

112 FERC ¶ 61, 302
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Nora Mead Brownell, and Suedeen G. Kelly.

ISO New England Inc. and
New England Power Pool

Docket No. ER05-1353-000

ORDER ACCEPTING AMENDMENTS TO THE REAL-TIME OPERATING
RESERVE CREDIT ELIGIBILITY RULES AND GRANTING WAIVER

(Issued September 16, 2005)

1. On August 16, 2005, ISO New England Inc. (ISO-NE or the ISO) and the New England Power Pool (NEPOOL) jointly submitted amendments to Market Rule 1 (section III of ISO-NE's tariff) and Appendix F thereto, to implement changes to the Real-Time Operating Reserve Credit eligibility rules. ISO-NE and NEPOOL also requested waiver of the Commission's 60-day prior notice requirement.¹ In this order, we will grant ISO-NE's and NEPOOL's request for waiver and accept the proposed tariff revisions for filing, effective October 1, 2005, as requested.

I. Background

2. On June 6, 2005, the Commission accepted a package of three market modifications jointly submitted by ISO-NE and NEPOOL to implement Phase I of the Ancillary Services Market project (ASM Phase I), to be effective October 1, 2005.² One of the market modifications will provide generating resources greater flexibility to adjust their supply offers during the re-offer period that occurs after the day-ahead energy market closes. Currently, only generators that fail to clear the day-ahead energy market may submit revisions to their supply offers during the re-offer period. When ASM Phase I takes effect, generators that clear the day-ahead energy market will also be able to revise their supply offers during the re-offer period.

¹ See 16 U.S.C. § 824d (2000).

² *ISO New England Inc. and New England Power Pool*, 111 FERC ¶ 61,364 (2005).

3. ISO-NE states that while developing systems to implement ASM Phase I, it discovered that the existing Real-Time Operating Reserve Credit eligibility rules could provide generators the opportunity to unduly increase their Real-Time Operating Reserve Credits when ASM Phase I takes effect. Under Market Rule 1, an eligible generating resource may receive Real-Time Operating Reserve Credits for unscheduled energy, which currently includes energy produced during start-up hours³ and shutdown hours.⁴ Currently, a generating resource clears the day-ahead energy market based on its supply offer, which includes start-up costs, no-load costs and incremental energy offers, along with several physical operating parameters. ISO-NE and NEPOOL explain that because the supply offer does not include start-up or shutdown profiles, ISO software does not separately and explicitly recognize the ramping required by a resource to achieve the energy output level accepted in the day-ahead energy market.

4. ISO-NE and NEPOOL also explain that the Real-Time Operating Reserve rule changes filed with ASM Phase I will make all energy produced in excess of the amount scheduled in the day-ahead energy market eligible for Real-Time Operating Reserve Credits, including energy produced by a generating resource starting up or shutting down. ISO-NE and NEPOOL state that in accordance with the ASM Phase I rule changes, a generation resource that clears the day-ahead energy market could submit a significantly higher incremental energy offer during the re-offer period, which would change its real-time energy offer amount for the start-up and shutdown hours. ISO-NE and NEPOOL also state that a significant increase in the resource's Real-Time Operating Reserve Credits would in turn occur because the credit is the difference between this significantly higher re-offer amount for incremental energy and the Real-Time value (*i.e.*, the locational marginal pricing). ISO-NE estimates that this could result in payments to a single unit as high as several hundred thousand dollars per day.⁵

5. ISO-NE and NEPOOL propose to remove the potential for this substantial escalation in payments by making generating resources ineligible to receive Real-Time Operating Reserve Credits attributable to real-time start-up and shutdown hours. The proposed tariff revisions exclude both the incremental energy costs and the revenues

³ The hours leading up to the first hour in which a generating resource produces scheduled energy.

⁴ The hours following the last hour in which the generating resource produces scheduled energy.

⁵ See Cases 3 and 4 in Attachment 3 to this filing. These cases demonstrate how a generating resource that clears the day-ahead energy market could use the re-offer period to increase its incremental energy offer to \$300/MWh or \$900/MWh. This would result in a generating resource receiving Real-Time Operating Reserve Credits of over \$100,000 and \$325,000, respectively.

associated with start-up and shutdown hours from the Real-Time Operating Reserve calculation. ISO-NE and NEPOOL assert that the proposed changes will not impose an unjust or unreasonable risk on generators. ISO-NE and NEPOOL contend that the proposed changes will provide incentives for generating resources to start-up and shutdown as quickly as possible, with resulting cost savings and efficiency gains for consumers and generators. Additionally, ISO-NE and NEPOOL argue that the changes will encourage generators to provide the most accurate start-up costs for use in day-ahead energy market supply offers. ISO-NE and NEPOOL assert that this will enhance efficiency by encouraging generating resources to include start-up and shutdown costs in their supply offers, thereby sending the market a more accurate signal as to each resource's true cost, rather than relying on Real-Time Operating Reserve Credit payments as the source of compensation. ISO-NE and NEPOOL believe that operational efficiency will be improved by discouraging generating resources from providing excessive unscheduled energy in order to increase Real-Time Operating Reserve Credits.

6. ISO-NE and NEPOOL state that eliminating Operating Reserve Credit treatment will not deprive generators of the opportunity to recover their costs; they will continue to be paid the appropriate clearing prices for the energy they produce, and generators will be able to recover revenues through a combination of start-up and no-load offers, as well as energy payments. Additionally, ISO-NE and NEPOOL state that energy produced during start-up and shutdown hours will still be eligible to receive Real-Time LMP and that generators may reflect costs associated with start-up and shutdown in the start-up fees included in their supply offers, which they may recover as part of the Day-Ahead Operating Reserve Credits calculated under section 3.2.3(b) of Market Rule 1. Further, ISO-NE explains that typically five or six generating resources a day receive Real-Time Operating Reserve Credits from start-up and shutdown hours, resulting in daily payments of approximately \$30,000 to \$40,000. Thus, ISO-NE expects few generating resources will be affected by the proposed changes.

7. ISO-NE advises that three alternatives to this proposal were suggested: (1) allow only generating resources with day-ahead schedules to be ineligible to receive Real-Time Operating Reserve Credits for real-time start-up and shutdown hours; (2) rely on the Internal Market Monitoring Unit (IMMU) to mitigate inappropriate incremental energy offers submitted in the re-offer period; and (3) allow generating resources to include start-up and shutdown profiles in their day-ahead energy market supply offers. However, ISO-NE states that it believes the proposal it filed is superior.⁶ The NEPOOL Markets

⁶ We will discuss the first alternative more fully in the discussion section. The other alternative proposals proposed as part of the stakeholder process but ultimately rejected are: (1) an option that would rely on the Independent Market Monitor to determine whether an incremental energy offer is just and reasonable; and (2) an option that is inconsistent with market principles and would require costly software design changes that would delay the start of the ASM Phase I on October 1, 2005.

Committee approved the proposed changes in this filing by a vote of 76.78 percent in favor at its July 25-26, 2005 meeting. The NEPOOL Participants Committee approved the changes with a vote of 83.93 percent in favor at its August 5, 2005 meeting.

8. ISO-NE and NEPOOL request that the revised tariff sheets be accepted effective October 1, 2005, to be effective when ASM Phase I takes effect, to eliminate excessive and unreasonable financial exposure to New England customers. ISO-NE requests that the Commission issue an order in this proceeding by September 15, 2005, so ISO-NE can issue the required two-weeks notice to allow ASM Phase I to be implemented by October 1, 2005.

II. Notice of Filings and Responsive Pleadings

9. Notice of the filing in Docket No. ER05-1353 was published in the *Federal Register*, 70 Fed. Reg. 50,313 (2005), with protests or interventions due on or before September 6, 2005. The Northeast Utilities (NU) Service Company, on behalf of the NU Companies and Select Energy, Inc. filed a timely motion to intervene. A timely motion to intervene and comments were filed by Mirant Americas Energy Marketing, LP, Mirant New England, LLC, Mirant Canal, LLC, and Mirant Kendall, LLC (the Mirant Parties). Timely motions to intervene and protests were filed by ANP Funding I, LLC (ANP Funding); NRG Power Marketing, Inc., Connecticut Jet Power LLC, Devon Power LLC, Middletown Power LLC, Montville Power LLC, Norwalk Power LLC, and Somerset Power LLC (the NRG Companies) and Calpine Corporation (Calpine). ISO-NE filed an answer to the protests of ANP Funding, the NRG Companies, and Calpine.

10. ANP Funding, NRG Companies and Calpine argue that ISO-NE's and NEPOOL's proposal goes beyond what is needed to solve the potential problem. The parties contend that it is unfair to deny all generating resources Real-Time Operating Reserve Credits during start-up and shutdown hours.

11. Instead, ANP Funding, NRG Companies and Calpine support the first alternative ISO-NE mentioned, in which only a generating resource with a Day-Ahead schedule would be ineligible to receive Real-Time Operating Reserve Credits for Real-Time start-up and shutdown hours. The NRG Companies and Calpine note that this alternative was supported by 57.04 percent of the NEPOOL Markets Committee. The NRG Companies and Calpine assert that this alternative would eliminate the potential for a substantial escalation in payments when ASM Phase I goes into effect, and it would also allow generating resources to recover their costs when they are scheduled only in the real-time market, or scheduled in the day-ahead market but do not increase their offers during the re-offer period.

12. ANP Funding, Mirant Companies, NRG Companies and Calpine contend that ISO-NE's and NEPOOL's statement that generators would still be able to recover appropriate revenues through a combination of start-up and no-load offers is not feasible because start-up and no-load offers can only be updated twice per month. ANP Funding, NRG Companies and Calpine state that it is especially difficult for generating resources to predict start-up and no-load offers during periods of high price volatility, and if there is a sudden price change, generating resources would have no opportunity to adjust their offers to receive fair and adequate compensation for service. The Mirant Companies, NRG Companies and Calpine state that generating resources would need the ability to change their start-up and no-load bids more often to ensure that generating resources are receiving Real-Time Operating Reserve Credits that reflect the generating resources' full cost of providing service. The Mirant Companies suggest that ISO-NE implement rules permitting daily modifications of start-up and no-load bids as quickly as possible.

13. ANP Funding, the NRG Companies and Calpine disagree that ISO-NE's and NEPOOL's proposal would provide incentives for generating resources to start-up and shutdown as quickly as possible. ANP Funding argues that ISO-NE can accomplish this by denying Real-Time Operating Reserve Credits to generating resources that start-up earlier than necessary or refuse to shutdown in a timely manner. The NRG Companies and Calpine contend that ISO-NE has failed to demonstrate that generating resources need incentives to start-up or shutdown as quickly as possible.

14. ANP Funding, NRG Companies and Calpine also disagree that ISO-NE's proposed changes will result in more accurate start-up costs, and thus send the market more accurate price signals. ANP Funding states that New England is a bid-based market, not a cost-based market, and a generating resource should be allowed to choose a strategy of bidding a low start-up cost and rolling a portion of those costs into its energy offers. The NRG Companies and Calpine contend that generating resources that desire to be committed in the day-ahead market already have incentives to offer the most competitive combination of start-up, no-load and energy offers. The NRG Companies and Calpine contend that ISO-NE's and NEPOOL's proposal would actually produce new costs and risks in the market because of the inflexibility of start-up and no-load offers.

15. The NRG Companies and Calpine request that the Commission direct ISO-NE and NEPOOL to revise Market Rule 1 and Appendix F only to the extent necessary to make generating resources cleared in the day-ahead market that increase their offers in the re-offer period ineligible to receive Real-Time Operating Reserve Credits for Real-Time start-up and shutdown hours.

III. Discussion

16. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the notices of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

17. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2005), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept ISO-NE's answer because it has provided useful information for deciding this case.

18. Concerning ISO-NE's and NEPOOL's request for waiver of the Commission's 60-day prior notice requirement, the Commission finds that ISO-NE's and NEPOOL's claim that customers of New England may face unreasonable financial exposure unless the market rule change proposed in the instant filing is implemented by October 1, 2005, has provided the Commission with good reason to grant ISO-NE and NEPOOL's request for waiver of the Commission's 60-day prior notice requirement.⁷

19. Under ASM Phase I, generators may revise their supply offers for incremental energy during the re-offer period. In other words, generators may continue to submit supply offers prior to the day-ahead market closing or during the re-offer period. This extension of the opportunity to revise supply offers to generators that have cleared the day-ahead market will allow generating resources to better reflect real-time costs.⁸ But because the Operating Reserve Credit methodology includes real-time start-up and shutdown hours in the Real-Time Operating Reserve calculation, revised supply offers could produce unwarranted Operating Reserve Credits in real-time of several hundred thousand dollars per day.

20. Given the potential exposure to the market, the Commission is persuaded by ISO-NE's and NEPOOL's argument that if a generator that clears in the day-ahead market significantly deviates its offer in the re-offer period from the parameters it used to originally clear the unit that generator could receive unwarranted payments. As a result, the Commission also finds that ISO-NE's and NEPOOL's proposal to make generating resources ineligible to receive Real-Time Operating Reserve Credits attributable to real-time start-up and shutdown hours is just and reasonable.

⁷ *Central Hudson Gas & Electric Corporation*, 60 FERC ¶ 61,106, *reh'g denied*, 61 FERC ¶ 61,089 (1992).

⁸ *See ISO New England, Inc. and New England Power Pool*, 111 FERC ¶ 61,364 (2005).

21. ISO-NE's and NEPOOL's proposal to make all generating resources ineligible to receive Real-Time Operating Reserve Credits attributable to Real-Time start-up and shutdown hours eliminates the potential for gaming. In the alternative supported by ANP Funding, NRG Companies and Calpine, only a generating resource with a Day-Ahead schedule would be ineligible to receive Real-Time Operating Reserve Credits for Real-Time start-up and shutdown hours. Because delisted units are exempt from the requirement to offer generation into the day-ahead market but may continue to do so, generators could circumvent this alternative by simply de-listing. In ISO-NE, existing supply offers of fully de-listed resources are carried forward until changed or cancelled by the market participant. These energy supply offers are not automatically removed from the ISO-NE market system.⁹ Therefore, a generating resource with a day-ahead schedule could potentially be eligible to receive Real-Time Operating Reserve Credits, absent other market rule changes.

22. Under ISO-NE's and NEPOOL's proposal to eliminate start-up and shutdown hours from Real-Time Operating Reserve Credits, de-list is not a factor. Because the re-offer modifications will further enhance flexibility and transparency, will be beneficial to ISO-NE's markets and have broad stakeholder support, we will accept the proposed market rule changes. We note that resources that clear the day-ahead market are compensated for their start-up costs, if eligible, through a Day-Ahead Operating Reserve Credit.¹⁰

23. We also note ISO-NE's commitment to work with stakeholders to consider additional start-up and no-load offer flexibility. Currently, market participants can only change start-up and no-load bids twice a month. ISO-NE explains that due to other market improving priorities reflected in the Wholesale Markets Plans, ISO-NE and stakeholders cannot formulate such flexibility immediately. Therefore, we encourage ISO-NE to continue exploring increasing bidding flexibility as it already committed to do.¹¹

⁹ See ISO New England Installed Capacity Manual-20 at § 3.9.2 Rights and Obligations of De-listed Resources. In addition, section III – Market Rule 1 -Installed Capacity – § 8.3.4A.

¹⁰ See Section III – Market Rule 1- Appendix F- Operating Reserve Accounting § III.F.2.1. “Credits for Generating Resources.” In addition, section III – Market Rule 1 – Appendix F – Operating Reserve Accounting § F.2.1.17 “Addition of Hourly Shortfall Payments.”

¹¹ See ISO-NE's and NEPOOL's transmittal letter filed in Docket No. ER05-1353-000 on August 16, 2005 at page 7.

24. With regard to the protests that ISO-NE's and NEPOOL's proposal does not result in more accurate start-up costs, and thus send the market more accurate price signals, we agree with ISO-NE and NEPOOL that the generators will have the incentive to provide the most accurate start-up costs for use in the day-ahead market rather than rely upon Operating Reserve Credits to compensate for start-up costs. . The market rule proposal would eliminate all Real-Time Operating Reserve Credits attributable to real-time start-up and shutdown MWh. As a result, the proposed market rule would encourage generators to include their true operating expenses that include start-up and shutdown costs in their day-ahead energy bids instead of relying on non-market payments such as Real-Time Operating Reserve credits. For example, ANP Funding states in its protest that, "If a generator chooses a strategy of bidding a low start-up cost and rolling a portion of those costs into its energy offers it is entitled to do so." However, the strategy ANP Funding proposes fosters market distortions, because its strategy does not provide the most accurate start-up costs for use in its day-ahead energy market supply offers. As a result, in the real-time energy market, market participants would have to pay uplift costs in the form of Real-Time Operating Reserve Credits, because a resource like ANP Funding's did not include the hour of ramping up to its low operating limit or the hour of ramping down from its low limit to zero in its day-ahead energy market supply offer.

The Commission orders:

(A) ISO-NE's and NEPOOL's proposed tariff revisions are hereby accepted for filing, to become effective October 1, 2005, as discussed in the body of this order.

(B) ISO-NE's and NEPOOL's request for waiver of the Commission's 60-day prior notice requirement is hereby granted, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.