122 FERC ¶ 61,057
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

ISO New England Inc. Docket Nos. ER08-61-000
ER08-61-001

ORDER ACCEPTING FILING AND ESTABLISHING TECHNICAL CONFERENCE

(Issued January 25, 2008)

1. On October 16, 2007, ISO New England Inc. (ISO-NE) submitted for filing an emergency revision to Market Rule 1 of its Transmission, Markets and Services Tariff (Tariff) to address a potential opportunity for market manipulation. For the reasons discussed below, we accept and suspend for a nominal period the revision to Market Rule 1, effective October 17, 2007, as requested, subject to refund, and to the outcome of a technical conference, which we order the Commission's staff to convene within 60 days of the date of this order.

I. Background

2. At the ISO-NE/New York Independent System Operator (NYISO) interface that precipitated the instant filing, net exports from ISO-NE to NYISO are limited by the Total Transfer Capability (TTC) of the interties between the two control areas. This TTC is approximately 1,000 MW and is rarely binding. Currently, when the TTC limit is binding, ISO-NE does not use congestion pricing to manage flows from import and export transactions over interties with neighboring control areas, such as NYISO. When fixed transactions for net transfers are submitted that exceed the TTC of the tie, the Day-Ahead Energy Market will economically clear enough counter-flow to honor the TTC. Because congestion is not priced on the External Node (in this case the Roseton location in New York), the offer price of the dispatchable imports required to clear the fixed exports will exceed the clearing price (i.e., energy plus losses only), and the balance will be paid to the scheduling entity as Net Commitment Period Compensation (NCPC). The NCPC is allocated as an uplift charge to market participants in proportion to the daily sum of their Day-Ahead Load Obligations.

3. On three days in October 2007,[1] physical circumstances caused the TTC for the ties between ISO-NE and NYISO to decline significantly in certain hours. Consequently, ISO-NE was forced to clear a material amount of imports from NYISO so that the TTC limit was not violated. As a result, about $230,000 in NCPC was paid to the price-sensitive dispatchable imports.

4. Although ISO-NE observed no inappropriate bidding during these three days, it is concerned that market participants may attempt to manipulate the market by submitting offsetting export and import offers in such a way as to generate inappropriate NCPC payments. Specifically, a market participant could simultaneously offer a large fixed export transaction (which is not price sensitive) and a high-priced dispatchable import transaction that offsets the export transaction, with the intent of collecting large NCPC payments.

II. Description of the Filing

5. ISO-NE proposes to eliminate this opportunity for market manipulation by modifying the way NCPC credits and charges are allocated to external transactions submitted by the same market participant and/or its affiliates. When the external interface is binding, the market participant will be ineligible to receive NCPC credits on any offsetting external transactions that clear the Day-Ahead Energy Market. For example, if a market participant submits a 100 MW fixed export transaction and a 120 MW priced import transaction, and the interface is binding, 100 MW of the priced import transaction will be ineligible to receive NCPC credits.[2]

6. ISO-NE states that it has made this filing under the exigent circumstances provision of its Participants Agreement with the New England Power Pool Participants Committee (NEPOOL) and Individual Participants, and that as a consequence, its proposed revisions have not been through the stakeholder process. However, ISO-NE states that it will consult stakeholders about additional changes or other potential solutions.

7. ISO-NE requests that the Commission waive its 60-day prior notice requirement[3] and make the proposed rate effective October 17, 2007. ISO-NE contends that good

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[1] October 3, 4, and 9.

[2] Specifically, ISO-NE proposes to amend sections III.F.2.3.4(c) and III.F.2.4.4(c) of Market Rule 1, Appendix F, and to make conforming changes to section III.3.2.3(d).

[3] *See Prior Notice and Filing Requirements Under Part II of the Federal Power Act*, 64 FERC ¶ 61,139, *order on reh'g*, 65 FERC ¶ 61,081 (1993) (*Prior Notice*); *Central Hudson Gas and Electric Corp*., 60 FERC ¶ 61,106, *reh'g denied*, 61 FERC ¶ 61,089 (1992) (*Central Hudson*).

cause exists to grant waiver because ISO-NE has advised market participants of an opportunity to misuse NCPC by making this filing.

III. Notice of Filing and Responsive Pleadings

8. Notice of ISO-NE's filing was published in the *Federal Register*,[4] with comments and interventions due on or before October 25, 2007. The Long Island Power Authority and its subsidiary, LIPA (collectively LIPA) and H.Q. Energy Services (U.S.), Inc., filed timely motions to intervene. NEPOOL and NSTAR Electric Company filed timely motions to intervene and comments. Constellation Energy Commodities Group, Inc. and Constellation New Energy, Inc. (collectively Constellation) filed a timely motion to intervene and comments protesting the filing. ISO-NE filed an answer to the protest and to NSTAR's comments.

9. In its comments, NEPOOL states that it currently has no position on ISO-NE's filing, but that it may develop a position as ISO-NE's proposal is considered in the stakeholder process. NSTAR states that while it does not oppose the proposed changes to Market Rule 1, it recommends that the Commission require ISO-NE to institute discussions about the scheduling and pricing of external transactions and require the internal market monitoring unit to certify that ISO-NE's revision comprehensively addresses the opportunity for market manipulation.

10. Constellation recommends exempting NCPC charges on the quantity of netted export/import transactions. Constellation argues that these charges unfairly penalize the exporting market participant, even though it did not engage in any market abuse.

11. Constellation further claims that ISO-NE's proposal results in market participants incurring ancillary charges from NYISO without receiving full compensation for these costs. Constellation explains that market participants must flow energy into NEPOOL across the Roseton interface, and therefore incur ancillary charges from NYISO, and that while the market participant's offer price includes costs incurred flowing energy into NEPOOL, including NYISO export charges and a locational marginal price (LMP) differential between the export interface in New York and the market participant's unit, the LMP at Roseton is often insufficient to cover the market participant's costs. As a consequence, Constellation argues that ISO-NE will ultimately pay the market participant less than the offer price, resulting in a loss—through no fault of its own—for the market participant. To remedy this alleged problem, Constellation suggests that ISO-NE compensate market participants for any costs incurred flowing power from New York to New England as a result of this revision to Market Rule 1.

[4] 72 Fed. Reg. 60,339 (2007).

12. Finally, Constellation argues that if the Commission accepts ISO-NE's revisions to Market Rule 1, it should set a sunset date of April 17, 2008. Constellation argues that setting a sunset date will ensure that stakeholder discussions will include alternative solutions to the problem ISO-NE has identified. Constellation further requests that the Commission require ISO-NE to file a report on February 16, 2008 advising the Commission of the progress and results of the stakeholder process, and indicating whether stakeholders have developed an alternative solution or providing a rationale for continuing with the solution proposed here.

13. In its answer, ISO-NE argues that Constellation is incorrect about the impact of its proposed revision. ISO-NE states that, contrary to Constellation's comments, the allocation of NCPC charges to exports is not changed by ISO-NE's proposal. ISO-NE explains that these charges will continue to be spread over all Day-Ahead Load Obligation in New England.

14. ISO-NE also rejects Constellation's request for compensation for costs incurred because of the proposed revision. ISO-NE states that the import in Constellation's hypothetical case will not receive Day-Ahead NCPC credits precisely because the import is required to clear the fixed export that the same market participant has submitted. In other words, ISO-NE argues that Constellation is seeking compensation for the difference between the LMP and the offer price of the import on the "netted-out" import, which is exactly the compensation that the proposed changes seek to preclude due to a potential for market manipulation.

15. ISO-NE opposes Constellation's request for a sunset date of April 17, 2008. ISO-NE opposes an arbitrary deadline that could preclude full consideration of the issues and potential solutions.

16. With respect to NSTAR's comments, ISO-NE states that it will fully consult with stakeholders about additional or alternative revisions, and that both the internal market monitoring unit and the external independent market advisor for New England have reviewed the market rule changes and found them to be an appropriate interim response to this situation.

IV. Deficiency Letter

17. On November 16, 2007, the Director, Division of Tariffs and Market Development—East (Director) issued a deficiency letter seeking additional information about ISO-NE's rationale for not using congestion pricing in external transactions. The deficiency letter also requested that ISO-NE explain whether congestion pricing for external nodes is required by Market Rule 1, and if so, whether it would eliminate the opportunity for market manipulation in this case.

18. In its response to the deficiency letter, ISO-NE emphasizes that it did not propose any changes to the application of congestion pricing at External Nodes, but merely attempted to address a gaming opportunity arising from "an asymmetry in the allocation of charges and credits for [NCPC]."[5]

19. ISO-NE states that the clearing of transactions at External Nodes follows the same optimization logic as the clearing of supply and demand at any other location in the wholesale electricity market. ISO-NE explains that the shadow price[6] of binding constraints fully reflects the marginal cost of serving the next increment of load at the External Node; however, this shadow price does not establish the clearing price. ISO-NE states that the published clearing price is the clearing price of the adjacent internal nodes, and that the cost of congestion at External Nodes in the Day-Ahead Energy Market is thus reflected as an NCPC payment rather than in congestion costs.

20. ISO-NE states that the real-time clearing price at the External Node is always equal to the price at the adjacent internal nodes,[7] and that the difference in the way that internal and external constraints are managed is the reason that congestion costs only occur on internal nodes. ISO-NE explains that transactions on external interfaces are physically scheduled such that the limits of the facility are maintained while internal congestion is managed via the economic dispatch of generation on either side of a binding internal constraint.

21. ISO-NE asserts that this practice is consistent with its Tariff, specifically, sections III. 2.5(a), III.2.6(a), and III.7.2.2 of Market Rule 1. Finally, ISO-NE argues that congestion pricing may not prevent the opportunity for market manipulation that it has identified.

22. Notice of ISO-NE's response to the deficiency letter was also published in the *Federal Register*,[8] with comments and interventions due on or before December 7, 2007. No comments or interventions were filed.

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[5] ISO-NE's November 28, 2007 Deficiency Response at 3.

[6] ISO-NE does not define or describe the term "shadow price" in its response.

[7] ISO-NE further notes that "[t]he decision to reflect congestion at External Nodes in the Day-Ahead Energy Market via NCPC payments rather than through LMPs was made to provide consistency between the pricing at the External Node in day ahead and in real time." ISO-NE's November 28, 2007 Deficiency Response at 4.

[8] 72 Fed. Reg. 69,203 (2007).

V. Commission Determination

A. Procedural Matters

23. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,[9] the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

24. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure,[10] prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept ISO-NE's answer because it has provided information that assisted us in our decision-making process.

B. ISO-NE's Proposal

25. We will accept and nominally suspend the revision to Market Rule 1, effective October 17, 2007, subject to refund, and to the outcome of a technical conference, which we order the Commission's staff to convene within 60 days of the date of this order.

26. We agree with ISO-NE that its proposed revisions could prevent market manipulation to the extent that congestion is not priced in external transactions. ISO-NE has identified a way that market participants can manipulate the market by recreating these conditions; specifically, by scheduling high-priced offsetting day-ahead transactions across the interface. This situation arises because of the asymmetrical nature of the NCPC uplift mechanism. The NCPC uplift is allocated to all market participants on a load ratio share basis; therefore, a participant that schedules certain transactions across the interface would only be allocated a small portion of the congestion cost while receiving all of the congestion revenues included in the NCPC that are related to its transaction. ISO-NE's proposed solution makes market participants ineligible to receive NCPC credits on any offsetting external transactions that clear the Day-Ahead Energy Market when the external interface is binding. We conclude that that ISO-NE's proposal effectively addresses the opportunity for manipulation it has identified, and eliminates the incentive for market participants to schedule offsetting transactions that would result in excessive NCPC payments.

27. With respect to Constellation's protest, we agree with ISO-NE that Constellation misinterprets the proposed tariff changes with respect to NCPC charges to exports. ISO-NE is not proposing to change the method used to allocate NCPC uplift charges. Rather, ISO-NE is proposing a solution to an opportunity for market manipulation that leaves the

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[9] 18 C.F.R. § 385.214 (2007).

[10] *Id*. § 385.213(a)(2).

allocation of NCPC uplift unchanged. Accordingly, we reject Constellation's argument in this regard.

28. We also reject Constellation's request that we require ISO-NE to compensate an importer for all of its costs due to LMP differentials between the External Node and its bid. Under ISO-NE's proposal, market participants are disallowed NCPC credits only when the import is required to clear the fixed export that the same market participant has submitted. Constellation's request effectively seeks compensation for the difference between the LMP and the offer price of an import on "netted-out" energy, *i.e.*, the congestion costs collected by NCPC. We agree with ISO-NE that this is precisely the type of transaction that this filing is designed to address.

29. We also reject Constellation's request for a specific sunset date. These revisions are designed to eliminate an opportunity for participants to manipulate the market; consequently, we do not believe it is appropriate to specify a date when they will expire. Moreover, we agree with ISO-NE that establishing an arbitrary sunset date may inhibit stakeholders from engaging in a full and thorough consideration of the issues. If stakeholder discussions result in an alternative solution, ISO-NE may make a new section 205 filing to further revise Market Rule 1.

30. Finally, we agree with ISO-NE that good cause exists to grant waiver of the Commission's 60-day notice requirement.[11] Accordingly, we grant waiver and accept and nominally suspend the revision to Market Rule 1, effective October 17, 2007.

C. Technical Conference

31. Although we agree that ISO-NE's proposed revisions could prevent market manipulation, we note that it appears that the opportunity for manipulation arises because ISO-NE does not price congestion in the LMP at External Nodes. Instead, congestion costs are recovered through an uplift charge, the NCPC.

32. Although ISO-NE maintains in its response to the deficiency letter that the Tariff does not require congestion pricing, it has yet to explain section III.2.6(a), which refers to congestion costs and appears to require ISO-NE to determine an LMP at external nodes that includes the cost of congestion. Section III.2.6(a), in relevant part, states:

> **Calculation of Day-Ahead Nodal Prices.** . . . . Such prices shall be determined in accordance with the provisions of this Section applicable to the Day-Ahead Energy Market and shall be the basis for the settlement of purchases and sales of energy, costs for losses *and Congestion Costs* resulting from the Day-Ahead Energy Market. . . . . In performing this

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[11] *Central Hudson*, 60 FERC ¶ 61,106 at 61,337.

> calculation, the ISO shall calculate the cost of serving an increment of load *at each Node and External Node* from each Resource associated with an eligible energy offer of bid as the sum of: (1) the price at which the Market Participant has offered to supply an additional increment of energy from the Resource of reduce consumption from the Resource; (2) *the effect on transmission Congestion Costs* (*whether positive or negative*) associated with increasing the output of the Resource or reducing consumption of the Resource, based on the effect of increased generation from that Resource or reduced consumption from a Resource on transmission line loading; and (3) the effect on transmission losses caused by the increment of load and generation. The energy offer or offers and energy bid or bids that can serve an increment of load *at a Node or External Node* at the lowest cost, calculated in this manner, shall determine the Day-Ahead Price at that Node.[12]

33. Although ISO-NE's deficiency response refers to the "shadow price," this term is not used in section III.2.6(a), which does not distinguish between shadow prices and clearing prices.[13] Moreover, ISO-NE does not reference any section of its Tariff that provides authority to establish clearing prices at an External Node either (i) at the clearing price of the adjacent internal node, or (ii) at any other level other than the level described in sections III. 2.5(a) and III.2.6(a) of the Tariff.

34. In its deficiency response, ISO-NE requested that the Commission convene a technical conference. We conclude that a technical conference is necessary to determine whether further detail should be added to the Tariff to capture ISO-NE's proposal and its current practice of using NCPC to resolve differences in clearing prices across interfaces. Accordingly, we direct Commission staff to convene a technical conference within 60 days of the date of this order and to report back to the Commission the results of the technical conference within 60 days of the conference. The Commission will issue another order based on the additional information gathered in the technical conference.

35. As part of its presentation, we direct ISO-NE to discuss whether removing congestion costs from the NCPC uplift mechanism and incorporating these costs in the LMP at the External Node, as the Tariff appears to require, would reduce or eliminate the opportunity for market manipulation that is the impetus for this filing.

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[12] ISO-NE FERC Electric Tariff No. 3, original sheet Nos. 7138-7141 (emphasis added).

[13] Although the instant filing pertains to the Day-Ahead Market, we note that the same is true for section III. 2.5(a), which addresses the calculation of Real-Time Nodal Prices.

The Commission orders:

(A) ISO-NE's proposed revision to Market Rule 1 is hereby accepted for filing and suspended for a nominal period, to become effective October 17, 2007, as requested, subject to refund, as discussed in the body of this order.

(B) The Commission's staff is directed to convene a technical conference to address issues raised by ISO-NE's filing within 60 days of the date of this order, and to report back to the Commission the results of the technical conference within 60 days of the date of the conference. The Commission will issue another order based on the additional information gathered in the technical conference.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.