

119 FERC ¶ 61,239  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;  
Sudeen G. Kelly, Marc Spitzer,  
Philip D. Moeller, and Jon Wellinghoff.

ISO New England, Inc.

Docket No. ER07-547-000

ORDER ACCEPTING MARKET RULES

(Issued June 5, 2007)

1. In this order, the Commission accepts the revisions to the market rules proposed by ISO New England, Inc. (ISO-NE) to implement New England's Forward Capacity Market (FCM), effective June 6, 2007.

**I. Background**

**A. New England's Forward Capacity Market**

2. As discussed in prior orders in this proceeding,<sup>1</sup> ISO-NE has, as a means of ensuring reliability, historically required load-serving entities to procure a specified amount of installed capacity (ICAP) based on their peak loads plus a reserve margin.<sup>2</sup> Beginning in 1998, ISO-NE began operating a bid-based market for ICAP.<sup>3</sup> In 2000, as the region began to develop wholesale power markets and utilize market-based rates, the Commission began to identify flaws in the ICAP market, and it allowed ISO-NE to

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<sup>1</sup> *Devon Power LLC*, 111 FERC ¶ 63,063 (2005) (Initial Decision); *Devon Power LLC*, 115 FERC ¶ 61,340 (2006) (FCM Order), *order on reh'g*, 117 FERC ¶ 61,133 (2006) (FCM Rehearing Order).

<sup>2</sup> Before the establishment of ISO-NE, the New England Power Pool (NEPOOL) similarly imposed an ICAP requirement.

<sup>3</sup> See *New England Power Pool*, 83 FERC ¶ 61,045 at 61,263 (1998).

replace the ICAP auction mechanism with an administratively-determined ICAP deficiency charge. The Commission agreed with ISO-NE that the auction “can produce inflated prices unrelated to the actual harm caused by ICAP deficiencies.”<sup>4</sup> In 2002, the Commission addressed further deficiencies in New England’s ICAP market, this time noting the lack of a locational element, and stating that it “believes that location is an important aspect of ensuring optimal investment in resources.”<sup>5</sup> As part of this overall process, certain generators sought cost-of-service Reliability-Must-Run (RMR) contracts. In a series of orders,<sup>6</sup> the Commission rejected the majority of the RMR agreements, out of concern about the effect widespread use of such contracts could have on the competitive market. The Commission directed the ISO “to file no later than March 1, 2004 for implementation no later than June 1, 2004, a mechanism that implements location or deliverability requirements in the ICAP or resource adequacy market. . . so that capacity within [congested areas] may be appropriately compensated for reliability.”<sup>7</sup> Accordingly, on March 1, 2004, the ISO submitted a filing seeking to implement a locational ICAP market in New England by June 1, 2004.<sup>8</sup>

3. After a hearing before an Administrative Law Judge and extensive further proceedings, the parties arrived at a settlement with regard to that filing (Settlement Agreement), which the Commission substantially approved in the FCM Order and FCM Rehearing Order.

### **B. The Instant Filing**

4. On February 15, 2007, ISO-NE filed the required market rule revisions, pursuant to section 205 of the Federal Power Act (FPA), 16 U.S.C. § 824d (2000), as required by

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<sup>4</sup> *ISO New England, Inc.*, 91 FERC ¶ 61,311 at 62,081 (2000).

<sup>5</sup> *New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287 at 62,278 (2002).

<sup>6</sup> *Devon Power LLC*, 102 FERC ¶ 61,314 (2003); *Devon Power LLC*, 103 FERC ¶ 61,082 (2003) ; *Devon Power Company*, 104 FERC ¶ 61,123 (2003); *PPL Wallingford Energy LLC*, 103 FERC ¶ 61,185 (2003); *PPL Wallingford Energy LLC*, 105 FERC ¶ 61,324 (2003).

<sup>7</sup> *Devon Power LLC*, 103 FERC P61,082 at P 37 (2003)

<sup>8</sup> *Id.*

the Settlement Agreement. ISO-NE also included an extension of its Load Response Program and changes to its Financial Assurance Policies and Billing Policy.

5. The proposed rules implementing the FCM establish that ISO-NE will conduct an annual auction to procure capacity. This annual auction (Forward Capacity Auction)<sup>9</sup> will be conducted three-plus years in advance of the period during which capacity will actually be supplied.<sup>10</sup> Capacity resources offer their capacity into the Forward Capacity Auction, and subsequent reconfiguration auctions, and, if chosen as capacity providers, commit to provide capacity during the relevant period in the future. With certain exceptions, each capacity provider will receive the clearing price developed through the auction process. Alternatively, capacity resources can choose to de-list from the FCM, either permanently or temporarily, in which case they will not participate in the auction.

6. ISO-NE states that the FCM rules were developed through an extensive stakeholder process.<sup>11</sup> The proposed rules on FCM (as well as the market rule and manual revisions necessary to extend the term of the existing Load Response Program) were supported by the Participants Committee with a vote of 78.74 percent in favor. ISO-NE states that the volume and timing of the instant filing were such that ISO-NE and NEPOOL were unable to file jointly. NEPOOL states in its comments, however, that it fully supports the filing.

7. The proposed rules on FCM in the instant filing are divided into eight sections, all of which are within section III (Market Rule 1) of ISO-NE's tariff. Section III.13.1 establishes the processes through which capacity resources qualify for participation in

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<sup>9</sup> Capitalized terms used but not otherwise defined in this order have the meanings ascribed to them in ISO-NE's Transmission, Markets and Services Tariff (the tariff), the Second Restated New England Power Pool Agreement, and the Participants Agreement. *See* Transmittal, February 15 filing, at 1 fn. 4.

<sup>10</sup> The FCM also entails additional reconfiguration auctions to be conducted in the time between the Forward Capacity Auction and the supply commitment period. For example, the initial Forward Capacity Auction will be held in February 2008 and will procure capacity for the period of June 1, 2010 to May 31, 2011.

<sup>11</sup> According to ISO-NE, formal discussions of the proposed rules on FCM began at the Markets Committee on September 13, 2006 and those discussions continued over the course of 23 meetings, with extensive involvement of the Reliability Committee and state utility regulatory agencies.

Forward Capacity Auctions, and section III.13.2 addresses the mechanics of the Forward Capacity Auction. On April 16, 2007, the Commission issued an order addressing those sections in Docket No. ER07-546-000.<sup>12</sup>

8. This order addresses the remaining sections of III.13, as well as the Financial Assurance and Billing Policies and remaining changes to Market Rule 1 proposed in the February 15 filing.

**1. Changes to Market Rules to implement FCM**

9. In this order, we are accepting the following sections:

- *Section 13.3 – Critical Path Schedule Monitoring.* The Settlement Agreement requires that the sponsor of a proposed new capacity resource provide a critical path schedule to ISO-NE. The schedule must contain sufficient detail to allow ISO-NE to evaluate the feasibility of the project being built and in service no later than the start of the commitment period.<sup>13</sup> The project sponsor is also required to provide continuing reports to ISO-NE as its project is constructed. The proposed rules also specify actions to be taken in the event that a project sponsor is unable to achieve commercial operation by the beginning of the commitment period.
- *Section 13.4 – Reconfiguration Auctions.* After the Forward Capacity Auction, which sets capacity obligations three years ahead of a delivery year, the Settlement Agreement also provides for annual, seasonal and monthly reconfiguration auctions.<sup>14</sup> Reconfiguration auctions provide a mechanism for resources to either acquire or shed capacity supply obligations. Reconfiguration auctions also enable ISO-NE to, among other things, replace capacity from units released from reliability agreements and replace capacity not procured as a result of de-list bids and export bids that are not replaced in the Forward Capacity Auction.<sup>15</sup>

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<sup>12</sup> *ISO New England*, 119 FERC ¶ 61,045 (2007) (April 16 Order).

<sup>13</sup> Settlement Agreement at section 11.II.B.3(b).

<sup>14</sup> Settlement Agreement at section 11.III.M.

<sup>15</sup> Section III.13.4.3.

- *Section 13.5 – Bilateral Contracts in the Forward Capacity Market.* The Settlement Agreement permits bilateral contracting between parties for supply obligations.<sup>16</sup> Any resource accepting a supply obligation pursuant to a bilateral contract will be subject to the qualification requirements of existing or new capacity, as applicable. Parties to a bilateral contract who are transferring a capacity supply obligation must submit their contract to ISO-NE for review. The submittal must include detailed information concerning the physical asset being transferred.<sup>17</sup> ISO-NE will review the submittal to ensure, among other things, that de-listing the previously listed resource does not present reliability issues.
- *Section 13.6 – Rights and Obligations of Capacity Resources.* Section 13.6 outlines the rights and obligations of listed and de-listed capacity resources. ISO-NE states that the obligations differ depending on whether the resource is listed or de-listed. A listed resource is any resource (generating, import, intermittent, or demand resource) that assumes an obligation to supply capacity through a Forward Capacity Auction, a reconfiguration auction, or a bilateral contract. A resource with a capacity supply obligation is “listed” for the duration of its obligation or until it transfers that obligation.<sup>18</sup> In accordance with the Settlement Agreement, the proposed rules require that a generating resource that is obligated to supply capacity (*i.e.*, a listed resource) must offer into both the Day-Ahead and Real-Time energy markets.<sup>19</sup> These energy market offers must reflect the physical operating characteristics of the resource. The proposed rules state that a listed resource may apply to recover its full operational costs during times of extraordinary fuel prices where the recovery of these costs from the market is otherwise precluded by the energy offer cap. Section III.13.6.1.3 of the proposed rules addresses intermittent power resources. Intermittent power resources may submit offers into the Day-Ahead energy market. If selected, such resources are required to submit offers into the Real-Time energy market “consistent with the characteristics of the resource.”<sup>20</sup> Fully listed intermittent power

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<sup>16</sup> Settlement Agreement at section 11.III.P.

<sup>17</sup> Section III.13.5.1.1.2.

<sup>18</sup> For existing resources, the duration of the obligation is one year, corresponding to the commitment period. For new resources, the obligation may be as long as five years.

<sup>19</sup> Settlement Agreement at section 11.IV.A.

<sup>20</sup> Section III.13.6.1.3.1.

resources are subject to auditing, rating, operating data collection, and planned outage requirements.

- *Section 13.7 – Performance, Payments and Charges.* The level of capacity payments paid to capacity resources is tied directly to the availability of those resources. The Settlement Agreement provides for loss of capacity compensation for capacity resources that fail to perform during Shortage Events (periods with a minimum duration of 30 minutes during which there is a shortage of Operating Reserves).<sup>21</sup> The Shortage Event approach is intended to capture hours when capacity resources are determined to be most needed due to conditions on the system. If a resource experiences no Shortage Events during a year, its Availability Score will be 100 percent. In order to be considered available, a resource must meet any of several criteria, such as being on-line and following dispatch instructions from ISO-NE.<sup>22</sup> Section III.13.7.2 addresses payments and charges to resources that have acquired an obligation to supply capacity. The proposed rules also address how excess revenues and Capacity Transfer Rights will be handled. Capacity Transfer Rights are a financial but not a physical right to transfer capacity between capacity zones. ISO-NE will create Capacity Transfer Rights for each interface associated with a capacity zone that has experienced price separation in the Forward Capacity Auction. The proposed rules provide that revenues collected from load serving entities in excess of revenues paid to resources will be paid to the holders of Capacity Transfer Rights.
- *Section 13.8 – Price Reporting and Finality.* Section 13.8 states that, no later than 90 days prior to the first day of the Forward Capacity Auction, ISO-NE will make an informational filing with the Commission detailing several determinations it has made and that will be incorporated into the Forward Capacity Auction. Among the determinations are: (1) the capacity zones that will be modeled into the Forward Capacity Auction; (2) transmission interface limits used in selecting capacity zones; (3) the existing and proposed transmission lines assumed to be in service by the start of the commitment period; and (4) those resources accepted and rejected for participation in the Forward Capacity Auction. Section III.13.8.2 states that as soon as practicable after completion of the Forward Capacity Auction, ISO-NE will file the results with the Commission pursuant to Section 205 of the FPA. Included therein

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<sup>21</sup> Settlement Agreement at section 11.V.C.

<sup>22</sup> Section III.13.7.1.1.3.

will be the final set of capacity zones, the clearing prices in each, and a list of which resources received capacity supply obligations.

## 2. Extension of Load Response Program

10. The instant filing also contains changes to ISO-NE's existing tariff provisions that govern the existing Load Response Program (Appendix E to Market Rule 1). Appendix E currently states that the existing Load Response Program will terminate on February 29, 2008.<sup>23</sup> However, ISO-NE states that this date is well before the beginning of the first commitment period under the FCM (June 1, 2010). ISO-NE proposes to extend the termination date to May 31, 2010 in order to coordinate between the existing Load Response Program and the Settlement Agreement. This extension will allow Real-Time Demand Response resources to continue participating in wholesale electricity markets on an uninterrupted basis until May 2010.

11. The proposed changes to Appendix E also contain a provision that would require further study and consultation with NEPOOL stakeholders and state regulatory agencies regarding the implementation of load response programs for energy-based resources beyond May 31, 2010. In the event that stakeholders determine that an energy-based load response program should be implemented beyond May 31, 2010, ISO-NE would make an appropriate filing with the Commission.

12. The proposal to extend the existing Load Response Programs through May 31, 2010, was considered and adopted by the Participants Committee, along with the market rule revisions to implement the FCM with a vote of 78.74 percent in favor.

## 3. Changes to the Financial Assurance Policies and Billing Policy

13. In addition to the proposed market rules changes, ISO-NE has submitted changes to its financial assurance policies and associated billing policy. ISO-NE states that the proposed amendments are needed to help facilitate implementation of FCM through conforming changes to the policies, and to make needed housekeeping changes. According to ISO-NE, these proposed changes are intended to help implement the

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<sup>23</sup> Attachment E to Market Rule 1 (1st Rev Sheet No. 7903) ("the Load Response Program will be effective from the Operations Date through February 29, 2008"). *New England Power Pool and ISO New England, Inc.*, 111 FERC ¶ 61,604 (2005).

financial assurance requirements of the Settlement Agreement and make the necessary changes to the billing policy in order to implement the FCM. ISO-NE has submitted changes to the separate Financial Assurance Policies for market participants, transmission customers, customers participating in the Financial Transmission Rights market, and customers participating in the Demand Response Program.

14. ISO-NE states that the proposed Financial Assurance Policies establish reasonable financial assurance and credit review procedures and provide assurance that payments owed will be received as and when due. The amendments proposed in the instant filing were developed following the approval of the Settlement Agreement and were presented several times to the Budget and Finance Subcommittee, the Reliability Committee and the Markets Committee. The Budget and Finance Subcommittee recommended that the Participants Committee support the proposed changes, and they were approved unanimously by a February 8, 2007 vote of the NEPOOL Participants Committee.

#### **4. Effective Date**

15. In its filing, ISO-NE requested that the balance of the proposed rules on FCM be made effective on June 15, 2007, and, with notice, for the changes to the Tariff's Financial Assurance and Billing Policies, to be made effective no earlier than June 1, 2007. Subsequently, on May 4, 2007, ISO-NE submitted a letter notifying the Commission that it would complete the development of software to implement the FCM market rules as of June 6, 2007 and requested an effective date of June 6, 2007 for those provisions not previously accepted in our April 16 Order.

#### **C. Interventions, Comments and Protests**

16. Notice of the filing, and the Commission's determination to consider the above-stated portions of it in this docket, was published in the Federal Register, with interventions and protests due on or before March 15, 2007.<sup>24</sup>

17. Timely motions to intervene, notices of intervention, protests or comments were filed by the NEPOOL Participants Committee, NSTAR Electric and Gas Corporation (NSTAR), EnerNOC, Brookfield Energy Marketing, Inc. (Brookfield), NRG Companies (NRG), the Massachusetts Municipal Wholesale Electric Company and Connecticut Municipal Electric Energy Cooperative (Public Systems), the Connecticut Department of

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<sup>24</sup> 72 Fed. Reg. 8368 (2007).

Public Utility Control (CT DPUC), FirstLight Parties (FirstLight), Casco Bay Energy Co. (Casco Bay), and Capacity Suppliers.<sup>25</sup>

18. Timely motions to intervene and notices of intervention were filed by International Power America, Con Edison Energy, Inc.; Fitchburg Gas and Electric Light Co., IRH Management Committee, J. Aron and Co., Pinpoint Power LLC, Dominion Resources Services, Inc., New Hampshire Public Utilities Commission, the New England Conference of Public Utility Commissioners, United Illuminating Co., Massachusetts Attorney General, Massachusetts Department of Telecommunications and Energy, Energy Management and Cape Wind Associates, H.Q. Energy Services (U.S.), Inc., PPL Companies, Exelon Corporation, Northeast Utilities Service Company, Bridgeport Energy Co., Milford Power Co., Conservation Services Group, Vermont Department of Public Service and Vermont Public Service Board. Motions to intervene out of time were filed by National Grid USA and the BG Entities.

19. ISO-NE filed a motion for leave to answer the protests, and answers. Casco Bay filed an answer to ISO-NE's answer.

## **II. Procedural Issues**

20. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.214 (2006)), the notices of intervention and the timely-filed unopposed motions to intervene serve to make the entities filing them parties to this proceeding. The motions to intervene out-of-time are granted, given the early stage of the proceedings, the parties' interest and the absence of undue prejudice or delay. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2006), prohibits an answer to a protest or an answer unless otherwise ordered by the decisional authority. We will accept ISO-NE's answer to the protests, and Casco Bay's answer to ISO-NE's answer, because they have provided information that assisted us in our decision-making process.

## **III. Discussion**

21. The Commission accepts the proposed rules as filed by ISO-NE, and denies the protests, as follows.

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<sup>25</sup> The Capacity Suppliers are Boston Generating, LLC; FPL Energy, LLC; and the Mirant Parties.

**A. Transferability of Capacity Obligations Resulting from FCM Auctions**

22. As noted above, the proposed rules at section III.13.5 provide that the owner of a resource that has taken on a capacity supply obligation may transfer that obligation to another resource by bilateral contract. The parties to that contract must submit their contract to ISO-NE for review, including information identifying the physical asset that will fulfill the obligation. ISO-NE may reject the bilateral contract, if it finds that the transfer would create reliability problems.

**1. Positions of the Parties**

23. NRG argues that the proposed FCM rules unreasonably limit the transferability of capacity obligations resulting from the FCM auctions, transforming a commodity product based upon a zonal requirement into a potentially resource/location-specific obligation. NRG argues that the Settlement Agreement allows a resource to transfer its obligations to another qualified resource and delist,<sup>26</sup> but the proposed rules contravene this express language. NRG states that the proposed market rules: (i) directly contradict the FCM Settlement; (ii) afford ISO-NE significant discretion in the review of such transfers; and (iii) impinge upon the Commission's exclusive jurisdiction under section 203 of the FPA,<sup>27</sup> and (iv) may result in undue discrimination, in that some resources will be allowed to enter bilateral arrangements while others will be denied.<sup>28</sup>

24. NRG argues that under the proposed rules, bidders would be forced to include a risk premium in their FCM offers to address the contingency that a contract to transfer the capacity obligation will not be allowed, yet section III.13.1.2.3.2.1.3 of the FCM rules

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<sup>26</sup> NRG cites to the Settlement Agreement at section IV(A)(6).

<sup>27</sup> 16 U.S.C. § 824b (2000).

<sup>28</sup> Additionally, NRG raises the following specific concerns: there is no timetable for ISO-NE to complete its review of such transfers, the ISO-NE review process will dramatically restrict the liquidity in the market and perhaps eliminate the secondary capacity market altogether, there is no clear review or timely review process from an adverse ISO-NE determination, ISO-NE can deny a transfer request and effectively hold a specific resource captive for "reliability issues," notwithstanding the fact that a replacement unit will provide identical capacity value, and ISO-NE can use these provisions to backstop its determinations of the proper level of capacity allowing it to potentially lower its determination of the Installed Capacity Requirement.

forbids the use of a risk premium as part of the acceptable components of de-list bids. NRG contends that ISO-NE "cannot have it both ways" -- limiting the ability of a participant to manage its risk through bilateral market sales or purchases of a fungible capacity product, while at the same time denying it the ability to recover the same risk.

25. NRG further argues that the potential for ISO-NE to interfere with, or delay, transfers among qualified capacity resources within the same capacity zone reveals a deficiency in ISO-NE's implementation of the FCM market. As an example, NRG argues that the inability to transfer a capacity obligation between two qualified suppliers within a zone could point to (i) a significant deficiency (either capacity or transmission) for which an appropriate market signal has not been sent; (ii) an understatement of the amount of capacity within the capacity zone required to ensure reliability within the zone; or (iii) the improper sizing of the capacity zone. NRG states that, to the extent any review of a transfer among qualified suppliers within the same zone is rejected, this demonstrates that the services provided by the two suppliers are not the same service, NRG contends that in this situation, the transferring supplier must be providing a premium product, where its "locational capacity" has more value than other capacity suppliers in that same region. Thus, NRG argues, ISO-NE's proposed restrictions will lead to continued reliance on out-of-market arrangements to support the forced participation of resources, a reliance that has historically plagued the New England markets.

26. NRG states that the only transfer obligation should be for a supplier to provide notice to ISO-NE for review of any such transfer. If ISO-NE seeks to prohibit a transfer due to reliability concerns, then NRG argues that ISO-NE should be required to make a section 205 filing with the Commission explaining its reasons for seeking to prohibit the transfer and whether the prohibition would result in undue discrimination. Further, NRG argues that ISO-NE should be required to explain how such a prohibition could be avoided through increased capacity purchases, improved transmission, or otherwise. Finally, NRG requests that the Commission direct ISO-NE to develop pricing rules that would both compensate a resource that was denied the right to transfer its obligation and send signals to the market and transmission owners as to the need for more capacity and/or transmission necessary to resolve the problem.

27. ISO-NE, in its answer, counters that NRG misperceives this market as a commodity market, like a market for sugar or corn, when, in fact, it is a physical market for a set of generating and demand resources that can provide reliable electric service to New England's customers. ISO-NE states that the FCM Settlement contemplates that the

Forward Capacity Auction would procure sufficient capacity to assure reliability as required by the region's Installed Capacity Requirement<sup>29</sup> and that the Forward Capacity Auction will also procure sufficient capacity in each sub-region of New England to assure enough capacity in each of those regions. Thus, ISO-NE states, the outcome of the Forward Capacity Auction should be a set of resources that will assure resource adequacy for the entire region and each sub-region, as well as meet any other relevant reliability concerns. ISO-NE also notes that the Settlement provides it with the ability to reject units that wish to leave but cannot because they are needed for reliability reasons. Thus, ISO-NE asserts, the provision in the Settlement that ISO-NE will review, and has the right to accept, bilateral transactions is not the same thing as a requirement that ISO-NE accept all bilateral transactions: according to ISO-NE, the Settlement's provisions that bilateral contracts "shall be allowed," and ISO-NE may "accept" those contracts,<sup>30</sup> are not equivalent to saying that ISO-NE "must allow" such contracts.

28. In response to NRG's argument that the market design should treat resources that qualify for the Forward Capacity Auction as equally deliverable and interchangeable, ISO-NE states that this argument ignores the crucial fact that there was no price separation in the auction expressly because the auction procured resources to meet reliability requirements. Specifically, ISO-NE states that the absence of price separation in the Forward Capacity Auction does not mean that there is no specific need for capacity in local potentially import-constrained zones, only that there was sufficient capacity in the import-constrained zone that was willing to remain in the auction at the region-wide clearing price.

29. To demonstrate that NRG's request represents flawed logic, ISO-NE introduces a scenario whereby all of NRG's units in Connecticut could clear in the Forward Capacity Auction, and enough other units in Connecticut could stay in the auction so that there would be no price separation in Connecticut. In this scenario, under NRG's proposal, NRG could simply sign a bilateral contract with units in western Massachusetts or Maine

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<sup>29</sup> The Installed Capacity Requirement is a projection of the minimum amount of capacity required to serve load (*i.e.*, peak demand for electricity) reliably in the New England region. It is determined in accordance with existing resource planning reliability criteria. *See ISO New England*, 118 FERC ¶ 61,157 (2007).

<sup>30</sup> ISO-NE answer at 11, *citing* Settlement Agreement at section 11, part III.P and part IV.B.2.

to replace their Connecticut capacity because there would be only one pricing zone: yet, as a result, there would be insufficient capacity in Connecticut. ISO-NE notes that this insufficiency could not be remedied in the reconfiguration auctions because the Settlement does not permit auctions for local zones when there is no price separation in the auction. Thus, in this example, NRG's proposal would result in a failed market.

30. ISO-NE further states that, by participating in the Forward Capacity Auction and clearing in that auction at a price accepted by the resource, each resource is accepting the obligation to provide capacity at a just and reasonable, market-determined rate. ISO-NE argues that if there is a free right to exit the market and renege on an obligation, then the basic bargain of the FCM Settlement has been broken, potentially allowing for gaming as owners of units who think they might be needed for reliability could simply remove their units from the market and wait to be offered some form of reliability agreement at a higher price. In addition, ISO-NE points out that a key component of the bargain struck in the FCM Settlement was that resources that had chosen to de-list would no longer be required to offer into the real-time market; the *quid pro quo* for this change from the existing market was to provide ISO-NE with the ability to review bilateral contracts to assure that reliability was not harmed by the de-listing of resources. Thus, ISO-NE asserts, generators gained the flexibility to avoid the requirement that they offer de-listed resources into the auction, but the trade-off for that flexibility was a restriction on shedding obligations through bilateral contracts or reconfiguration auctions. ISO-NE states that NRG's arguments would overturn this balance, leaving generators with flexibility but providing ISO-NE with no ability to maintain reliability.

31. ISO-NE responds to NRG's argument that suppliers fulfilling local reliability needs are providing an additional service (for which separate compensation would be appropriate). ISO-NE asserts that, in reconfiguration auctions:

Resources may also be prevented from shedding obligations for local reliability reasons, such as providing VAR [reactive power] support. The rejection of these resources for reliability does not imply that these resources should be entitled to additional compensation. They are simply being held to the obligation they undertook in the Forward Capacity Auction. If they are asked to provide additional services, *e.g.* VAR support or regulation, they will be compensated for those services through the appropriate ISO tariff or markets.<sup>31</sup>

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<sup>31</sup> Transmittal letter at 142, cited in ISO-NE answer at 13.

32. ISO-NE also responds to NRG's argument that ISO-NE advises suppliers to include a risk premium in their FCM offers to address the contingency that transferability will not be allowed, yet forbids the use of the risk premium in the proposed market rules (specifically, the acceptable components of de-list bids). ISO-NE asserts that NRG is making an "apples vs. oranges" argument, as the proper cost components of a de-list bid are different from those of an offer into the Forward Capacity Auction: according to ISO-NE, a risk premium associated with assuming a Capacity Supply Obligation is not properly includable in a de-list bid because it is not a going forward cost.

33. In response to NRG's argument that the Commission should require ISO-NE to make a filing with the Commission to prevent a bilateral contract that threatens reliability from going forward, ISO-NE states that the FCM market design depends upon physical assets assuming commitments several years in advance of the Capacity Commitment Period and upon the committed capacity itself being in place to serve load, and the free substitution of resources urged by NRG is incompatible with this design. In ISO-NE's view, to the extent that a market participant disagrees with ISO-NE's reliability determination, that market participant should bear the burden of demonstrating that ISO-NE is in error, and exercise its rights before the Commission under section 206.

34. Finally, in response to NRG's arguments about procedures and timetables for denial of transfers, ISO-NE states that NRG's complaint in this regard is premature. ISO-NE states that, as it acknowledged during the stakeholder process, the timing and the details of the process for submission and review of bilateral contracts will be detailed in the Manuals that remain to be developed to implement these provisions. As such, ISO-NE states that NRG should await the development of the Manuals, and the stakeholder process that surrounds such development where it can actively participate and raise its concerns about timing.

## **2. Commission Determination**

35. We reject NRG's protest. We do not agree with NRG's assertion that that the proposed FCM rules impose unreasonable limitations on the transferability of a capacity obligation and contradict the FCM Settlement. As ISO-NE notes in its answer, the FCM Settlement formally establishes that the Forward Capacity Auction should procure sufficient capacity to assure reliability as measured under the Installed Capacity Requirement<sup>32</sup> and also should procure sufficient capacity in each sub-region of New

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<sup>32</sup> Settlement Agreement, Transmittal Letter at 23, n.41; and Settlement Agreement at section 11, Part III.C.

England. We note that the FCM Settlement, to which NRG was a signatory, also provides ISO-NE with the ability to prohibit units from de-listing if they are needed for reliability reasons.<sup>33</sup> Thus, we disagree with NRG's claim that the proposed relevant market rules, which allow for ISO-NE review of proposed bilateral transfers of capacity obligations and reject any that endanger reliability, contradict the FCM Settlement

36. ISO-NE asserted in its February 15 transmittal letter that "the FCM is a forward market for physical resources, not financial obligations."<sup>34</sup> ISO-NE further stated that the objective of procuring "just enough installed capacity to maintain system reliability" requires that the Forward Capacity Auction procure capacity from actual, specific resources that will be available at the start of each commitment period.<sup>35</sup> However, NRG's position would establish reliability as secondary to the ability of generators to transfer capacity obligations and would be inconsistent with this stated objective. We agree with ISO-NE that NRG's interpretation of the FCM Settlement misconstrues the authority over bilateral transfers granted to ISO-NE. The language that NRG references from the FCM Settlement in support of its argument states that "[b]ilateral contracts shall be allowed up to the applicable Seasonal Claimed Capability of the Resource..."<sup>36</sup> and "a resource that transfers its capacity market obligations to another resource...shall be de-listed pursuant to the delisting process."<sup>37</sup> However, as ISO-NE states in its answer, the FCM Settlement also explicitly provides ISO-NE with the right to "accept" these transactions.<sup>38</sup> If ISO-NE can choose to "accept" certain contracts, as a corollary, it must also have the right to reject others, just as limiting ISO-NE's authority to determine which resources may or may not de-list for reliability reasons would threaten reliability. Thus, the cited language from the FCM Settlement does not represent a directive that all bilateral transfers of capacity obligations be accepted unconditionally. Rather, we view the FCM Settlement as providing that bilateral transfers of capacity obligations only be permitted subject to ISO-NE review and acceptance.

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<sup>33</sup> Settlement Agreement at section 11, Part IV.B.2.

<sup>34</sup> Transmittal letter at 7.

<sup>35</sup> Transmittal letter at 8.

<sup>36</sup> Settlement Agreement at section III (P).

<sup>37</sup> Settlement Agreement at section IV (A)(6).

<sup>38</sup> *Id.* at section 11, Part IV.B.2.

37. As noted previously, NRG asserts that to the extent any review of a transfer among qualified suppliers within the same zone is rejected, this demonstrates that the services provided by the suppliers are not the same and the resource whose transfer was rejected should be paid additional compensation. We disagree with NRG's position that suppliers providing local reliability needs should be paid additional compensation through the FCM market. ISO-NE states that "the Forward Capacity Auction is designed such that it will purchase just enough resources region-wide and at least the Local Sourcing Requirement in specific zones to assure regional and local resource adequacy."<sup>39</sup> As ISO-NE notes, the lack of price separation in the Forward Capacity Auction does not mean that there is no need for capacity in a local potentially import-constrained zone. Instead, it reflects the fact that the region-wide clearing price was high enough to incent enough resources to remain in the auction that the amount of capacity in the zone was sufficient. Further, as ISO-NE details in its answer, if generators are asked to provide additional services including VAR support or regulation, they will be compensated for those services through the appropriate ISO tariff or markets, not through the FCM.

38. ISO-NE is properly concerned that an unchecked ability to exit the market after accepting a capacity obligation could lead to gaming, whereby owners who believe their units will be needed for reliability could leave the market (through the bilateral transfer of a "needed" capacity obligation) in search of a higher priced reliability agreement. We find that it is appropriate for ISO-NE, as the independent grid operator responsible for ensuring reliability in the region, to review these proposed transfers of capacity obligations before accepting them, and to reject bilateral contracts that could endanger reliability. We note that this reliability review prevents gaming by holding these units needed for reliability to their committed capacity obligation.

39. We also disagree with NRG's assertion that the proposed market rules impinge upon the Commission's exclusive jurisdiction under section 203. NRG appears to be arguing that, because ISO-NE will review (and potentially disallow) the transfer of some capacity obligations, a party may be forced to use a particular unit to meet its capacity obligation, and that this determination by ISO-NE encroaches on the Commission's section 203 jurisdiction over the transfer of ownership of that unit. This is incorrect. Section 203 addresses the Commission's jurisdiction over the purchase, lease or other

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<sup>39</sup> Transmittal letter at 141.

acquisition of a generating facility itself.<sup>40</sup> The proposed market rule, by contrast, provides that "[a] resource having a Capacity Supply Obligation seeking to shed that obligation . . . may . . . enter into a bilateral transaction to transfer its Capacity Supply Obligation . . . to [another] resource," after providing information to ISO-NE including the location of the resource and amount of capacity it can provide (section III.13.5.1). However, ISO-NE reviews the information provided, and then "may reject the [contract] for . . . reasons [including] identified reliability issues" (section III.13.5.1.1.3(a)), namely, if "[t]he capacity [is] needed for reliability reasons [because] the absence of the capacity would result in the violation of any [North American Reliability Council] or [Northeast Power Coordinating Council] (or their successors) criteria, or ISO New England System Rules" (section III.13.2.5.2.5). This market rule does not implicate the activities placed under the Commission's jurisdiction by section 203 of the FPA, and we therefore reject this argument.

40. As mentioned previously, NRG asserts that ISO-NE suggests that generators include a risk premium in their offers to address the contingency that transferability will not be allowed, yet are expressly forbidden to do so by section III.13.1.2.3.2.1.3 of the market rules. Addressing this point, ISO-NE asserts that NRG is making an "apples vs. oranges" argument, as the proper cost components of a de-list bid are different from those of an offer into the Forward Capacity Auction; ISO-NE contends that a risk premium associated with assuming a Capacity Supply Obligation is not properly includable in a de-list bid because it is not a going forward cost. Although we reject NRG's protest of the unreasonable limitations on the transferability of a capacity obligation, we fail to comprehend ISO-NE's "apples vs. oranges" argument. An existing resource's de-list bid

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<sup>40</sup> Section 203(a)(1), 16 U.S.C. § 824b(a)(1), provides as follows:

No public utility shall, without first having secured an order of the Commission authorizing it to do so—(A) sell, lease, or otherwise dispose of the whole of its facilities subject to the jurisdiction of the Commission, or any part thereof of a value in excess of \$ 10,000,000; (B) merge or consolidate, directly or indirectly, such facilities or any part thereof with those of any other person, by any means whatsoever; (C) purchase, acquire, or take any security with a value in excess of \$ 10,000,000 of any other public utility; or (D) purchase, lease, or otherwise acquire an existing generation facility (i) that has a value in excess of \$ 10,000,000; and (ii) that is used for interstate wholesale sales and over which the Commission has jurisdiction for ratemaking purposes.

represents the minimum price at which the resource is willing to provide capacity in the FCM and accept the associated obligations of a capacity resource. In that regard, ISO-NE's assertion that a de-list bid is different from an offer into the FCA is unclear. From our reading, it appears that an existing resource may not include a risk premium for the inability to transfer a capacity obligation in its de-list bid. Nevertheless, we do not consider this a sufficient reason to reject this market rule. We agree with ISO-NE that a risk premium associated with the possible inability to transfer a capacity obligation is not a going forward cost, because the resource would not expect to profit from transferring its capacity obligation. That is because if an existing resource's de-list bid includes all of its legitimate going forward costs (including opportunity costs other than sales in reconfiguration auctions) and the FCA's clearing price equals or exceeds the de-list bid (and thus, the resource is selected to provide capacity), the resource would make more profit by providing capacity than by de-listing. It, therefore, would not expect to profit from transferring its capacity obligation to another resource. Moreover, as indicated previously, the FCM is a forward market for physical resources and bilateral capacity transfers represent a secondary objective; thus, the market rules should facilitate the goal of ensuring a reliable supply of capacity for the New England market, rather than the goal of enabling parties to transfer their obligations as freely as possible.

41. In terms of the development of procedures and timetables for denial of bilateral transfers, the Commission will not establish ISO-NE's priorities. NRG's complaint on this point is premature because the forthcoming manuals that will detail this information have not yet been developed, and ISO-NE has committed to developing these manuals through a stakeholder process. We note that the development of manuals will provide NRG the opportunity to voice any concerns.

42. ISO-NE has also committed to providing written notice and explanations to resources when it rejects bilateral agreements.<sup>41</sup> We do not agree with NRG's suggestion that ISO-NE instead should be required to make a filing with the Commission under section 205 of the FPA each time that it prohibits a bilateral transfer, detailing the reasons behind the denial and how the prohibition could be avoided (through increased capacity purchases, transmission, or other means). Under section 205(d), 16 U.S.C. § 824d(d),

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<sup>41</sup> ISO-NE answer at 14 ("NRG is correct that the ISO must provide written notice and explanation to a resource already committed through the Forward Capacity Auction explaining the rationale for refusing to accept a bilateral agreement, and the process for so doing will be laid out in the Manuals, as described below").

"no change shall be made by any public utility in any . . . rate, charge, classification, or service [relating to any transmission or sale subject to the jurisdiction of the Commission], or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public." ISO-NE's rejection of a proposed bilateral contract to transfer a capacity obligation would not result in a change in capacity prices or other rates or charges subject to our jurisdiction. For this reason, we do not believe a section 205 filing will be necessary any time that ISO-NE rejects a proposed bilateral contract, and we find ISO-NE's intended notification and explanation to the resource to be appropriate.

## **B. Requirement to Provide Ancillary Services**

### **1. Positions of the Parties**

43. Proposed section III.13.6.1.1.2 states that "for each day, Day-Ahead Energy Market and Real-Time Energy Market offers for the listed portion of a resource must reflect the then-known unit-specific operating characteristics (taking into account, among other things, the physical design characteristics of the unit) consistent with good utility practice." FirstLight requests that the Commission confirm that proposed section III.13.6.1.1.2 does not impose additional obligations on listed capacity resources, such as the obligation to provide ancillary services (such as synchronized reserves and load following services) based on its physical design characteristics.

44. In its answer, ISO-NE argues that the request for clarification by FirstLight should be denied. ISO-NE states that FCM market rules simply require that listed capacity units must include their physical operating characteristics in their offers, and follow dispatch instructions consistent with such characteristics. ISO-NE states that aside from the obligations expressly contained in section III.13.6.1 and the requirement to follow dispatch instructions, the FCM market rules do not mandate participation in other markets. Thus, according to ISO-NE, the requested clarification is unnecessary.

### **2. Commission Determination**

45. We deny FirstLight's request. The various sections of proposed section III.13.6.1.1 may, in fact, require the provision of certain ancillary services by listed resources, because that requirement is subsumed within the obligation that is placed on resources that offer to provide energy in the real-time market. The essence of providing some ancillary services (such as ten-minute spinning reserves, ten-minute non-spinning reserves, and thirty-minute operating reserves) is that resources stand ready to provide energy, if instructed by ISO-NE, within a specified time frame. Section III.13.6.1.1.1 requires a listed resource to make offers to provide energy into the day ahead and real-time energy markets, subject to then-known unit-specific operating

characteristics. If a unit's operating characteristics allow it to produce energy within the time frame associated with a particular ancillary service, the requirement to offer into the real-time energy market necessarily involves standing ready to provide energy in real time within that time frame, and therefore, to provide the applicable ancillary service.

### C. Termination of Price Response Programs

#### 1. Positions of the Parties

46. Prior to the FCM Settlement, ISO-NE offered various "price response" programs to reduce the cost of energy, including a 30-minute Real-Time Demand Response program, under which demand responders could receive payments in return for reducing demand when the Locational Marginal Price of energy rose to a certain level. ISO-NE's tariff currently provides that such programs will terminate on February 29, 2008.<sup>42</sup> Under the FCM Settlement, these demand response programs would be retained for the whole of the transition period commencing on December 1, 2006 and ending on May 30, 2010, during which transition payments would be made to all current demand response providers.<sup>43</sup> The proposed rules in the instant filing extend the termination date to May 30, 2010 in order to match the end of the transition period to the Forward Capacity Market.

47. EnerNOC, a demand response provider, states that, although overall it supports the FCM market rules filed by ISO-NE, it is concerned that under the proposed rules demand resources will no longer be able to participate in the energy markets, and that the energy payments that are currently part of the 30-minute Real Time Demand Response program will be eliminated. It states that, while it "expects that the forward capacity markets will prove to be a workable substitute for the existing ISO-NE capacity-based demand response programs," it fears that eliminating the ability of Demand Resources to participate in the energy markets will reduce the benefits of demand response to customers and the ability of resources to provide demand response to New England.<sup>44</sup> It

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<sup>42</sup> Attachment E to Market Rule 1 (1st Rev Sheet No. 7903): "The Load Response Program will be effective from the Operations Date through February 29, 2008." *New England Power Pool and ISO New England, Inc.*, 111 FERC ¶ 61,604.

<sup>43</sup> Settlement, Attachment 1 at 46.

<sup>44</sup> EnerNOC comments at 3.

further states that it believes that ISO-NE's exclusion of demand resources from the energy markets stems from ISO-NE's assumption that a majority of customers will be taking service under Time-of-Use or Real-Time-Pricing tariffs by 2010. EnerNOC supports the use of such tariffs, but questions whether such pricing mechanisms will be widely adopted by 2010. Therefore, according to EnerNOC, it is not yet appropriate to eliminate the ability of demand resources to participate in the energy market.

48. In its response, ISO-NE states that EnerNOC's argument is based on an overly limited view of the participation by demand resources in the energy markets. ISO-NE states that "[d]emand resources participate in all markets, including the energy markets, by using less when price increases. Nothing in the FCM rules affects this basic right."<sup>45</sup> ISO-NE points out that the filing at issue in fact extends the expiration date for demand response programs (which was previously February 29, 2008) to May 31, 2010, so as to permit participants in demand response programs to receive transition payments for an additional 2½ years. ISO-NE further states that once the FCM commences, there will be "no need for the capacity based [demand response] programs . . . because the Commission's objective of integrating demand-side [resources] into the market will be achieved," and that, once demand resources are completely integrated into the wholesale markets, there will be no need to extend the price response programs beyond 2010.<sup>46</sup> ISO-NE then states:

Notwithstanding, at the request of several stakeholders, the ISO has committed to discuss the termination of the price-based programs in the stakeholder process prior to their termination in June 2010. Thus, EnerNOC's request to continue these programs is premature and should be addressed in the upcoming stakeholder process.<sup>47</sup>

## 2. Commission Determination

49. The Commission rejects EnerNOC's protest. Because ISO-NE has indicated that it is willing to continue evaluating this question through a stakeholder process, we consider EnerNOC's protest to be premature. As noted above, the existing tariff

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<sup>45</sup> ISO-NE answer at 15.

<sup>46</sup> *Id.* at 16.

<sup>47</sup> *Id.*

terminates these programs in early 2008. Under the market rules filed here, the price response programs will not terminate until May 31, 2010. Extending the termination date by over two years should provide New England's stakeholders additional time to arrive at a resolution of EnerNOC's concern.

50. As an initial matter, however, we note that, if the price response programs are terminated prematurely, important demand response capability that could provide relief during system emergencies may be lost. In this regard, ISO-NE's position here is that demand resources do not need to be integrated into the energy markets. However, because ISO-NE has indicated that it is willing to continue evaluating this question through a stakeholder process,<sup>48</sup> we agree with ISO-NE that addressing EnerNOC's protest is premature. We encourage ISO-NE and its stakeholders to continue their negotiations on this question, so as to ensure that the benefits that demand response can bring to the system are preserved by completely integrating demand resources into the wholesale markets.

#### **D. Disclosure of Rejection of Bids for Reliability Reasons**

##### **1. Positions of the Parties**

51. Capacity Suppliers reiterate their protest regarding the transparency of the disclosure process of de-list bids rejected for reliability reasons, originally filed in Docket No. ER07-546-000. Specifically, Capacity Suppliers request that ISO-NE be required to report, with explanations of reliability limitations, the following: offers of new capacity rejected because of interconnection limitations under section III.13.1.1.2; demand bids that were not included because the resource is required for reliability pursuant to section III.13.4.2.2(d). Further, if a capacity supply obligation bilateral is rejected for failing the standards under section III.13.2.5.2.5, Capacity Suppliers assert that ISO-NE should be required to report such rejections in an annual filing or separately to the Commission with an explanation of the reliability limitation.

52. In addition, Capacity Suppliers argue that if ISO-NE has identified a transmission upgrade that could alleviate the reliability issue, the affected market participant should be informed. Capacity Suppliers further assert that no de-list bid in a Forward Capacity Auction or any demand bid in a reconfiguration auction should be rejected for reliability reasons without considering alternative supply sources that could address the reliability

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<sup>48</sup> We also encourage ISO-NE to coordinate with the ISO/RTO Council as it assesses best practices that may be applicable to the New England region.

issues. Capacity Suppliers suggest several revisions to the market rules to achieve these results.<sup>49</sup> According to Capacity Suppliers, these changes will allow market forces to achieve the required level of resource adequacy while limiting the unnecessary “command and control” decisions by ISO-NE.

## 2. Commission Determination

53. The Commission will reject Capacity Suppliers’ requested revisions as unnecessary. The proposed market rules already provide sufficient transparency regarding determination of resources needed for reliability and de-list bids rejected for reliability reasons. Section III.13.8.2 of the proposed market rules already requires ISO-NE to provide a list of resources rejected for reliability reasons and the reasons for rejection. The proposed rules also require ISO-NE to send notification of individual rejections to the affected resource with the reasons for rejection. ISO-NE is also required to file a report on all resources rejected during the qualification process for annual auctions and annual reconfiguration auctions, including an explanation of why a resource was rejected for reliability, if applicable.

54. Capacity Suppliers’ request that no de-list bid be rejected for reliability reasons without consideration of all available alternatives to address the reliability issue is unnecessary as well. As ISO-NE pointed out in its answer in Docket No. ER07-546-000, ISO-NE will consider all resources and transmission improvements that are committed to provide capacity for the relevant capacity commitment period in determining whether a resource is needed for reliability, and will report to suppliers on that determination.<sup>50</sup>

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<sup>49</sup> Capacity Suppliers protest, Appendix A at 20-21.

<sup>50</sup> ISO-NE answer at 56 (“In determining whether a unit is needed for reliability, the ISO will include all resources and transmission improvements that are committed to provide capacity for the year in question, which it believes are all alternatives to the supply resources that should be included. Units that are competing in the auction, but have not yet cleared or committed to provide capacity will not be included since there is no way of knowing whether such units will clear the auction. *The combination of the Regional System Plan and the reporting on the reasons for rejection should meet the suppliers’ request that they be notified if a transmission improvement will meet the reliability need*”) (emphasis added).

**E. Compensation to Holders of Capacity Transfer Right****1. Positions of the Parties**

55. Casco Bay requests that the Commission require ISO-NE to begin a stakeholder process to ensure that holders of Capacity Transfer Rights (CTRs) recover their investment in the upgrades to constrained interfaces that resulted in the award of CTRs.<sup>51</sup> Casco Bay states that the proposed section III.13.7.3.3.2(c) of the Tariff provides for an allocation of 325 MW of CTRs to Casco Bay, consistent with the FCM Settlement. Casco Bay does not object to the steps taken in the ISO-NE filing, but argues that these steps may be inadequate to ensure that entities that have provided participant funding for upgrades to constrained interfaces receive adequate compensation for the benefits that they have provided through their investment. Casco Bay is concerned that the value of its previously-awarded CTRs between two capacity zones would be eliminated in the event that additional regionally-funded upgrades reduce or eliminate the capacity price separation between the capacity zones. Casco Bay states that the ISO-NE Tariff contemplates that market efficiency transmission upgrades that serve to decrease congestion between two areas may be approved as part of ISO-NE's Regional System Plan. Casco Bay proposes that where future transmission upgrades funded through the network tariff increase the interface capability and reduce congestion, the CTR holder should have the choice between (i) being paid an amount equal to the cost of the new transmission upgrade in \$/MW times its CTR MW value (with the cost of such payments rolled into the network rate) in return for relinquishing its CTRs and other transmission rights associated with its upgrade funding, or (ii) retaining its CTRs and other transmission rights. Casco Bay's proposal would not apply to future upgrades that are participant-funded. Casco Bay states that while future participant-funded upgrades may reduce congestion, the risk is less, because (unlike the situation when an upgrade is funded through network rates) participants will not fund an upgrade when the expected value of the associated transmission rights does not cover the cost of the upgrade.

56. In its answer, ISO-NE argues that Casco Bay's proposal should be rejected. ISO-NE states that a CTR is a financial mechanism, rather than a physical one. According to ISO-NE, a CTR confers a financial right on an entity that funded an upgrade for the

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<sup>51</sup> CTRs are a type of financial transmission right associated with the New England capacity market. When capacity prices differ in two different capacity zones, the holder of a CTR between the two zones is entitled to revenue equal to the difference in the capacity prices in the two zones.

purpose of relieving congestion to receive the financial equivalent of exporting capacity over the constrained interface, if it has to obtain energy across the constrained interface. ISO-NE points out, however, that once a constraint ceases to exist, there is no longer price separation between a constrained area and adjacent areas, so the need for the CTR and the payment for the CTR no longer exist. In ISO-NE's view, Casco Bay misinterprets a CTR as a guaranteed source of revenue to pay for its investment *ad infinitum*. ISO-NE argues that if the value of capacity on both sides of the interface is the same, there is no need for the CTR, since the investment has achieved its objective of allowing that entity to sell across the interface.

57. Casco Bay, in its response to ISO-NE's answer, states that, contrary to ISO-NE's understanding, Casco Bay recognizes that CTRs only provide compensation to the CTR holder while congestion persists across the relevant interface (*i.e.*, there is price separation between the two capacity zones). Casco Bay reiterates that, because the value of CTRs depends upon continued congestion, the intended purpose of the allocation of those CTRs to holders, such as Casco Bay, could be frustrated if that congestion is eliminated by pool-funded upgrades. Casco Bay argues that, since the purpose of allocating CTRs to Casco Bay and other was to allow "those who ultimately pay the costs of the transmission system, including market participants that have funded specific upgrades that increased transfer capacity" to receive the benefits of CTRs,<sup>52</sup> those CTRs will only serve that purpose as long as congestion persists and capacity has a higher locational value on one side of the interface than the other. However, the CTRs allocated to Casco Bay as compensation for the reduction in congestion achieved by its privately-funded upgrades could be substantially reduced or eliminated by pool-funded upgrades, which result would reduce the benefits received by participants such as Casco Bay for the benefits they provided to the system by previously funding upgrades. Thus, Casco Bay states, because perpetuating the congestion clearly makes no sense, an alternative means of providing for CTR holders to receive appropriate recovery should be implemented in such circumstances.

## 2. Commission Determination

58. We deny Casco Bay's request. Participant-funded upgrades are made at the risk of the participant-funder, *i.e.*, the investor. In the past, such investors have funded upgrades in exchange for receiving certain benefits, including financial transmission

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<sup>52</sup> Casco Bay answer at 4, *citing Devon Power, LLC*, 107 FERC ¶ 61,240 at P 66 (2004).

rights in the energy market operated by ISO-NE. One of the risks of such investments is that future transmission upgrades (either participant-funded or pool-funded) may be constructed that reduce the congestion along the applicable transmission path, or new generation and demand response may be developed within the constrained area to reduce congestion; either of these possibilities would reduce the value of financial transmission rights awarded to the participant-funder. Casco Bay's proposal would shield participant-funders from some of this risk by providing them with the opportunity for cash rebates after-the-fact (in exchange for giving up financial transmission rights) if future upgrades reduced congestion. The Commission finds that mandating such rebates would distort the incentive to invest in upgrades, because the investor would not bear the full risk of the investment in the event that the upgrade later turns out to be less profitable than the investor originally expected.

59. Moreover, CTRs are a creation of the FCM Settlement: they have not existed in the past, they do not exist now, and they will not exist until the first delivery year under FCM, *i.e.*, 2010-2011. Any participant-funded upgrades added to the system in the past could not have been made in the expectation of CTR revenues, because CTRs did not exist when the upgrades were funded. Casco Bay is incorrect in claiming that the proposed market rules would upset the expectations it had at the time it funded past transmission upgrades with respect to CTR revenues.<sup>53</sup>

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<sup>53</sup> Public Systems offer comments with regard to the requirement that self-supplied resources, in order to fulfill a capacity requirement, must either be located within the same capacity zone as the load unless the resource has an allocation of CTRs – *see* section III.13.1.6.2. Public Systems considers this provision inconsistent with related aspects of the proposed market design. Public Systems further state that the mechanics of how CTR-related benefits will be flowed through to CTR holders are being developed, and assert that ISO-NE should address the interface between CTRs that are not allocated based on the ownership of pool-planned units or through other “special” allocation arrangements and self-supplied resources. In its answer filed in Docket No. ER07-546-000, ISO-NE stated that the resources that satisfy a load serving entity's local sourcing requirement are either located in the same capacity zone or are pool planned units with a special allocation of CTRs, and that any additional CTRs allocated to an LSE are not dependent on entitlements in any particular resource and thus cannot be used to meet a local sourcing requirement.

Given that additional CTRs cannot be used to meet a local sourcing requirement, as ISO-NE asserts, the Commission will not direct ISO-NE to address the interface

(continued)

## **F. Recovery of Extraordinary Fuel Expenses**

60. Proposed section 13.6.1.1.3 provides that, when, due to extraordinary fuel expenses, the Energy Offer Price that a generator would need to offer to recoup all of its costs is greater than the Energy Offer Cap on supply offers, and a generator has provided ISO-NE with supporting documentation of what the supply offer would have been but for the cap, the resource may submit into the day-ahead or real-time energy market offers equal to the Energy Offer Cap. Then, if the resource is subsequently dispatched for the relevant period, it will be paid all of what its offer would have been, through both the payment of the locational marginal price and Net Commitment Period Compensation credits (uplift). The payment may not exceed the resource's fuel costs, including commodity cost, transportation cost, and imbalance charges or other penalties applicable to such generation.<sup>54</sup>

### **1. Positions of the Parties**

61. NSTAR protests this provision. It argues that there is little incentive to coordinate gas and electric markets when pipeline penalties such as imbalance penalties can be passed through to end-use customers. According to NSTAR, the FCM rules allow gas generators to take more gas than they had previously nominated, at the very time the gas system is at its most stressed, because the generators are secure in the knowledge that

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between certain CTRs and self-supplied resources. Moreover, Public Systems has failed to demonstrate how section III.13.1.6.2 of the proposed market rules is inconsistent with the proposed market design.

<sup>54</sup> Transmittal letter at 159:

If, due to extraordinary fuel prices, a Market Participant cannot submit a bid which would recover its full operational cost, it may then submit a Supply Offer in either the Day-Ahead or in the Real-Time Energy Market at the energy offer cap. At the same time, it must advise the ISO that the Supply Offer would have been equal to or greater than the energy offer cap and state what the Supply Offer would have been but for the cap. If the capacity resource is subsequently dispatched, the Market Participant will be paid its offer for each MWh of energy produced through the payment of the Locational Marginal Price (“LMP”) and appropriate Net Commitment Period Compensation (“NCPC”) Credits. However, such a payment may not exceed the capacity resource’s fuel costs, including . . . imbalance charges or other penalties applicable to such generation.

they can recover any resulting penalties from their customers. Thus, NSTAR claims, the FCM rules would provide *carte blanche* to generators to rely upon gas taken from firm customers. NSTAR contends that this proposal effectively destroys the reliability of the gas system in order to preserve the reliability of the electric system. NSTAR argues that the tariff language cannot be just and reasonable when the customers that are having their firm gas "expropriated" by a generator are the same customers that are paying a premium to that generator for electric reliability. NSTAR further notes that under the FCM rules, customers will also pay for the generator's gas penalties that were imposed for the purpose of protecting the same firm gas customers from having their gas expropriated. NSTAR contends that although reliability is the paramount return for the investment made by load through forward capacity payments, relying upon generation availability through the forgiveness of gas pipeline penalties (under the proposed rules) sacrifices physical reliability for financial expediency.<sup>55</sup> According to NSTAR, one of the purposes of the FCM was to include incentives for generators to firm up commitments for either gas supply and/or transportation to maintain reliability during times when the system needs it the most. NSTAR acknowledges that while the language filed in section 13.6.1.1.3 of the FCM tariff is consistent with the Settlement, the fact that reliability is threatened should compel the Commission to disallow the ability of electric market participants to recover gas pipeline penalties through the electric tariff.

62. ISO-NE argues that the protest should be rejected because the issue NSTAR raises will be addressed when the ISO submits a further filing on gas-electric market coordination pursuant to section VII of the FCM Settlement. Therefore, ISO-NE requests that the Commission defer ruling on the issue raised by NSTAR until ISO-NE submits a further filing on the coordination of the gas and electric markets.

## **2. Commission Determination**

63. The Commission rejects NSTAR's protest. ISO-NE has stated that it will address the ability of generators to recover gas pipeline imbalance charges and other penalties incurred during periods of extraordinary fuel costs.<sup>56</sup> Further, ISO-NE has noted that it

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<sup>55</sup> NSTAR states that it has raised this issue in both Docket EL07-2 and the stakeholder process for the instant filing, proposing draft language to tariff section 13.6.1.1.3 that was subsequently struck under opposition from generators.

<sup>56</sup> Transmittal letter at 157 ("as the ISO files rules to implement section VII of the Settlement regarding gas availability, it may seek to clarify the provision to assure that they do not provide improper incentives"); ISO-NE answer at 6

(continued)

will be prioritizing the further development of several items, and will make a compliance filing setting out the prioritization of these items by September 1, 2007. ISO-NE has asked that the Commission refrain from prejudging this prioritization process.<sup>57</sup> As such, while the Commission recognizes NSTAR's concern, at this time we will refrain from offering judgment on the pending FCM rules addressing section VII of the FCM Settlement until they have been vetted through the stakeholder process and presented to us.

## **G. Ability of Intermittent Resources to Back Capacity Exports**

### **1. Positions of the Parties**

64. Brookfield objects to ISO-NE's proposal in the market rules to prohibit Intermittent Resources from backing a capacity export to an external control area.<sup>58</sup> Brookfield claims that the FCM Settlement did not contemplate a limitation on Intermittent Resources from backing a capacity export. Brookfield further argues that this proposed limitation would create a new seams issue with neighboring control areas, especially since neighboring control areas have historically accepted intermittent capacity from ISO-NE. Brookfield also states that ISO-NE's proposed limitation would place Intermittent Resources at a competitive disadvantage compared with other resources that are free to sell their capacity to the highest bidder, either ISO-NE or a purchaser in an external control area. Brookfield asserts that this competitive disadvantage would discourage future investment in Intermittent Resources.

65. ISO-NE states in response to Brookfield's argument that intermittent resources differ from conventional resources, in that their output can go from zero to full output outside the control of the owner, and that the level of their output is not easily predictable on a day ahead basis. ISO-NE points out that, for this reason, its market rules exempt

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("NSTAR's protest should be rejected because the issue it has raised will be addressed when the ISO submits a further filing on gas-electric market coordination pursuant to section VII of the FCM Settlement").

<sup>57</sup> *Id.* at 22.

<sup>58</sup> *See* section III.13.6.2.2.

intermittent resources from the requirement of offering into the day ahead market, like all other capacity resources.<sup>59</sup>

## 2. Commission Determination

66. The Commission will accept ISO-NE's proposal to prohibit Intermittent Resources from backing capacity exports to external control areas. In order to back a capacity export, a resource must be able to commit weeks or months ahead of time; however, Intermittent Resources characteristically have uncontrollable and unpredictable output. As such, it would be inappropriate to allow Intermittent Resources to back capacity exports. As ISO-NE notes, because of their unpredictable and uncontrollable output, Intermittent Resources are exempt from the requirement imposed on all other capacity resources to offer into the day ahead energy market. Thus, exempting Intermittent Resources from the ability to back capacity exports would treat intermittent resources consistently, according to their physical characteristics: Intermittent Resources would be exempt from certain requirements imposed on units with more predictable and controllable output, but would also not be able to fulfill all the functions of such units.

The Commission orders:

The portions of ISO-NE's February 15 filing discussed above are hereby accepted.

By the Commission

( S E A L )

Kimberly D. Bose,  
Secretary.

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<sup>59</sup> ISO-NE answer in Docket No. ER07-546-000, dated March 23, 2007.