UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Consolidated Edison Company of New York, Inc.	) Docket No. EL01-45-000) Docket No. ER01-1385-000

NOTICE OF INTERVENTION AND ANSWER OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

Pursuant to Rules 213 and 214 of the Federal Energy Regulatory Commission's (Commission's) Rules of Practice and Procedure (18 C.F.R. §§ 385.213 and 385.214) and the Commission's Notice of Extension of Time issued March 16, 2001, the Public Service Commission of the State of New York (NYPSC) hereby submits its notice of intervention and answer in the above-captioned proceeding.

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BACKGROUND AND SUMMARY

On March 1, 2001, Consolidated Edison Company of New York, Inc. (Con Edison) submitted, pursuant to Section 205, 206 and 309 of the Federal Power Act, a request that the Commission approve revisions to the "Localized Market Power Mitigation Measures Applicable to Sales of Capacity, Energy, and Certain Ancillary Services from Specified Generating Units in New York City" (mitigation measures).[1] The Commission previously approved Con Edison's mitigation measures on September 22, 1998.[2]

Con Edison explains that the need for revising the in-City mitigation measures is to close unanticipated loopholes that allow exploitation of market power in the New York Independent System Operator (NYISO)-administered energy market. According to Con Edison, the mitigation measures are inadequate because they: 1) do not apply to the real-time market; 2) fail to mitigate prices for generation that must be run to meet local reliability requirements; 3) allow unmitigated start-up and minimum generation bids; and 4) do not apply to all generators in New York City (NYC). The NYPSC supports Con Edison's proposal to close these loopholes.

The NYC marketplace is not yet workably competitive at periods of high demand, unlike many other parts of the Northeast. Effective competition is limited by the fact that

[1] Con Edison Filing at 1.
[2] Consolidated Edison Company of New York, Inc., 84 FERC ¶61,287 (1998).

there are only a small number of generators in NYC and the city itself is a load pocket. Transmission constraints limit the transfer of power into NYC. Thus, mitigation measures have always been necessary to protect against market power.

The NYPSC contends that the current in-City mitigation measures are insufficient to perform the job of mitigating load pocket market power in NYC. There have been and continue to be numerous occasions when the NYC transmission interfaces are constrained in real-time, giving in-City generators an opportunity to exert unmitigated market power, since the mitigation measures do not apply to the real-time market.[3] Furthermore, the NYISO's regular use of supplemental resource evaluations to address local reliability needs provides additional opportunities for in-City generators to exert unmitigated market power.[4] There have also been a number of instances where units within NYC, other than those divested by Con Edison, appear to have played a role in contributing to high day-ahead market prices in the NYC load zone because of the

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[3] See http://mis.nyiso.com/public/P-4Alist.htm

[4] A supplemental resource evaluation is a determination of the least cost selection of additional generators, which are to be committed, to meet changed conditions that may cause the original system dispatch to be inadequate to meet load and/or reliability requirements.

failure of the in-City mitigation measures to include these generators under their purview.[5]

Several parties may suggest that revisions to the mitigation measures are not needed given the NYISO's "Market Monitoring Plan" and "Market Mitigation Measures," both of which apply to all generators participating in the NYISO markets, and the automatic 'circuit breaker' mechanism that NYISO staff will implement this summer. However, the proposed circuit breaker assumes that the market is functioning in a competitive manner the majority of the time and at limited times a generator may attempt to exercise market power. But, NYC's market is not yet functioning as a competitive market.

Various parties may also claim that further mitigation measures are unwarranted because they will deter construction of new generation in NYC. This argument lacks merit because bids by newer generators, even when mitigated to equal their marginal costs, still yield high prices, due to the high costs of older existing units that often set the clearing prices. Furthermore, in-City generators receive lucrative payments for simply providing installed capacity. These payments were designed to exceed the level needed to attract new entrants. Currently,

[5] Due to confidentiality requirements, we are unable to provide specific information.

there are numerous applications at various stages of review to construct electric generating units within NYC.[6]

Finally, the Con Edison in-City mitigation measures need to be revised to reflect approved changes in the NYISO's tariff regarding the Installed Capacity Auction process. While the Commission approved the NYISO tariff revisions, the Commission did not direct the Con Edison or the NYISO to conform the mitigation measures to the Installed Capacity Auction requirements. Thus, the mitigation measures should be amended to be consistent with the NYISO's current tariff provisions.

I. Amendments to the Mitigation Measures Are Needed to Close Loopholes Which Allow Generators to Exert Market Power in NYC's Uncompetitive Market

Upon divestiture of Con Edison's generation resources in 1998, the New York City market was left with only four major players. It was agreed, at that time, that four was an insufficient number of competing sellers to yield a competitive market during times in which the New York City load pocket becomes separated from the rest of the United States by transmission constraints. Furthermore, even fewer competitors were available in the smaller load pockets within New York City. As a result, the NYPSC required in-City mitigation measures as a condition of Con Edison's divestiture, which the Commission

[6] There are currently seven applications to construct electric generating units undergoing review in NYC.

subsequently adopted as a necessary tool to protect consumers from market power during constrained periods.

The NYPSC's strategy has been to ensure the deployment of mitigation measures to protect customers in the short term, while pursuing long-term policies that will facilitate new entry of generation into the market so that competition will flourish and the mitigation measures can be removed.[7] However, the same market power conditions that existed at the time of Con Edison's divestiture are present today.

Absent sufficient new generation owners, mitigation measures are needed to protect consumers in New York City from market power and unjust and unreasonable rates, at least in the short term. Until such time as new entry yields a competitive environment, the mitigation measures must remain in place, and any unintended loopholes in them must be closed via improvements of the type that Con Edison has proposed.

A. The Mitigation Measures Should Apply in the Real-Time Market

A competitive real-time market is essential to a competitive market. Prior to trading in the NYISO's real-time market, buyers and sellers may enter into contracts in the

[7] The NYPSC has been working to establish demand side bidding and load curtailment programs. In addition, the New York State Board on Electric Generation Siting and the Environment (Siting Board) has approved two applications to construct electric generating units, totaling 1,880 MWs. Another five applications, totaling 3,460 MWs, are currently pending before

forward market or may trade in the NYISO's day-ahead market for energy. For the energy market to function efficiently, both the day-ahead and real-time markets must produce competitive prices. In the forward or day-ahead markets, a buyer or seller can choose to wait for the real-time market to finalize its purchase or sale. If the players are confident that the real-time market produces fair, competitive outcomes, then this reliance on a real-time market as a backstop for all the other markets will function, as it should. However, generators who sell energy into the NYISO-administered real-time market in NYC are not subject to the mitigation measures.

Consequently, generators' bids go unmitigated and are limited only by the $1,000/MWh bid cap that the Commission previously approved. For example, a generator's bid into the day-ahead market, which has been rejected, may subsequently be increased in the real-time market. This allows generators to exert market power by economically withholding their capacity in the day-ahead market to increase prices in the real-time market and then submitting increased bids in the real-time market. Furthermore, the potential for exercise of market power is exacerbated in the real-time market, where there are fewer competitors that can start units quickly or have excess capacity. Thus, we agree with Con Edison's conclusion that mitigation measures should apply to the real-time market to

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the Siting Board. In addition, 14 applications, totaling 8,397 MWs, are under review at various stages of the siting process.

correct for the fundamental problem that there are not enough sellers in the market to protect against real-time market power.

B. The Mitigation Measures Should Apply to Generation Required for Reliability Purposes

Currently, the NYISO only applies the mitigation measures to generators that are required in the day-ahead market to meet Con Edison's second contingency reliability criteria for its system as a whole.[8] The measures are not applied when the generation is required for any other local reliability requirements, such as maintaining second contingency reliability within one of the various NYC load pockets or for meeting reliability needs that arise in the real-time market. As Con Edison explains, this is because second contingency reliability "is the only local reliability rule that is taken into account in the NYISO's day-ahead unit commitment mechanism." Consequently, once a generator is called upon to meet reliability requirements, they are aware that they are needed for reliability and can raise their bids in the real-time market above competitive levels. Thus, the mitigation measures should apply to all generation that must be operated to ensure reliability.

[8] The second contingency reliability criteria are the ability of the system to withstand the loss of the two largest supply sources without a loss of load.

C. The Mitigation Measures Should Apply to Start-Up and Minimum Generation Bids

The current mitigation measures apply to incremental energy bids, but do not apply to start-up and minimum generation bids. The absence of a competitive market allows generators to artificially raise these bids as a way of increasing the commitment portion of their bid. This practice can be used by generators to either "extract higher payments from the NYISO under the Bid Production Cost Guarantee or to economically withdraw a unit and raise the price of in-City energy."[9] As a result, the mitigation measures should be revised to mitigate start-up and minimum generation bids.

D. The Mitigation Measures Should Apply to All In-City Generators

Con Edison's proposal to apply the mitigation measures to all in-City generators is reasonable. Because the mitigation measures only apply to Con Edison's divested generators, one unmitigated unit may set the market clearing price for all units in this transmission constrained load pocket. New units and the New York Power Authority's units in NYC have opportunities to drive up prices as do the divested units, and therefore to protect the market from "unjust and unreasonable prices,"[10] in-City mitigation should apply to all generators.

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[9] Con Edison Filing at 16.

[10] Pursuant to Section 205 of the Federal Power Act (16 U.S.C. § 824d), "[a]ll rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the

II. The Circuit Breaker Will Not Obviate the Need for Additional Mitigation Measures

Various parties may claim that there is no need for additional mitigation measures if the NYISO's proposed circuit breaker is implemented. However, the circuit breaker is aimed at preventing the most flagrant behavior. For example, the circuit breaker would only be triggered when the price exceeds $150 per megawatt-hour and a bid is $100 above its reference price and the market price in increased by $100. These three limitations will permit a market, which is not workably competitive, to regularly yields prices that are $99 or more above the competitive market level. A circuit breaker would simply prevent the most egregious market power attempts within NYC while routinely allowing significant price premiums from market power to harm NYC consumers. Thus, the mitigation measures need to be revised, notwithstanding the proposed circuit breaker.

III. Revising the Mitigation Measures Will Not Have a Negative Impact on the Entry of New Generation in New York City

New York City currently relies on a number of generating plants that are old and inefficient. These plants have running costs that are dramatically higher than the state-

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Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful." See also, Farmers Union Cent. Exch., Inc. v. FERC, 734 F.2d 1486 (D.C.

of-the-art facilities that are proposed. Whenever the NYC market relies on these inefficient plants, the market-clearing price in New York rises to the high cost at which these plants run. Consequently, so long as NYC lacks enough excess capacity to render its old and inefficient plants completely unneeded, the new entrants can expect to receive prices in the energy market that are well above their running costs. At the point that there are enough new entrants to drive the old and inefficient plants out of the market, mitigation measures may be unnecessary.

Moreover, NYC's locational installed capacity (ICAP) market provides incentives to construct new generation, even if mitigation measures are in place. [11] The installed capacity market was designed to provide a revenue stream as an incentive to build new generators. Currently, the ICAP market is trading at the very high price of roughly $105 per kilowatt per year. With this market, a generator can enter and receive a substantial revenue stream even if it sells no energy at all. As long as the relationship between NYC demand and supply is roughly in equilibrium, the ICAP market should continue to provide substantial revenue streams for generators that locate

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Cir. 1984) (holding that the Federal Power Act requires market prices to be just and reasonable).

[11] The mitigation measures simply induce bidding behavior that mimics that of a competitive market (i.e. bids that roughly equal a unit's marginal costs in the energy and ancillary services markets).

in NYC. Currently, a large number of new developers have applied to build electric generating plants in New York City.[12]

IV. The Mitigation Measures Need to be Revised to Reflect the Installed Capacity Auction Process in the NYISO Tariff

The Commission previously approved a NYISO tariff revision regarding the ICAP Auction process. However, the Commission did not direct the NYISO or Con Edison to change the language contained in the mitigation measures referring to such process. Con Edison's filing requests that the mitigation measures provide that "[t]he NYISO will charge LSEs that procure Installed Capacity through the auction the weighted average price of those generators that receive the market clearing price established through the auction and those of the Subject generators that receive the Capacity Reference Price."[13] This provision should be replaced by section ___ of the NYISO's tariff that was approved by the Commission on **[Keller - date & section]**. Market Administration and Control Area Services Tariff-original sheet 148 issued 1/16/01.

CONCLUSION

For the reasons discussed above, the Commission should approve Con Edison's revisions to the mitigation measures. That will close the loopholes, which allow exploitation of market power in the NYC load pocket. Despite the NYISO's proposed

[12] There are seven applications under various stages of review to construct electric generating units within NYC.

circuit breaker, the revisions are needed. Furthermore, the NYC market does not need prices that are inflated by the unmitigated exercise of market power in order to attract new entrants. Finally, the Commission should amend the mitigation measures to include the current ICAP auction process in the NYISO's tariff.

Respectfully Submitted,

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[13] Con Edison Filing at Attachment A, Original Sheet Nos. 5 and 6.