments

#### A. State-Wide Integrated Resource Planning Should Be Done Through the NYISO's Comprehensive Reliability Planning Process

The electric industry in New York has been restructured over the past fifteen years to encourage the development and growth of competitive wholesale and retail markets in place of the centrally planned and regulated supply service traditionally provided by electric utilities. While electric utilities continue to have the obligation to provide commodity supply services to their customers, new institutions, such as the NYISO, and new market participants, such as ESCOs and merchant generators, are now facilitating the provision of electric supplies to customers in New York through the competitive market place. Because electric supplies are now being provided by both suppliers and electric utilities, it is inappropriate to return to traditional, utility-specific IRP procedures as suggested in Staff's Initial Comments. Rather, integrated resource planning should be coordinated through the NYISO, with mechanisms designed to ensure reliability, support the competitive markets and promote state-wide energy policies.

The NYISO is already required to conduct an assessment of resource needs through the CRPP, which provides an evaluation of the electric infrastructure needed for reliability through an annual cycle of studies and reports using a 10-year planning horizon.<sup>7</sup> The CRPP process provides an existing platform for promoting state policy objectives and ensuring the availability of appropriate resources. As the NYISO noted in its Initial Comments:

The NYISO is positioned to help the state in this process, and is in a unique position to assist in such an effort. The NYISO can provide reliable information and useful expertise in the design of mechanisms to effectuate new energy policies. A market based

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<sup>7</sup> Initial Comments of NYISO, pp. 4-5 (June 5, 2007) (the "NYISO Comments").

approach to implement state-determined policy objectives is the best opportunity to meet the state's needs in an efficient manner.<sup>8</sup>

The NYISO CRPP process can be enhanced to meet the State's policy objectives, including economics, energy efficiency, renewable resources security, resource diversity or environmental criteria. The NYISO's reliability and planning process should be allowed to develop and mature without the Commission imposing conflicting or redundant planning procedures.

Under the CRPP procedures, the NYISO identifies where new resources are required to maintain grid reliability and the timeframe in which such resources will be needed.<sup>9</sup> While the CRPP looks first to the market to meet the identified demands, the NYISO relies upon electric utilities to provide back-stop solutions when the market does not provide an adequate response.<sup>10</sup> Under New York law, electric utilities have the ultimate responsibility for providing supply service to their customers which either choose utility commodity service or are unable to procure electric supplies from the market. The NYISO and electric utilities should be afforded the flexibility to manage the resource needs of the state consistent with their responsibility to ensure adequate and reliable supplies. In carrying out these responsibilities, the NYISO and electric utilities can also reflect the state's policy objectives in arranging for adequate resources.

As noted in the comments of the NYISO, the implementation of the state's Renewable Portfolio Standard ("RPS") is an example of how the NYISO's procedures can facilitate a collaboration to meet the state's policy objectives. The state established a policy goal of increasing renewable generation to 25% by 2013. In response, the NYISO analyzed the reliability and market implications of new wind resources and revised its market rules to encourage greater wind investment in New York.

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<sup>8</sup> Id. at pp. 1-2.

<sup>9</sup> Id. at pp. 4-5.

<sup>10</sup> Id.

The NYISO CRPP can be enhanced to ensure adequate supplies which reflect the State's policy goals through a state-wide solicitation process. Where the CRPP identifies reliability needs that are not being met by the market, the NYISO could conduct, directly or indirectly, a more comprehensive solicitation for additional resources based upon state policy objectives. The NYISO bid evaluation process could reflect scoring for benefits consistent with policy goals, such as cost effectiveness, diversity and environmental benefits. All resources, including utility owned generation, would be eligible to bid into the solicitation. This type of procedure could provide an efficient mechanism for meeting the state's resource needs and reflecting policy objectives, without instituting new and duplicative planning procedures.

B. Return to a Centralized, Utility-Specific IRP Process Is Inappropriate and Unnecessary

Staff's proposal to institute a duplicative and complex IRP process is inconsistent with the restructured electric markets and unnecessary. The NYISO and electric utilities, along with other market participants and interested parties including the Commission, have developed procedures for evaluating the resource needs of New York on a long and short-term basis and planning for adequate resources to meet those needs.<sup>11</sup> Staff has proposed a three-staged IRP process which is redundant and potentially inconsistent with the NYISO CRPP. As other commentators have noted, in the restructured market the NY PSC should be a participant, but not the lead agency, in assessing energy demand and resource needs.

The Commission need not and should not seek to reinvent the integrated resource planning wheel by engaging in a separate planning process. Instead, the Commission can inform utilities, the NYISO and consumers regarding its objectives with its continued

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<sup>11</sup> NYISO Comments at 2-6.

participation in existing processes so that the results of those efforts can reflect Commission priorities.<sup>12</sup>

Staff's proposed procedures would require a major effort by electric utilities, interested parties and the Commission in developing an interim plan, preparing a long range evaluation and requiring annual filings by each electric utility.<sup>13</sup> The stated purpose of Staff's proposal is to fill a perceived "planning gap" because the NYISO planning process purportedly does not address cost-effectiveness of projects or other public policy issues.<sup>14</sup> Staff's asserted "planning gap" is illusory. Market participants, not Staff or the Commission, should be evaluating the cost-effectiveness of resource options and reflecting state policy objectives in their market offerings. Staff's proposal would return to the centralized, utility-specific planning model under which Staff, rather than the market, would evaluate the cost-effectiveness of resource options. Such a model has failed in the past, is inconsistent with the growth of competitive markets and redundant of the CRPP process established by the NYISO.

Public policy goals such as energy efficiency, emissions reductions, fuel diversity and reliability can best be supported by providing incentives for market driven solutions rather than through the top-down, long-term planning process advocated by Staff. There is no need for the Commission to institute an interim plan or a Dynamic Energy Planning Process at the PSC because the NYISO's CRPP process can be used to reflect state policy objectives. Once the State's policy objectives are determined the Commission should work within the context of the NYISO planning process to identify market-based mechanisms for promoting those policy goals.

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<sup>12</sup> Initial Comments of KeySpan Corporation, p. 2 (June 5, 2007) (the "KeySpan Comments").

<sup>13</sup> Staff Comments at 5-7.

<sup>14</sup> Id. at 5.

C. Electric Utilities Should Not Be Directed Nor Required to Enter into Long-Term Supply Contracts

Under the New York statutory framework, electric utilities have the obligation to provide supply service to any customer in their service territories at just and reasonable rates. Electric utilities should have the opportunity to meet their supply obligations based upon a portfolio of diverse resources which may include new or re-powered utility-owned generation or long-term contracts where appropriate. In no event, however, should electric utilities be required or directed to enter into long-term contracts to facilitate new supply. Requiring utilities to enter into long-term contracts to meet their uncertain load obligations under the current retail access paradigm may unnecessarily increase customer costs and will shift risk from project developers to utilities and their customers. The Commission should avoid the pitfalls created by past experiments with mandated long-term contracts and should provide distribution utilities with the opportunity to manage load migration, participate in the NYISO markets and to meet their customer's needs through a diverse portfolio of resource options, including utility-owned generation.

As noted by the Energy Association of New York, there is a sound basis for avoiding mandated long-term contracts.

This aversion is rooted in the hard reality of New York's historic experience with mandated supply contracts and terms, and the impact they had on the ability of the Commission and the companies to meet their obligation to provide safe, reliable service at just and reasonable prices. The economic consequences to customers in terms of overpayment and stranded costs, from New York's last well-intentioned foray in mandated supply contracts negatively impacts New Yorkers to this day. It was, to a significant degree, in reaction to those cost impacts that the state sought to shift the risks of supply development from local utilities

and their customers to developers through the creation of a competitive market.<sup>15</sup>

The state's negative experience with the Six Cent Law, for which ratepayers continue to pay, argues against the use of mandatory long-term contracts.<sup>16</sup>

While some view long-term contracts as a quick-fix to encourage resource development in New York, many parties point out that this 'solution' fails to address the actual barriers to investment in resources in New York, including a cumbersome siting process and regulatory uncertainty.<sup>17</sup> Mandatory long-term contracts may hinder the development of competitive markets, prevent customers from receiving accurate price signals and expose customers to price shock at the end of the contract period. Long-term contracts are also unnecessary because the forward capacity markets provide a better alternative for supporting new generation and public policy objectives. The NYISO is currently considering implementation of a forward capacity market which could stimulate investment in new resources.<sup>18</sup> Forward capacity markets can provide price certainty over an extended period of time for new development and a mechanism for addressing the State's policy objectives.<sup>19</sup> As suggested by a number of commentators, the Commission should fully consider the potential for forward capacity markets to increase resource development rather than imposing mandatory long-term contracts.<sup>20</sup>

Long-term contracts should be an option for utilities in maintaining a resource portfolio to meet their obligations to provide supply service to their customers. The Commission

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<sup>15</sup> Energy Assoc. of NY Comments at 2.

<sup>16</sup> P.S.L. §66-C (partially replaced) (the "Six Cent Law")

<sup>17</sup> See e.g., NYISO Comments at 4; ConEd Comments at 15; Constellation Comments at 16-17; KeySpan Comments at 5.

<sup>18</sup> NYISO Comments at 4.

<sup>19</sup> ConEd Comments at 3-4.

<sup>20</sup> See e.g., NYISO Comments at 4; Key Span Comments at 7; ConEd Comments at 3-4.

should not, however, mandate long-term supply commitments and should encourage utilities to consider more optimal alternatives, including utility-owned generation. Utility generation projects may provide a lower cost option, with greater flexibility than long-term purchased power agreements. A utility owned facility provides greater operational benefits because, in the event of changed circumstances, it avoids the need to amend a contract, and allows discontinuation of the project without any contractual constraints.<sup>21</sup> There are also cost benefits associated with utility built projects because the owner of the asset is a credit worthy entity and customers are not paying a third party for the risk of default in the out years of a long-term contract.<sup>22</sup> Moreover, with utility owned generation ratepayers retain the benefit of the project over the full life of the asset rather than paying a third party for the full cost of the project over a 10-15 year contract term.<sup>23</sup>

D. The Commission Should Conduct Further Proceedings on the Phase II Issues

Given the wide variety of opinions reflected in the initial comments in Phase II, and the significant divergence between Staff's IRP proposal and the recommendations of the majority of the market participants, the Companies recommend that the Commission conduct further proceedings on the Phase II issues. Most parties agree that it is an appropriate role for the Commission to solicit comments on, and consider, the state-wide policy objectives related to energy supply. Accordingly, as a next step, the Companies recommend that the Commission solicit comments, or conduct a collaborative proceeding, on the procedure for conducting an investigation to consider state-wide energy policy goals related to electric supply resources. This should involve consolidation with other pending generic proceeding, particularly Case 07-M-

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<sup>21</sup> See ConEd Comments at 11.

<sup>22</sup> Id.; see also Constellation Comments at 16-17.

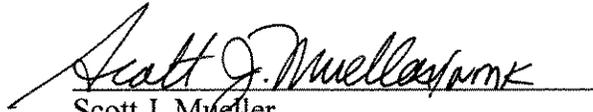
<sup>23</sup> See ConEd Comments at 11.

0548 regarding energy efficiency, or bifurcation of discrete issues or problems, such as resource adequacy in the New York City area.

IV. Conclusion

The Companies appreciate this opportunity to provide their reply comments on the issues identified in the Order and look forward to further participation in the Phase II proceedings.

Respectfully submitted,



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Corporation and  
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CERTIFICATE OF SERVICE

I hereby certify that I caused an original and ten (10) copies of New York State Electric & Gas Corporation's and Rochester Gas and Electric Corporation's Reply Comments in Case No. 06-M-1017 ("Reply Comments") to be served, by hand delivery, upon the Honorable Jaclyn A. Brillling, Secretary to the New York State Public Service Commission. In addition, copies of the Reply Comments were served upon the Active Party List for Case 06-M-1017 via First Class Mail and electronic mail.

Dated this 25<sup>th</sup> day of June, 2007.



Darci L. DeLisle