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December 23, 2002

Honorable Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Room 1-A209
Washington, D.C. 20426

Re: Docket No. EL01-50-002
New York Independent System Operator, Inc.

Dear Secretary Salas:

For filing, please find the Petition for Rehearing in the above-entitled proceeding.
Should you have any questions, please feel free to contact me at (518) 473-7136.

Very truly yours,

Leonard Van Ryn
Assistant Counsel

Enclosures

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

New York Independent) Docket No. EL01-50-002
System Operator, Inc.)

PETITION FOR REHEARING

Pursuant to Rule 713 of the Commission's Rules of Practice and Procedure, the Public Service Commission of the State of New York (NYPSC) hereby submits its Petition for Rehearing in the captioned proceeding.

Copies of all documents and correspondence should be sent to:

Lawrence G. Malone,
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Ronald Liberty, Director
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In its November 22, 2002 Order on Compliance Filing (Compliance Order) in this proceeding,¹ the Commission accepted in its entirety the station power tariff filed by the New York

¹ New York Independent System Operator, Inc., 101 FERC ¶61,230 (2002).

Independent System Operator (NYISO).² In so doing, the Commission exempted wholesale generators from the ancillary services charges that similarly-situated customers must pay for transmission service. Moreover, the Commission, without so stating, appears to exempt wholesale generators from its Order No. 888,³ and its BART Orders.⁴

BACKGROUND

As justifications for the decisions reached in the Compliance Order, the Commission cited a need to eliminate discrimination between generators owned by integrated electric utilities and generators owned by others. Because New York utilities have largely divested their generation, the potential for discrimination does not exist in New York.

Moreover, there is no basis for freeing wholesale generators from charges imposed on other similarly-situated customers owning on-site generation. Transmission costs

² Station power is the electric energy used for the heating, lighting, air-conditioning, and office equipment needs of the buildings on a generating facility site, and for operating the electric equipment that is on the generating facility site. PJM Interconnection, LLC, 94 FERC ¶61,251 (2001)(PJM II).

³ Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services By Public Utilities, Order No. 888, FERC Stats. & Regs. ¶31,036 (1996).

⁴ San Francisco Bay Area Rapid Transit District, 87 FERC ¶61,255 (1999)(BART Order) and 90 FERC ¶61,291 (2000)(BART Rehearing Order).

incurred to serve on-site generation customers are substantially the same as the costs of serving wholesale generators. Charging ancillary services to one, but not the other, is unduly discriminatory and irrational.

Finally, the decisions reached in the Compliance Order are premised in part on a finding that no sale occurs when an out-of-service generator purchases and consumes energy, because the cost of that energy is netted against the prices paid the generator for its output when it is operating. Irrespective of the accounting for the costs of the generator's station use energy, a sale occurs because energy is delivered and consumed at retail. Accordingly, rehearing should be granted and the Compliance Order should be modified.

SPECIFICATION OF ERRORS

NYPSC requests that the Commission grant rehearing on the Compliance Order, based on the following errors of fact and law:

1. The exemption from ancillary services charges afforded merchant wholesale generators in the Compliance Order is not rational.
2. The Commission arbitrarily deviates from policies expressed in prior Orders, where it decided that there is an element of local distribution service in any unbundled retail transaction and that state jurisdiction over delivery service includes the authority to impose non-bypassable distribution or retail stranded cost charges.

3. The Commission erred, as a matter of law and fact, in finding that netting the cost of the energy delivered to wholesale generators against the price of their prior production is not a retail sale, when the energy delivered under those circumstances is supplied from the NYISO spot markets.

ARGUMENT

I. The Ancillary Services Exemption Is Not Rational

The Commission has not justified exempting wholesale generators from payment of ancillary services charges. In explaining its decision, the Commission relies primarily on PJM II, where it propounded a similar exemption on the grounds that it eliminated discrimination between integrated utilities owning generators and merchant wholesale generators. The Commission also accepts the NYISO's unsupported hypothesis that the ancillary services charges are not worth the cost that would be incurred to collect them.

As indicated above, the discrimination the Commission found in PJM cannot exist in New York. New York's utilities are no longer integrated, because they have divested their generators, with a few de minimus exceptions. These few exceptions are not capable of creating the discrimination that

the Commission perceives. NYPSC urges the Commission to respect regional distinctions between PJM and NYISO.⁵

In filing its compliance tariff, NYISO, without offering a reason, reversed its prior position in this proceeding on ancillary services charges -- that a waiver of the charges for wholesale generators would be not needed because of the magnitude and scope of NYISO's numerous ancillary services markets.⁶ Given the mature development of these markets, the administrative cost of collecting the charges is simply that incurred to bill the wholesale generators the price those markets readily yield. The Commission nonetheless accepted NYISO's new contention that a waiver of ancillary services charge recovery from wholesale generators is warranted, because the magnitude of the administrative costs of collection exceeds the relatively small volume of the charges themselves.

NYISO, however, must already account and bill for netted energy, when netting is accomplished by using transmission service to deliver to the wholesale generator the energy from NYISO spot markets consumed when generation

⁵ The Commission has previously recognized regional differences; the netting period for ISO New England is one hour instead of the monthly period tariffed by PJM and NYISO. See Rumford Power Associates, L.P., 97 FERC ¶61,173 (2001).

⁶ New York Independent System Operator, Inc., 99 FERC ¶61,167 (2002)(Tariff Filing Order), at 61,678.

equipment is out of service. Because the cost of that netted energy, and its delivery, is offset against the price paid for energy the generator produces while in service, NYISO must gather, record, and cumulate all the hourly price and usage data it will input into the calculation of the netted energy delivery and consumption offset. Adding the ancillary services charges to the netting calculation is a ministerial process that should spawn little or no administrative cost.

Just as the NYISO failed to support its contention that the administrative costs of billing ancillary services would be burdensome, the Commission has failed to present a scintilla of cost or other data in support of its finding on the magnitude of the administrative costs. The Commission also fails to articulate why the similarly-situated customers who own and operate on-site generation, but are not wholesale generators, fail to qualify for exemption from ancillary services charges. For those customers, the "costs" of recovering the ancillary services charges are just as "high" compared to the "volume used" as for the wholesale generators.⁷ Because NYISO is capable of billing these direct customers for the ancillary services costs they impose on the transmission

⁷ Compliance Order, p. 15.

system, it is also able to efficiently assess the charges against wholesale generators.

As indicated above, instead of eliminating discrimination, the Compliance Order creates undue discrimination. Wholesale generators are exempted from the ancillary services costs they impose on the transmission system, but other large industrial and commercial customers who own on-site generation must pay those costs when their generators are out of service. The usage patterns of these large customers owning on-site generation often resemble the usage patterns of the wholesale generators at times when their generation equipment is out of service. When either type of customer consumes energy delivered over the grid because a generator is out of service, the same types of costs are imposed on the transmission system. The Compliance Order offers no reason for favoring the wholesale generators with an exemption from ancillary services charges. As a result, rehearing should be granted because the Compliance Order affords wholesale generators unduly discriminatory treatment.

Finally, the Commission failed to adequately consider NYPSC's argument that exempting wholesale generators from the ancillary costs they impose on the transmission system raises the potential for harm to the transmission system. All ancillary services supporting the transmission system must be

properly charged if the system is to operate efficiently. To pick and choose when ancillary services should be charged to a particular class of customers ignores the operating characteristics of the transmission system. If revenues necessary to support the system's ancillary services operations are not collected, and those operations are not adequately funded, the security of system operations is thereby threatened (unless the costs are improperly subsidized by other customers).

II. The Commission's Deviation From Policies Expressed In Prior Orders Is Arbitrary

NYPSC previously requested that the Commission clarify the application of Order No. 888 and the BART Orders. Under Order No. 888, the Commission found that "there is an element of local distribution service in any unbundled retail transaction"⁸ and state jurisdiction over delivery service includes the "authority to impose non-bypassable distribution or retail stranded cost charges."⁹

Elaborating upon that principle, the Commission found in the BART Order that, even where there are no identifiable local distribution facilities, states have jurisdiction over retail delivery to end-users and so may assess separate charges

⁸ Order No. 888, at 31,783.

⁹ Order No. 888, at 31,781-82.

for distribution service in addition to the Commission's jurisdictional charge for transmission service. This state jurisdiction over distribution service permits the use of suitably-developed retail rates for stand-by service, which may include non-bypassable customer or stranded cost charges, for customers taking delivery at either distribution or transmission levels.

The Compliance Order analysis of Order No. 888 and the BART Orders is inconsistent. At one point, the Compliance Order states any "delivery of station power over local distribution facilities, and the compensation for such delivery is a matter properly for [NYPSC]." ¹⁰ Yet, at another point, the Order requires NYISO to clarify "that any energy delivered that falls under the definition of station power must be netted against energy produced" by a generator, no matter "at what voltage or meter" the delivery occurs. ¹¹ Since distribution meters are included in this netting mandate, and given the broad definition of station use, it appears the Commission is unlawfully asserting jurisdiction over retail energy use and distribution. The result is not only ultra vires action, but is a de facto modification of the prior Orders.

¹⁰ Compliance Order, p. 12.

¹¹ Compliance Order, pp. 16-17.

The Compliance Order, along with other recent Orders on station use, states that the Commission has not altered Order No. 888 or the BART Order provisions allowing the states to impose stranded cost and customer charges on retail use. But the recent Orders obstruct the imposition of those charges on wholesale generators. For example, in PJM III, which the Commission relies upon in the Compliance Order, the Commission states that, where transmission service is unbundled, it may limit charges to those set forth in the pro forma tariff "unless we specifically approve other terms (emphasis added)."¹² That statement is in conflict with the BART Rehearing Order, which states that "no matter where the state/federal jurisdictional line is drawn, some portion of the transmission service is subject to [state] jurisdiction."¹³

The recent USGen Clarification Order continues the conflict.¹⁴ There, the Commission reiterated its PJM III Order approach, claiming that when wholesale generators "self-supply" netted generation at the transmission level, the only service used is unbundled transmission service subject to its jurisdiction. That Order then failed to decide the question if

¹² PJM Interconnection LLC, 95 FERC ¶61,333 (2001), at 62,185.

¹³ BART Rehearing Order, p. 9.

¹⁴ USGen New England, Inc., 100 FERC ¶61,199 (2002).

a state can attach its stranded cost and customer charges to that service provided a wholesale generator.

Given, however, that the Commission has found that only unbundled transmission service is involved in such an arrangement, precluding distribution service as a source for the charges, and that it has found there is no sale of energy to tack the charges onto, it appears that the Commission does intend to prevent states from presenting the charges. The Commission does not explain how a state might present the charges if it is preempted from including them on a transmission services bill, and there is no distribution or energy sale element to station use at the transmission level. Prior Orders are thereby overturned without explanation.

III. The Commission's Finding That Netting
is Not a Retail Sale is Incorrect
As a Matter of Fact and Law

The Commission has found that a generator's self-supply of station power does not involve the sale of energy.¹⁵ When a generator is operating, and draws its electricity directly from its generating equipment, this is undoubtedly true. The Commission, however, did not limit its finding to those circumstances. Instead, it found that when a generator did not operate, its netting of the cost of the energy delivered

¹⁵ PJM II, at 61,889-91.

to it against the price paid for its production is not a sale, even when station use energy under those circumstances is supplied from a third party -- the NYISO spot markets.

While the Commission has jurisdiction over wholesale sales, and may find that station use is not a wholesale sale, it lacks jurisdiction over retail sales of energy. A finding on the absence of a wholesale sales does not extend to a finding on the existence of a retail sale. Whatever the validity of the Commission's assertion of jurisdiction over the retail transmission of station use power, its expansion of its jurisdiction into the area of retail energy sales is ultra vires.

While FERC has the jurisdiction to decide what is a wholesale sale, it concedes that none is present in station use.¹⁶ Once it is decided there is no wholesale sale, the Commission lacks the jurisdiction to rule that energy consumed for station use is not a retail sale. That determination must be left to the states that have jurisdiction over retail sales.

Moreover, a finding that a retail sale does not occur when an out-of-service generator consumes electricity delivered from the NYISO markets is unsustainable. Generators netting their energy costs most certainly do consume retail energy

¹⁶ PJM II, at 61,894.

supply from the NYISO markets when their equipment is incapable of generating. Otherwise, they would not be able to operate their non-generation equipment or restart their generators. While netting may be a useful approach to accounting for that station use energy, it does not change the fact that the energy consumed is being purchased and delivered for use at retail.

Indeed, the Commission, at its most recent Open Meeting on December 18, 2002, found that there was a retail sale when a wholesale generator purchases its station use energy from an independent third party. A purchase from the NYISO markets is a retail purchase and sale just the same, even though the cost is accounted for through netting.¹⁷

As another justification for netting, the Commission, in PJM III, asserted that allowing wholesale generators to net and take transmission retail service was analogous to netting by integrated utilities at generators they own. In fact, when New York utilities were integrated, they accounted for station use energy and its delivery as charges to their customers. They did not suggest that generators failed to consume energy for station use when out-of-service, or that the cost of delivering station use energy from elsewhere was less than the costs of delivering energy to other customers.

¹⁷ Docket No. EL03-10, Northeast Utility Services Company, Draft Order (December 18, 2002)(NUSC Draft Order), pp. 8-9.

Moreover, integrated utilities were able to supply energy to an out-of-service generator from other generators that were operating. Few, if any, wholesale generators in New York can make the same claim.¹⁸ The new form of netting service the Commission has devised for wholesale generators differs in these respects from integrated utility operations.

Therefore, whether to net the delivery of retail energy is a decision that must be left to the states. Accordingly, the tariffing of netting in the NYISO OATT as a transmission service is without foundation in law or fact.

NYPSC does not oppose the practice of energy netting for transmission-level wholesale generators. Indeed, NYPSC does not necessarily oppose energy netting through distribution meters at distribution voltages. What NYPSC does oppose is the Commission's use of netting to assert jurisdiction over retail energy supply. Instead of asserting jurisdiction over retail energy supply and distribution, the Commission should decide that Order 888 and the BART Orders continue to adhere. As a result, wholesale generators must pay stranded cost and customer charges applicable to any similarly-situated customer who takes electric service when its generator is out of operation.

¹⁸ Even where a parent owns indirectly interests in multiple wholesale generators located in New York, in most cases the generators may not net against each other because each is owned and operated by an independent affiliate.

IV. The Compliance Order Should Be Modified
To Provide That Delivery and Supply of
Netted Energy is Subject to State Charges

The Commission rejected the requests of many parties to this proceeding that it find that transmission service for netted generation be provided under Part IV of the NYISO Open Access Transmission Tariff (OATT). Use of that tariff would have made application of the stranded cost and customer charges automatic. Moreover, it would have eliminated discrimination, since on-site generators who purchase energy from the NYISO spot markets when their generation units are out-of-service would be charged under Part IV for the transmission of that energy.

Instead, the Commission chose to rely upon the NYISO's selection of OATT Part II as the appropriate tariff for transmitting netted station use energy. This tariff provides for wholesale transmission service. Since wholesale generators are taking a retail service, it is unreasonable to charge for the service under OATT Part II alone.

Moreover, selection of OATT Part II as the applicable service makes it difficult for NYPSC to properly arrange for the assessment of state-jurisdictional stranded cost and customer charges. The finding that netting does not result in a sale of energy, preventing the attachment of the charges to that sale, further frustrates the ability of NYPSC to arrange for presentment of the charges it adopts. To avoid these obstacles,

netted energy should be transmitted under OATT Part IV, after the decision to allow netting at retail is left to the states.

CONCLUSION

The Commission should grant rehearing and find that NYISO must charge merchant wholesale generators for the ancillary services they use in transmitting netted energy; that retail sale jurisdiction is left to the states; and, that NYPSC may attach stranded cost and customer charges to the retail energy and delivery services wholesale generators consume when their generation equipment is not operating.

Respectfully submitted,

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General Counsel

Leonard Van Ryn
Assistant Counsel
Public Service Commission
of the State of New York
Three Empire State Plaza
Albany, New York 12223-1350

Dated: December 23, 2002
Albany, New York

CERTIFICATE OF SERVICE

I, Janet Burg, do hereby certify that I will serve on December 23, 2002, the foregoing Petition for Rehearing by depositing a copy thereof, first class postage prepaid, in the United States mail, properly addressed to each of the parties of record, indicated on the official service list compiled by the Secretary in this proceeding.

Date: December 23, 2002
Albany, New York

Janet Burg