

STATE OF NEW YORK DEPARTMENT OF PUBLIC SERVICE

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PUBLIC SERVICE COMMISSION

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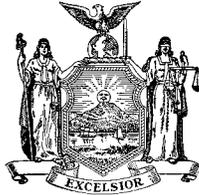
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Acting Secretary

December 29, 2003

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

Re: Docket No. RM01-10-000 - Standards of Conduct for
Transmission Providers

Dear Secretary Salas:

For filing, please find the Motion for Clarification or, in the alternative, Request for Rehearing of the New York State Public Service Commission in the above-entitled proceeding. Should you have any questions, please feel free to contact me at (518) 473-8178.

Very truly yours,

David G. Drexler

David G. Drexler
Assistant Counsel

Attachment

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Standards of Conduct for) Docket No. RM01-10-000
Transmission Providers)

**MOTION FOR CLARIFICATION OR, IN THE ALTERNATIVE,
REQUEST FOR REHEARING OF THE
PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK**

Pursuant to Rules 212 and 716 of the Federal Energy Regulatory Commission's (Commission) Rules of Practice and Procedure, 18 C.F.R. §§ 385.212 and 385.716, the Public Service Commission of the State of New York (NYPSC) respectfully submits this Motion for Clarification or, in the alternative, Request for Rehearing with respect to the Commission's Order No. 2004 (Final Rule)¹ issued on November 25, 2003 in the above-referenced proceeding.

Copies of all documents and correspondence should be addressed to:

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Ronald Liberty, Director
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Office of Electricity
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¹ *Standards of Conduct for Transmission Providers*, Order No. 2004, III FERC Stats. & Regs. (Regulations Preambles) ¶ 31,____ (November 25, 2003), 68 Fed. Reg. 69,134 (December 11, 2003)("Final Rule" or "Order No. 2004").

SUMMARY

The fundamental principle underlying the Final Rule is the requirement that a natural gas pipeline and electric transmission provider's ("Transmission Provider") employees engaged in transmission system operations must function independently from the Transmission Provider's marketing and sales employees and from any employees of its Energy Affiliates. An Energy Affiliate is defined as anyone that is involved in, manages or controls transmission capacity, or anyone that buys, sells, trades or administers natural gas or electric energy in the U.S. However, an Energy Affiliate does not include a local distribution company (LDC) that does not make any wholesale/off-system sales.

The NYPSC supports the Commission's goal of reducing opportunities for anti-competitive behavior by ensuring that electric and gas Transmission Providers and their energy affiliates do not share market-sensitive information on a preferential basis. We believe that the development of workably competitive markets requires specific guidelines that protect against the misuse of such confidential information. However, we are concerned that the Commission has failed to demonstrate that certain provisions of the Final Rule will not: 1) intrude upon the jurisdiction of states to regulate retail distribution

service; 2) unnecessarily limit the ability of LDC's to use the transmission systems of non-affiliated Transmission Providers; 3) adversely affect the operational reliability of the natural gas and electric industries; and 4) result in excessive and unnecessary compliance costs. As a result, the NYPSC seeks clarification or, in the alternative, rehearing of the issues contained herein.

I. Request For Clarification

The NYPSC believes that the majority of the comments discussed below may be more appropriately addressed in the form of clarification. However, out of an abundance of caution, the discussion is structured to comply with the rehearing requirements.

II. Request For Rehearing

SPECIFICATIONS OF ERROR

1. The Commission's imposition of standards of conduct on local distribution system's gas and electric employees that are not engaged in sales for resale is an unlawful exercise of jurisdiction in contravention of Section 1(c) of the Natural Gas Act and Section 824 of the Federal Power Act;

2. The Commission's limitation of the LDC exemption to only those Energy Affiliates that make no off-system sales is arbitrary and discriminatory in its application.

3. Even assuming the Commission has the jurisdiction to broadly define an Energy Affiliate as it has done, the Commission's failure to include a provision for the permissible sharing of operational reliability information between an operating employee of the distribution system and the Transmission Provider is arbitrary; and

4. Even assuming the Commission has the jurisdiction to broadly define an Energy Affiliate as it has done, the Commission's failure to balance the need to take such corrective action in the rulemaking against the cost of compliance with the rule is arbitrary and demonstrates a lack of reasoned decision-making.

DISCUSSION

I. The Commission's Imposition Of Standards Of Conduct On Local Distribution Company's Gas And Electric Employees That Are Not Engaged In Sales For Resale Is An Unlawful Exercise Of Jurisdiction In Contravention Of Section 1(c) Of The Natural Gas Act And Section 824 Of The Federal Power Act

The Natural Gas Act and the Federal Power Act clearly provide that the Commission's regulation of sales in interstate commerce is limited to those at wholesale, leaving to the states the function of regulating the distribution and sale of the

commodity.² It is clear that Congress intended to leave retail distribution transactions to state regulation.³

While the Commission has recognized that jurisdiction over retail sales is reserved to the states,⁴ the Final Rule indicates that "if a retail sales unit engages in any wholesale sales, the separation of functions requirement will apply."⁵ With respect to electric, the Commission's exemption from the separation requirement for sales units that engage solely in bundled retail sales does not apply, because the Commission considers retail electric service to have been unbundled in New York. It is our understanding that where an electric distribution unit has excess energy that is sold through the New York Independent System Operator, Inc., that action would subject the entire retail distribution unit to federal regulation. Thus, the Commission's imposition of federal standards of conduct on all distribution system employees, including those that are not engaged in sales for resale, is an unlawful exercise of

² *Central States Electric Co. v. City of Muscatine, Iowa* 324 U.S. 138, 144, 65 S.Ct. 565, 568 (U.S. 1945).

³ No area was intended to be outside any regulation, and if a given area is not suitable for state regulation the Commission can regulate it. Federal Power Com'n v. Transcontinental Gas P.L. Corp., 365 U.S. 1, 81S.Ct. 435 (U.S. 1961).

⁴ Id.

⁵ Order No. 2004 at ¶79.

jurisdiction in contravention of Section 824 of the Federal Power Act.⁶

On the gas side, FERC explains that an LDC that engages in **any** off-system sales will be considered an Energy Affiliate and become subject to the standards of conduct. The consequences for this characterization are severe: the transmission function employees of a Transmission Provider must function independently from all employees of an Energy Affiliate. In other words, the Final Rule prohibits employees of the gas affiliates from having any communications relating to transmission, distribution, scheduling and reliability of the retail sales service with the Transmission Provider. Because reliability cannot be compromised, the LDC may have no real choice other than to eliminate the use of off-system sales as a means to balance supply and demand on the system. The resulting loss of revenue from off-system sales and the increased costs to consumers associated with new balancing contracts are significant.

The fact that a LDC makes a limited number of off-system sales does not provide the Commission with the authority to regulate the conduct of all employees in the affiliated

⁶ FPA §824; *New York v. FERC*, 535 U.S. 1, 20-23 (2002) (noting that FERC's jurisdiction over the sale of power is confined to wholesale markets and does not extend to retail sales). As the Commission indicated in its Order No. 888, "the Commission's jurisdiction over sales of electric energy extends only to wholesale sales." Order No. 888 at p. 430.

distribution company. To conclude otherwise would allow FERC to unnecessarily intrude upon the state's authority. Moreover, as a policy matter, allowing FERC to regulate in this area is duplicative, especially in states like New York, which have their own state-imposed codes of conduct.⁷

In sum, there is no basis for the Commission to utilize limited off-system sales as the hook for imposing regulation in an area expressly reserved by Congress for the states. Thus, the Commission should indicate that the separation requirement will not be applied to employees engaged in retail sales.

II. The Commission's Limitation Of The LDC Exemption To Only Those Energy Affiliates That Make No Off-system Sales Is Arbitrary And Discriminatory In Its Application

On the gas side, by excluding state-regulated LDCs that do not make any off-system sales from the definition of an Energy Affiliate, the Final Rule creates a distinction between affiliated LDCs that make off-system sales, and therefore are

⁷ See, e.g., Cases 01-E-0359 et al., Petition of New York State Electric & Gas Corporation for Approval of its Electric Price Protection Plan, Order Adopting Provisions of Joint Proposal With Modifications (issued February 27, 2002), Appendix B; Cases 93-G-0932 et al., Proceeding on Motion of the Commission to Address Issues Associated with the Restructuring of the Emerging Competitive Natural Gas Market, Order (issued March 29, 1996); Case 93-G-0932, supra, Order Resolving Petitions for Rehearing (issued September 13, 1996); Case 00-G-1858, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of National Fuel Gas Distribution Corporation, Order Adopting Terms of Joint Proposal (issued April 18, 2002).

subject to the Final Rule, and non-affiliates that also make off-system sales, but are not subject to the Final Rule. However, this distinction does not recognize whether such off-system sales involve transmission by an affiliated or by a non-affiliated pipeline. As such, an affiliated LDC engaged in off-system sales using the facilities of a non-affiliated pipeline would be subject to the requirements of the Final Rule, despite the fact that they would not have an opportunity to gain preferential treatment. Notwithstanding the lack of preferential treatment, the affiliated LDC would not be provided with an exemption under the Final Rule. The affiliate rule is unnecessary to protect against discrimination because the Commission has no basis for treating Energy Affiliate LDCs that use non-affiliated pipelines the same as LDCs that use affiliated pipelines. For example, there is only one LDC in New York that is an affiliate of an interstate pipeline, National Fuel Distribution Corporation (NFDC).⁸ Although NFDC engages in limited off-system sales, none of those sales take place on or involve affiliate-related transportation facilities.

⁸ Keyspan has an approximate 30% ownership interest in Iroquois Gas Transmission System. Iroquois, however, obtained a waiver under Order No. 497 from the existing regulations.

III. The Commission's Failure To Include A Provision For Permissible Sharing Of Information Relating To Operational Reliability Between An Operating Employee Of The Distribution System And The Transmission Provider Is Arbitrary

The Final Rule provides the following two provisions:

§ 358.4(a)(1) Except in emergency circumstances affecting system reliability, the transmission function employees of the Transmission Provider must function independently of the Transmission Provider's Marketing or Energy Affiliates' employees.

§ 358.5(b)(8) A Transmission Provider is permitted to share crucial operating information with its Energy Affiliate to maintain the reliability of the transmission system.

New York seeks clarification that the general prohibition of § 358.4(a)(1) is not intended to limit the specific exemption under §358.5(b)(8) for sharing "crucial operating information" with an Energy Affiliate in order to maintain the reliability of the transmission system on a daily basis. In the alternative, New York requests the following rehearing.

As New York explained in its earlier comments on the proposed rulemaking, the transmission and distribution functions of an Energy Affiliate and a Transmission Provider must communicate effectively to ensure the reliable and efficient operation of the system. Otherwise, basic information such as pressures on the system and capacity constraints, which are necessary for the reliable and efficient operation of the system, would not be known. Under the previous rules, the only

entities that were required to operate independently were the transmission related employees of the Transmission Provider and the employees of the distribution system that were engaged in marketing and sales functions.

In the Final Rule, the Commission provided for the sharing of employees between Transmission Providers and their Marketing and Energy Affiliates at the executive level (senior officers and directors) and in the trenches (field and maintenance personnel), but not for mid-level operating personnel (i.e., employees engaged in distribution and retail sales operations). Based on the foregoing, we seek rehearing of the failure of the Commission to include within the permissible sharing between Transmission Providers and their Marketing and Energy Affiliates those operational employees of the distribution company that are not engaged in wholesale sales and marketing.

IV. Even Assuming The Commission Has The Jurisdiction To Broadly Define An Energy Affiliate, The Commission's Failure To Balance The Need To Take Such Corrective Action In The Rulemaking Against The Cost Of Compliance With The Rule Was Arbitrary And Demonstrates A Lack Of Reasoned Decision-Making

The record demonstrates that the complete separation of employees and facilities for National Fuel Supply, which serves a transmission function, and NFDC, which serves a sales function, would cause significant disruption and serious cost impacts. According to NFDC, it would cost \$18 million per year

to comply with the separation of functions requirement. There is no basis in the record for concluding that the cost imposed on NFDC will be offset by any measurable benefits to NFDC's customers. Under these circumstances, the Commission has failed to demonstrate that consumers will receive any net benefit of the application of the standards of conduct to distribution employees not engaged in wholesale sales and marketing.

CONCLUSION

For the reasons stated above, the Commission should either grant our Motion for Clarification or, in the alternative, our Request for Rehearing of its Order No. 2004.

Respectfully submitted,

Dawn Jablonski Ryman

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Dated: December 29, 2003

CERTIFICATE OF SERVICE

I, Karen Houle, do hereby certify that I will serve on December 29, 2003, the foregoing Petition for Clarification and Rehearing of the Public Service Commission of the State of New York 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 29, 2003
Albany, New York

Karen Houle
Karen Houle