

126 FERC ¶ 61,115
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

ISO New England Inc. and
New England Power Pool Participants Committee

Docket No. ER09-356-000

ORDER ACCEPTING TARIFF REVISIONS
AND REQUIRING COMPLIANCE FILING

(Issued February 13, 2009)

1. In this order, the Commission accepts tariff changes submitted by ISO New England, Inc. (ISO-NE) and the New England Power Pool (NEPOOL) Participants Committee (collectively, the Filing Parties) revising certain provisions of New England's Forward Capacity Market (FCM). In addition, we require a compliance filing, as discussed below.

I. Background

A. FCM

2. ISO-NE has recently implemented a forward market for capacity, pursuant to which capacity resources (both generators and demand resources) compete to provide capacity to New England, on a three-year-forward basis, by participating in an annual Forward Capacity Auction. Providers whose capacity clears the Forward Capacity Auction acquire capacity supply obligations, which they must fulfill three years later. Prior to the delivery year, parties can adjust their capacity supply obligations, and ISO-NE can increase or decrease the amount of capacity it anticipates needing, in periodic reconfiguration auctions. ISO-NE held the first two Forward Capacity Auctions in 2008, the third Forward Capacity Auction will be held in October 2009, and the fourth Forward Capacity Auction will be held in August 2010.

B. The Instant Filing

3. On December 1, 2008, the Filing Parties proposed changes to several aspects of the markets rules governing the FCM. The instant revisions largely expand the details

behind several previously existing market rules. In particular, the Filing Parties propose to revise or create market rules, including rules addressing:

- the reconfiguration auctions, including the qualification of capacity for those auctions and various related timing issues;
- identification of ISO-NE's role in reconfiguration auctions;
- the bilateral contracts for both supply and load obligations;
- arrangements for supplementing resource availability; and
- the reliability review performed by ISO-NE for reconfiguration auctions and bilateral contracts.

4. The Filing Parties further stated that stakeholders have raised issues regarding the limits that the proposed rules placed on the tradability of capacity, especially the requirements of the reliability review process and the use of any reliability review beyond the Local Sourcing Requirement. Some parties have also questioned the use of

different reliability standards in different contexts, in particular ISO-NE's reliance on a probabilistic approach that focuses on resource adequacy when establishing Local Sourcing Requirements and Capacity Zones for the FCA, while relying on a deterministic approach that focuses on system security (including the transmission security analysis) when performing reliability reviews applied to resources that seek to de-list or trade their obligations.¹

5. According to the Filing Parties, the argument is that the current use of a probabilistic approach could result in a failure to model separate Capacity Zones for the Forward Capacity Auctions when local security concerns could support zonal separation. The parties contend that this has an impact on how much capacity will be procured within a zone and the price of that capacity.

6. As discussed elsewhere in this order, to address these concerns, the Filing Parties propose a stakeholder process, to begin in the first quarter of 2009, to address additional issues related to the FCM, culminating in a Commission filing no later than February 20, 2010, which would enable new rules to be in place before the Installed Capacity Requirements and Informational Filings must be made for the 2013-2014 Power Year and the fourth Forward Capacity Auction.

¹ December 1 filing, Transmittal Letter (Transmittal Letter) at 4.

7. The Filing Parties request an effective date for this tariff change of February 16, 2009.

C. Notice of Filings

8. Notice of the filing was published in the Federal Register, with motions to intervene, notices of intervention, comments and protests due on or before December 22, 2008.² The FirstLight Parties,³ Dominion Resources Services, NRG Companies, Exelon, Northeast Utilities Service Company, and BG Energy Merchants filed timely motions to intervene. The PSEG Power Companies (PSEG), Dynegy Power Marketing (Dynegy), the New England Power Generators Association (NEPGA) and the Mirant Parties (Mirant) filed timely motions to intervene and protests or comments. ISO-NE and NEPOOL filed separate answers to the protests.

II. Discussion

A. Procedural issues

9. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.214 (2008)), the notice of intervention and the timely-filed unopposed motions to intervene serve to make the entities filing them parties to this proceeding.

10. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2008), prohibits an answer to a protest or an answer unless otherwise ordered by the decisional authority. We will accept the answers filed by ISO-NE and NEPOOL because they have provided information that has assisted us in our decision-making process.

B. Supplemental Availability Bilaterals

1. Filing Parties' Proposal

11. Under the current FCM rules, each generating capacity resource that takes on a capacity obligation receives an "availability score" that measures its availability during shortage events, and if a resource is penalized for unavailability, the penalty it incurs is based in part on this availability score.⁴ The FCM rules allow a resource to increase its availability score during a shortage event by supplementing it with the performance of a

² 73 Fed. Reg. 78,772 (2008).

³ FirstLight Power Resources Management, LLC, FirstLight Hydro Generating Company and Mt. Tom Generating Company LLC.

⁴ See ISO-NE Tariff, Market Rule 1, section III.13.7.1.1.2.

resource without a Capacity Supply Obligation during that event. However, the current rules do not set forth the means by which this will be accomplished.⁵

12. Therefore, the Filing Parties propose the following mechanism. A resource that does not currently have a Capacity Supply Obligation (and is therefore not receiving a capacity payment) may be designated prospectively as a Supplemental Capacity Resource. Once so designated, the Supplemental Capacity Resource must also offer its capacity into the day-ahead energy market. If there is a shortage event, a capacity resource that failed to meet its obligations during the shortage event can enter into a Supplemental Availability Bilateral agreement, after the fact, which enables the deficient capacity resource to supplement its availability score with the capacity provided by the supplemental capacity resource. These Supplemental Availability Bilaterals are a way for resources that have capacity obligations to hedge against the risks that they themselves will fail to meet those obligations.

13. The instant proposal develops the Supplemental Availability Bilateral mechanism, outlining the identification of resources, amount being transferred in megawatts, and the term of the transaction. A Supplemental Availability Bilateral does not transfer a Capacity Supply Obligation. However to ensure the substitute resource is actually capable of electrically supplementing the availability of the unavailable resource, the Supplemental Capacity Resource and Supplemental Capacity Resource must be located in the same Reserve Zone.⁶

2. Protests and Answers

14. While generally supportive of the Supplemental Availability Bilateral construct, PSEG disagrees with the requirement that the Supplemental Availability Bilateral resource be located in the same Reserve Zone as the resource with the original Capacity Obligation. Consistent with the other generator parties, PSEG argues that this requirement reveals the flaw underlying the current design – the use of a probabilistic reliability standard for establishing Installed Capacity Requirements and Local Sourcing Requirements compared to the deterministic Transmission Security Analysis standard

⁵ See *id.*, section III.13.7.1.1.4, and FCM Settlement Agreement section 11, part V.C.4.

⁶ Under section III.2.7.c of Market Rule 1, Reserve Zones shall be established by ISO-NE which represents areas within the New England Transmission System that require local 30 minute contingency response as part of normal system operations in order to satisfy local second contingency response reliability criteria. In addition, section III.12.7.d establishes a Reserve Zone which represents the remaining areas within the New England Transmission System that are not included within the Reserve Zones established under section III.2.7(c).

when evaluating reliability needs. PSEG contends that units should be deemed substitutable Supplemental Availability Bilateral resources when they are located in the same FCM Capacity Zone, as the need for separate Capacity Zones is determined through the existence or absence of price separation in the Forward Capacity Auction. PSEG argues that since capacity is not locationally procured in a Forward Capacity Auction based on its Reserve Zone, applying this criterion for substitutability of resources is without basis. As such, PSEG requests that the Commission direct ISO-NE to replace the term “Reserve Zone” from Section III.13.5.3.2 of Market Rule 1 with “Capacity Zone.”⁷

15. PSEG argues that the ability to utilize a Supplemental Availability Bilateral from within the same Capacity Zone is not a reliability issue. In support, PSEG notes that a Supplemental Availability Bilateral does not transfer a capacity obligation. As such, PSEG states that the obligation of the capacity resource to perform is unaffected by the availability of Supplemental Availability Resources. Second, PSEG argues that since the assignment of a Supplemental Availability Bilateral transaction takes place after the shortage event has occurred (and ISO-NE has already taken all appropriate actions to manage the shortage event), no Supplemental Availability Bilateral transaction can affect the ability of ISO-NE to manage the system through the shortage event. Thus, PSEG argues that Supplemental Availability Bilaterals are simply a settlement accounting mechanism which creates incentives for resources without Capacity Supply Obligations to offer their services in the day ahead and real time energy markets. Last, PSEG notes that since Supplemental Availability Bilateral transactions are used only to fulfill Capacity Supply Obligations during Shortage Events and because Shortage Events cannot occur in individual Capacity Zones unless the zone experienced price separation in the Forward Capacity Auction, then capacity from anywhere in the region should be a fully substitutable product. In addition, PSEG states that because it has been long standing practice in ISO-NE to look to energy imports from neighboring control areas during capacity deficiencies to help restore the system to normal operations, it would be inconsistent to adopt a mechanism whereby internal resources to the pool are not deemed to provide the same benefits as external resources when managing capacity deficiencies.

16. Addressing PSEG’s concern, NEPOOL contends that the issue for the Commission in this proceeding is whether the Reserve Zone restriction for Supplemental Availability Bilateral Transactions is just and reasonable, and not whether an alternative restriction based on Capacity Zones is also just and reasonable. NEPOOL acknowledges that ISO-NE may be able to maintain reliability while reducing the restrictions on Supplemental Availability Bilateral Transactions. However, NEPOOL argues that the instant filing proposes to restrict the transfer of Supplemental Availability Bilateral

⁷ Under section III.13.2.3.4 of Market Rule 1, after the Forward Capacity Auction is concluded for all modeled Capacity Zones, the final set of Capacity Zones shall be those having distinct Capacity Clearing Prices as a result of constraints between modeled Capacity Zones binding in the running of the Forward Capacity Auction.

Transactions across Reserve Zones in the interest of enhancing reliability by increasing the likelihood that, during a Shortage Event, a substitute resource will actually be able to contribute to the real-time resolution of the problem. NEPOOL notes that there was an unsuccessful attempt during the stakeholder process to implement the change now sought by PSEG, which received only a 41.59% Vote in favor.

17. In its answer, ISO-NE contends that PSEG's arguments overlook important reliability implications. Addressing PSEG's point that because Supplemental Availability Bilaterals are entered into after a Shortage Event rather than before, they cannot present a reliability issue, ISO-NE argues that if protecting reliability in real time was the only consideration, then PSEG's arguments might have merit. However, ISO-NE contends that expanding the limitation on Supplemental Availability Bilaterals beyond a Reserve Zone would dilute important incentives to perform in real time, by expanding greatly the pool of potential supplementing resources, negating the reliability analyses performed in support of the Forward Capacity Auction, reconfiguration auctions, and bilateral transactions.

18. As an example, ISO-NE states that the owner of a resource whose de-list bid is rejected for a reliability need could effectively ignore such a rejection, and just submit Supplemental Availability Bilateral Transactions – which are not themselves subject to reliability reviews – with remote resources on any day when the system was in shortage, receiving payment for capacity service while failing to meet the reliability need that prevented the resource from being allowed to de-list. ISO-NE states that such a scenario would diminish the effect of Shortage Hour availability provisions which are intended to incent the availability of capacity resources and allow for operational predictability. ISO-NE states that by restricting Supplemental Availability Bilaterals to resources located in the same Reserve Zone, and thus reflecting the most significant interface constraints monitored by ISO-NE in real-time operation, it is virtually certain that the substitute resource is able to make a similar contribution to resolution of reliability problems as the supplemented resource. ISO-NE avers that since PSEG has not shown that the use of Reserve Zones in this manner is not just and reasonable, then its alternate proposal must be rejected.

19. Last, ISO-NE acknowledges that the stakeholder process that it commits to in the instant filing includes a comprehensive review of the use of Capacity Zones in the Forward Capacity Market. ISO-NE states that the primary reason for this review is to consider whether different treatment of Capacity Zones will affect the tradability of capacity obligations through reconfiguration auctions and bilateral contracts. As such, ISO-NE states that PSEG should raise these related issues concerning Supplemental Availability Transactions in the context of the upcoming stakeholder process.

3. Commission Conclusion

20. We reject PSEG's protest in this matter. As PSEG is aware, and as other generator parties have noted, the issue from the generator's perspective (and the subject of the stakeholder process offered by the Filing Parties) is that there is currently a different standard in place for the establishment of Local Sourcing Requirements and Capacity Zones in support of a Forward Capacity Auction relative to the reliability review that ISO-NE performs for resources seeking to de-list from the Forward Capacity Auction or trade their obligation either bilaterally or through a Reconfiguration Auction. As such, the Filing Parties specifically note that several parties object to ISO-NE's use of a probabilistic approach driven by resource adequacy in the establishment of Local Sourcing Requirements/Capacity Zones for the Forward Capacity Auction while relying on a deterministic system security approach to perform reliability reviews. The Filing Parties state that these protesting parties contend that the use of the probabilistic standard fails to recognize local security concerns that could allow for zonal separation, directly impacting the amount of capacity required in particular zones and thus, zonal capacity prices.⁸ As such, the Filing Parties note that opposition to the instant proposal from the generation sector rests largely on this fundamental disagreement, rather than the details of the instant rules.

21. While the Commission has previously found the use of these different standards to be consistent with ISO-NE's tariff,⁹ we have also indicated our preference that this issue be addressed in the NEPOOL stakeholder process.¹⁰ In the instant filing, the Filing Parties have committed to initiating this stakeholder process in the first quarter of 2009 "to address the interrelated issues of: application of the transmission security analysis and its parameters, how Capacity Zones and Local Sourcing Requirements are established and aligning the standards to be used in establishing those zones and requirements with those used in performing reliability reviews."¹¹ Expressing concern about the complexity of the issues relative to the timeline, the Filing Parties have committed to a subsequent Commission filing no later than February 20, 2010 in time for the fourth Forward Capacity Auction. As detailed elsewhere in this order, we support

⁸ Transmittal Letter at 4.

⁹ *ISO New England Inc.*, 123 FERC ¶ 61,290, at P 29-31 (2008).

¹⁰ *ISO New England Inc.*, 125 FERC ¶ 61,154, at P 60 (2008); *ISO New England Inc.*, 123 FERC ¶ 61,290 at P 27-28, 36, 82 (rehearing requests by Richard Blumenthal, Attorney General for the State of Connecticut, Connecticut Department of Public Utility Control, and others pending); *ISO New England Inc.*, 125 FERC ¶ 61,102, at P 114 (2008).

¹¹ Transmittal Letter at 5.

this stakeholder process and will require ISO-NE to meet this February 20, 2010 deadline.

22. The Commission is aware that improvements can be made in the aforementioned stakeholder process to better coordinate local security concerns into the determination of Local Security Requirements and Capacity Zones. Such improvements may eliminate PSEG's stated concern. However, we do not agree with PSEG's contention that Supplemental Availability Bilaterals are simply a settlement accounting mechanism. It is important that this mechanism maintains the incentive for resources to maximize their availability, rather than using Supplemental Availability Bilaterals to render ISO-NE's reliability determinations meaningless. For example, ISO-NE demonstrates why PSEG's approach, allowing for Supplemental Availability Bilaterals within Capacity Zones rather than Reserve Zones, cannot be supported. Under PSEG's approach, during a system shortage, a resource with a rejected de-list bid (because, for example, the resource is required to address a local security concern, for example voltage support) could simply submit Supplemental Availability Bilateral Transactions with a remote resource. This would allow the needed resource to receive payment for capacity service while failing to meet the reliability need that prevented the needed resource from being allowed to de-list. To prevent these situations, we find the Filing Parties' requirement that the Supplemental Availability Bilateral Resource be located in the same Reserve Zone as the resource with the original Capacity Obligation to be just and reasonable, as it is more likely that the Supplemental Availability Bilateral Resource would be able to address the identified reliability issue. We therefore reject PSEG's request to allow units to be deemed substitutable Supplemental Availability Bilateral resources when they are located in the same FCM Capacity Zone.

C. Entry of Demand Bid for Potentially Unavailable Resources

1. Filing Parties' Proposal

23. New section III.13.4.2.1.3 addresses adjustments for significant decreases in capacity for the third annual reconfiguration auction. Under the proposed rules, a resource with a Capacity Obligation may cure any potential shortfall with a plan to fix the resource or may shed the obligation through an annual bilateral contract. If the shortage is not cured, ISO-NE will submit a demand bid on behalf of the resource in the third annual reconfiguration auction.

2. Protest and Answers

24. Mirant contends that the instant proposal seeks to revise the FCM rules to increase the potential unavailability penalty for capacity resources, in conflict with language in the FCM Settlement Agreement stating that there should be strong economic incentives for capacity resources to be available when needed without creating unnecessary payment risk to resources. Specifically, Mirant notes that under the instant proposal, if ISO-NE

believes that a capacity resource will not be able to meet its capacity supply obligation as the applicable commitment period approaches, then ISO-NE will enter a demand bid at 2.0 times the Cost Of New Entry (CONE) on behalf of the resource in the third annual reconfiguration auction (i.e., the unavailable resource will be forced to purchase replacement capacity). Mirant notes that in addition to this payment, a resource would continue to have its FCM payments adjusted for unavailability if the full capacity supply obligation of the resource were not transferred to others through the reconfiguration auction. Mirant contends that this proposal would result in the imposition of significant penalties on a resource in the event of its projected unavailability which could result in total payments from the resource that exceed its annual FCM payments. While arguing that the proposal deviates from the current availability-adjusted payments under the shortage hour construct, Mirant also argues that the proposal is not just and reasonable because it violates the Commission's long-standing mandate that "[p]enalties be narrowly designed to balance the need to deter conduct that is harmful to the system with the need to limit excessive and unnecessary costs."¹²

25. Mirant further contends that ISO-NE cannot justify its proposed revisions to the unavailability provisions on the system reliability, security, competitiveness, or efficiency as required under section 4 of the FCM Settlement Agreement. Mirant notes that the Filing Parties cannot argue that the proposed changes are triggered by reliability concerns, given that the calculation of the Installed Capacity Requirement (ICR) expressly factors in a reserve margin to address the fact resources are not available one hundred percent of the time. In addition, Mirant states that the instant proposal for ISO-NE to enter a demand bid on behalf of capacity resources would effectively force resources to participate in the third annual reconfiguration auction as purchasers. Mirant argues that this contrasts with the FCM Settlement Agreement provision finding that participation in reconfiguration auctions is voluntary. Mirant also contends that there is no provision in the FCM Settlement Agreement for ISO-NE to participate in reconfiguration auctions based on the anticipated unavailability of a resource.

26. NEPOOL, in its answer, notes that while the proposal addresses details regarding how ISO-NE would handle adjustments for significant decreases in capacity, the proposal does not represent a "radical change" as characterized by Mirant. Instead, NEPOOL and ISO-NE state that the ability of ISO-NE to enter a demand bid on behalf of a resource that will be unable to meet its Capacity Supply Obligation has already been accepted by the Commission on June 5, 2007 as part of the original FCM market rule filing.¹³ Thus, ISO-NE states that, contrary to Mirant's implication, there is no such proposal in the

¹² Mirant protest at 8, citing *Mirant Kendall, LLC*, 110 FERC ¶ 61,272, at P 17 (2005).

¹³ In support, NEPOOL and ISO-NE cite *ISO New England Inc.*, 119 FERC ¶ 61,239 (2007).

instant proposal for the Commission to reject. NEPOOL and ISO-NE offer that while the proposal revises some of the more particular aspects of this rule,¹⁴ Mirant does not appear to take issue with those changes. Thus, to the extent Mirant's concerns focus on the ability of ISO-NE to submit a demand bid on behalf of a resource, NEPOOL avers that Mirant's arguments constitute a collateral attack and should be rejected by the Commission.

27. Addressing the general position offered by Mirant that the instant proposals contravene the letter and purpose of the FCM Settlement Agreement, NEPOOL states that section 4 of the FCM settlement Agreement expressly permits full Section 205 and Section 206 filings relating to the FCM Market Rules following September 5, 2008. NEPOOL states that that date ended the "Waiver Period" under the FCM settlement, making inapplicable the language quoted by Mirant as to any "extra" showings required by ISO-NE for section 205 filings. Thus, NEPOOL offers that while the understandings reflected in the terms of the FCM settlement agreement are relevant to whether changes should be accepted as just and reasonable, they no longer impose the specific limitations reflected in section 4.

28. ISO-NE states that the significant decrease provisions are not redundant penalty provisions, as Mirant states, but are distinct from the availability provisions in the rules. ISO-NE states that the significant decrease in capacity provisions are part of a larger mechanism in the FCM rules designed to ensure that the region has procured sufficient resources to meet the ICR as of the start of the Capacity Commitment Period. By contrast, the availability provisions are designed to ensure that the resources procured and paid to provide that capacity actually provide that capacity during the Capacity Commitment Period. ISO-NE states that Mirant's implication that the availability provisions provide sufficient economic incentives such that ISO-NE should not be concerned with a resource's actual capacity rating, operational status, or construction completion schedule before the start of the Capacity Commitment Period ignores critical reliability implications.

3. Commission Conclusion

29. Mirant challenges the provision that allows ISO-NE to enter a demand bid at 2.0 times CONE on behalf of a resource in the third (and final) annual reconfiguration auction if it concludes that the capacity resource will not be able to meet its capacity supply obligation as the applicable commitment period approaches. Among other

¹⁴ For example, ISO-NE explains rather than compare a resource's most recent Seasonal Claimed Capability to its Qualified Capacity (as described in currently-effective III.13.6.1.1.4), it is appropriate to compare its qualified capacity for the third annual reconfiguration auction to its Capacity Supply Obligation for the Capacity Commitment Period (as reflected in new section III.13.4.2.1.3).

contentions, Mirant argues that ISO-NE's approach is inconsistent with section 4.A of the FCM Settlement Agreement.¹⁵

30. Citing to this section, Mirant contends that the restriction on ISO-NE's ability to revise the FCM market rules pursuant to section 205 (specifically its required demonstrations before the Commission) will only end when the prices from the second Forward Capacity Auction become final, stating that "as the waiver period is still in effect, ISO-NE continues to be subject to this restriction."¹⁶ We disagree. While any section 205 filing is subject to the just and reasonable standard, we note that this settlement language, which terminates the Waiver Period at the earlier of September 5, 2008 or the date on which the second Forward Capacity Auction prices become final, terminated the Waiver Period on September 5, 2008, eliminating these additional requirements. Further, we have noted the expiration of the Waiver Period in a previous Commission order.¹⁷

31. Addressing the merits of Mirant's concern about the proposal being punitive and redundant in light of the already existing FCM availability penalties, we agree with the

¹⁵ Section 4.A of the FCM Settlement Agreement states the following:

From March 6, 2006 through the earlier of September 5, 2008 or the date on which the prices from the second FCA become final (the Waiver Period), the Settling Parties waive their rights under Section 206 of the FPA to seek to modify the terms of this Settlement Agreement or, except as provided in Section 3.B, the Market Rules approved or accepted by the FERC to implement the Forward Capacity Market. Except as provided in Section 4.C, during the Waiver Period, the ISO shall retain its authority under Section 205 of the FPA to file modifications of the Market Rules that address the terms of the Settlement Agreement; where the ISO makes such a filing, the ISO must demonstrate to the FERC that failure to implement the proposed change in the Market Rule would have a negative effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. If the ISO makes such a filing, then the Settling Parties shall retain all rights to challenge the modification proposed by the ISO before the FERC.

¹⁶ Protest at fn 10.

¹⁷ *ISO New England Inc.*, 125 FERC ¶ 61,355, at P 37 (2008).

Filing Parties that this construct already has been approved by the Commission when we approved current section III.13.6.1.1.4.¹⁸ Specifically, that section currently states that if a resource with a capacity obligation has a Summer Seasonal Claimed Capability below its summer Qualified Capacity (pursuant to certain thresholds), then “the ISO shall enter a demand bid at 2.0 times CONE on behalf of the Market Participant in the reconfiguration auction to replace the missing capacity in the appropriate Capacity Zone in the last annual reconfiguration auction prior to the Capacity Commitment Period.”¹⁹

32. We also agree with the Filing Parties that Mirant’s protest does not concern the details of how this mechanism is implemented, but the actual existence of the mechanism itself. As the Filing Parties note, new section III.13.4.2.1.3 that Mirant disputes here is the result of moving and revising currently-effective sections III.13.6.1.1.4 and III.13.6.1.3.2. As we have already approved this proposal in June 2007, we dismiss Mirant’s arguments as a collateral attack on that order.²⁰ Further, addressing Mirant’s redundancy argument, we note that the availability provisions, which provide an incentive for capacity resources to perform during the Capacity Commitment Period are distinct from the significant decrease in capacity provisions discussed here, which seek to ensure that ISO-NE procures the ICR prior to the Capacity Commitment Period.

D. Participation of Local Transmission Owner in Reliability Reviews

1. Filing Parties' Proposal

33. The Filing Parties propose to revise the FCM rules so that ISO-NE will conduct a reliability review to determine whether any Capacity Supply Obligation Bilateral contract²¹ would result in the violation of any North American Electric Reliability Corporation (NERC) or Northeast Power Coordinating Council (NPCC) criteria or

¹⁸ *ISO New England, Inc.*, 119 FERC ¶ 61,239 (2007).

¹⁹ FERC Electric Tariff No. 3, Original Sheet No. 7316R Market Rule 1, section 13.6.1.1.4.

²⁰ Of note, though it intervened in that proceeding, Mirant did not dispute that provision.

²¹ Capacity Supply Obligation Bilateral contracts "allow suppliers to exchange Capacity Supply Obligations - the Capacity Acquiring Resource gains a Capacity Supply Obligation and the Capacity Transferring Resource sheds a Capacity Supply Obligation for the period of the bilateral, subject to specified requirements. Capacity Supply Obligation Bilaterals allow for negotiations between parties, meeting the commercial desire to have one-to-one trading of obligations and providing flexibility to market participants to respond to changes in circumstances." Transmittal Letter at 12.

ISO-NE system rules. ISO-NE states that the reliability review is intended to ensure that regional and local adequacy and other reliability needs are maintained. The proposal also states that, "[f]or a monthly Capacity Supply Obligation Bilateral, a Capacity Supply Obligation cannot be shed by a Transferring Resource if the Local Control Center determines it is needed for local system conditions and is not adequately replaced by the Acquiring Resource."²²

2. Protest and Answers

34. Mirant argues that this provision, which permits a local transmission owner to prevent a monthly Capacity Supply Obligation Bilateral due to local reliability issues, is not necessary, since ISO-NE by itself has the ability to conduct a thorough reliability review of such contracts, including considering any local reliability concerns. Mirant argues that while it does not object to the participation of a transmission owner in the reliability review process, the proposed language would give the local transmission owner a veto right over monthly Capacity Supply Obligation Bilaterals, with no restrictions as to the transmission owner's ability to exercise this right. Mirant asserts that such a veto right would violate the requirement that a Regional Transmission Organization's decision-making process be independent of control by any market participant or class of participants.

35. ISO-NE states in its response that its ability to take into account local reliability concerns is based largely on input from local transmission owners, and that ISO-NE does not have the resources or means independently to survey the transmission system down to the local distribution level. ISO-NE states that "[i]f a Local Control Center indicates that a proposed bilateral creates local reliability problems, the ISO will defer to that determination and proceed accordingly,"²³ and that Mirant is objecting to language which simply codifies and makes transparent that deference. ISO-NE also states that in other proceedings the Commission has approved the participation or involvement of other entities when those entities have critical input to reliability determinations. ISO-NE notes that Mirant's argument that the FCM Settlement Agreement does not contemplate transmission owner involvement in the review of Capacity Supply Obligation Bilaterals is without merit, since the FCM Settlement Agreement provides few details about bilaterals at all, and required elaboration. ISO-NE finally notes that, as the Commission recently stated, "all parties [to the Settlement Agreement] were aware that, after a period during which parties waived their rights to seek changes to the Settlement's provisions or

²² Proposed Tariff section III.13.5.1.1.3(b).

²³ ISO-NE answer at 17.

the related market rules, any party (including ISO-NE and NEPOOL) could seek to make such changes."²⁴

36. NEPOOL argues in its response that the Commission's prior ISO-NE orders contemplate an active role for local transmission owners in matters of local reliability. It further notes, however, that that role is subject to the oversight of the Commission and ISO-NE, and that the rule changes proposed here empower local transmission owners to reject transactions that compromise local reliability; they do not provide local transmission owners with unchecked power.

3. Commission Conclusion

37. The Filing Parties propose the following language at section III.13.5.1.1.3(b):

For a monthly Capacity Supply Obligation Bilateral, a Capacity Supply Obligation cannot be shed by a Transferring Resource if the Local Control Center determines it is needed for local system conditions and is not adequately replaced by the Acquiring Resource.

In accordance with this language, ISO-NE states that it will "defer" to the determination of Local Transmission Owners that a monthly Capacity Supply Obligation Bilateral will compromise reliability, and reject the bilateral contract accordingly.

38. The Commission agrees with Mirant that the position stated by ISO-NE – namely, that ISO-NE will automatically "defer" to individual transmission owners in deciding whether to approve a Capacity Supply Obligation Bilateral -- is inconsistent with the principle that a Regional Transmission Organization's decision-making authority should be independent of any single market participant or group of market participants. We note, however, that NEPOOL states that while the ISO-NE structure contemplates a role for local transmission owners in matters of local reliability, this role is "subject to the ultimate oversight of ISO-NE and FERC,"²⁵ and that, "while the Rule Changes empower local transmission owners to reject transactions that compromise local reliability, they do not provide local transmission owners unchecked power."²⁶ In light of NEPOOL's clarification of what it views as ISO-NE's obligation, we will require ISO-NE to make a compliance filing, within 30 days of the date of this order, to revise the language of section III.13.5.1.1.3(b) to provide that, in determining whether to accept or reject a monthly Capacity Supply Obligation Bilateral, ISO-NE will obtain and consider a Local

²⁴ *Id.* at 18, citing *ISO New England Inc.*, 125 FERC ¶ 61,355, at P 37 (2008).

²⁵ NEPOOL answer at 9.

²⁶ *Id.*

Control Center's view on whether that bilateral contract will impair reliability, before ISO-NE makes the final determination as to whether or not to accept the Capacity Supply Obligation Bilateral.

E. Disclosure of Bilateral Price to ISO-NE

1. Filing Parties' Proposal

39. The Filing Parties propose that, when parties enter into a Capacity Supply Obligation Bilateral, they should submit certain information to ISO-NE, including "the price, in \$/kW-month, associated with" that contract.²⁷

2. Protest and Answers

40. Mirant disputes the requirement from the instant proposal that parties disclose the price they negotiated with respect to a Capacity Supply Obligation Bilateral. Mirant notes that proposed revisions to section III.13.5.1.1.3 which establishes the standards by which ISO-NE will review information submitted by transacting parties in support of a Capacity Supply Obligation Bilateral, does not provide any indication regarding how such price information could be relevant to ISO-NE's evaluation as to whether to approve a contract. Further, Mirant argues that such information is not relevant for ISO-NE billing or settlement purposes and that providing such commercially sensitive information to ISO-NE is not contemplated in the FCM settlement agreement.

41. ISO-NE states that the intent of this provision was not that the submitted price be the actual, specific contract price negotiated among the parties to the bilateral transaction. Instead, ISO-NE notes that the use of its settlement system requires that some non-zero price be associated with any submitted Capacity Supply Obligation Bilateral since in the absence of a price submitted by the parties to that contract, ISO-NE would enter a default price of \$0.00, forcing the parties to separately settle the contract outside of its system. However, ISO-NE states that it understands Mirant's concern that the rule as written can be read to require submission of the actual, negotiated contract price. As such, ISO-NE states that in the pending stakeholder process addressing the filing of further FCM rule revisions, ISO-NE and the stakeholders should consider revising section III.13.5.1.1.2 to state that the parties to a Capacity Supply Obligation Bilateral "may" submit "a" price for the contract, rather than "shall" submit "the" price associated with the contract, as currently written. ISO-NE argues that no compliance filing should be ordered by the Commission in this instance.

42. In its answer, NEPOOL notes that it is reasonable to permit ISO-NE access to such information if ISO-NE desires it to fulfill its market monitoring or operations roles.

²⁷ Transmittal Letter at 3.

However, NEPOOL acknowledges that ISO-NE's need for this information was not explored and warrants consideration for clarification in the pending stakeholder process.

3. Commission Conclusion

43. We are satisfied with ISO-NE's clarification that section III.13.5.1.1.3 does not require parties to disclose their negotiated price associated with the Capacity Supply Obligation Bilateral to ISO-NE, but simply provides parties the optional ability to use the settlement software. It appears from ISO-NE's and NEPOOL's answers, however, that it is not clear that all the stakeholders share this view of the meaning of that section. We direct ISO-NE to make a compliance filing, within 30 days of the date of this order, to clarify the language of section III.13.5.1.1.3 consistent with its answer.

F. Stakeholder Process

1. Filing Parties' proposal

44. As mentioned previously, to address concerns regarding ISO-NE's use of different reliability standards in different contexts (and as supported by the Commission in prior orders), the Filing Parties have committed to initiate a stakeholder process in the first quarter of 2009.

2. Protest and Answers

45. NEPGA states that while it and its members do not support all the revisions in the instant filing, the objections are principally to market design problems that are best addressed through discussions in the stakeholder process. NEPGA asserts that the stakeholder process suggested by ISO-NE is critical to address design flaws in FCM so that the market procures the full quantity of capacity needed for reliable operations, to ensure resource adequacy and all other appropriate reliability standards, and to ensure that services being procured and the obligations of those resources from which services are procured are comparable if priced comparably. NEPGA states that it accepts ISO-NE's commitment to the stakeholder process and will devote its resources to that process as the best means available at this time to address these issues.

46. NEPGA explains that while the Filing Parties have generally included the important issues to be reviewed in the stakeholder process, the scope of the stakeholder process must include additional issues. According to NEPGA, the scope of the stakeholder process should include: ensuring that the full extent of reliability needs is transparent and purchased through the auction; developing consistent obligations for all capacity resources; ensuring that Out of Market capacity participating in the auctions does not have a detrimental effect on price formation; and ensuring that CONE adequately reflects the actual cost of new entry.

47. Additionally, NEPGA argues that the Commission should require ISO-NE to implement these changes prior to the fourth Forward Capacity Auction because the removal of the price collar²⁸ in the fourth Forward Capacity Auction highlights the urgency of correcting market design flaws immediately. According to NEPGA, the price collar was intended to provide some limits on price during the first three auctions while the region tested the capacity market and gained experience, which has revealed design flaws. NEPGA asserts that in the fourth Forward Capacity Auction, without price limits in the form of a collar, and without correcting the flaws described above, the entire FCM construct will be at risk. While NEPGA believes that the problems identified in the instant filing should be resolved in time for the third Forward Capacity Auction, it recognizes that that may not allow for the full stakeholder process envisioned by ISO-NE, but states that the process should not be allowed to delay needed market reforms any longer than the minimum necessary time. NEPGA asserts that if ISO-NE makes a filing as proposed on February 20, 2010, several important deadlines for the fourth Forward Capacity Auction will already have passed, such as the submittal of new resource qualifications and certain de-list bids (which are due in December 2009), and the lack of resolution of those issues before February 2010 will create difficulties for many participants. NEPGA requests that the Commission direct ISO-NE to consider making its filing prior to the deadlines for submitting de-list bids for the fourth Forward Capacity Auction in December 2009, or, if that is not possible, to consider extending the deadline for these early fourth Forward Capacity Auction submittals so that market participants will have the benefit of any ISO-NE filing resulting from the stakeholder process prior to the deadline for these binding bidding and participation decisions.

48. Dynegy supports the filings submitted in this proceeding by NEPGA and PSEG, and it requests that the Commission grant the relief sought by these parties. In addition, Dynegy states that assuming the Commission does approve any or all of the revisions now proposed, the Commission should do so only upon the express understanding and condition that ISO-NE will engage in a deliberate and thorough stakeholder process to reevaluate and further revise the FCM rules and that it will submit an appropriate filing to the Commission so that such revisions are in place in time for the fourth Forward Capacity Auction, as it has expressly committed to doing in the instant filing.

49. In its answer, NEPOOL argues that the proposed rule changes should be accepted by the Commission as just and reasonable without predetermining or restricting the scope and timing of the upcoming stakeholder process committed to begin in the first quarter of 2009. NEPOOL states that the rule changes contained in the instant filing are the result of extensive work by ISO-NE and NEPOOL to further refine and implement the FCM.

²⁸ Under the terms of the FCM Settlement Agreement, a price collar (establishing a price floor and ceiling) exists until three Successful Forward Capacity Auctions have been conducted in the Rest-of-Pool Capacity Zone, but in no case for more than the first five Forward Capacity Auctions. *See* Market Rule 1, section III.13.2.7.3.

NEPOOL explains that due to the broader concerns of the FCM design, NEPOOL and ISO-NE committed to evaluate such issues in a detailed and comprehensive manner through a stakeholder process commencing in the first quarter of 2009 and culminating with a Commission filing no later than February 20, 2010. According to NEPOOL, prejudging the scope or timing of discussion of the FCM beyond the commitments outlined in the December 1 Filing is unnecessary and undesirable. NEPOOL argues that an order on scope and timing now, before a more complete discussion among all the stakeholders, would be premature and potentially counterproductive by forcing decisions ahead of when the necessary discussions have been completed. NEPOOL asserts that the commitment to a filing by February 20, 2010, by no means precludes an earlier filing, or multiple filings. NEPOOL argues that decisions regarding the complete scope of the issues to be explored, the prioritization of issues, the sequencing of discussions, and possible findings and implementation of any changes are all matters best left to the region to determine with full consideration of all the other issues and priorities.

50. In its answer, ISO-NE argues that the Commission should not expand the scope or alter the timing of the stakeholder process proposed in the December 1 filing because the region's agenda and priorities should not be set by a single set of market participants. ISO-NE states that it does not object to NEPGA's inclusion of alignment between Local Sourcing Requirements and Transmission Security Analysis and all reliability constraints in calculating the Installed Capacity Requirement because ISO-NE has already committed to this in the stakeholder process. However, ISO-NE states that three of the issues that NEPGA seeks to include in the stakeholder process (developing consistent obligations for all Capacity Resources so that all resources sold at the same price have the same set of obligations; ensuring that out of market capacity participating in the auctions does not have a detrimental effect on price formation; and ensuring that the CONE parameter adequately reflects the actual cost of new entry) are not directly implicated by the December 1 filing, and, while important, are only some of the many important issues that ISO-NE and its stakeholders will need to address in completing the design of the FCM. ISO-NE explains that there is an annual process in place in which ISO-NE, NEPOOL, and the New England Conference of Public Utility Commissions consider the prioritization of the various issues facing the region. ISO-NE states that the start of the next round of this process is imminent and NEPGA should be directed to that process with its remaining issues so that they can be vetted and weighed in light of the full range of important issues facing the region.

51. Further, ISO-NE asserts that the timeline proposed in the instant filing is aggressive given the complexity of the issues involved, even without expanding the scope as NEPGA requests. ISO-NE explains that a filing in November 2009 might be possible if the relevant technical committees and ISO-NE resources were completely available to work on nothing but this project, but that is not the case. ISO-NE argues that it is not reasonable to expect that ISO-NE and its stakeholders will be able to complete the required work with substantial agreement among the parties prior to December 2009.

According to ISO-NE, NEPGA's alternative to delay the submission of de-list bids for the fourth Forward Capacity Auction would be extremely difficult to accomplish and has not been fully vetted within ISO-NE or with stakeholders. ISO-NE states that attempting to compress the qualification schedule would risk leaving insufficient time to complete the necessary work. Thus, ISO-NE argues that it is premature to order a particular timing solution now.

3. Commission Conclusion

52. As detailed previously, the Commission supports ISO-NE's commitment to the stakeholder process beginning in the first quarter of 2009 to discuss the identified issues related to Local Sourcing Requirements and Capacity Zones. The Commission has previously expressed its desire for the New England stakeholders to address this issue, including recently in an order addressing compensation for resources needed for reliability that seek to de-list from the FCM.²⁹ We appreciate NEPGA's concern regarding the timing of any proposed changes resulting from the stakeholder process. We agree with NEPGA and ISO-NE that any proposed revisions should be filed for Commission consideration such that if approved, they may go into effect prior to the fourth Forward Capacity Auction. However, considering the magnitude of this issue, we also note ISO-NE's arguments that it might not be reasonable to expect a submission before February 20, 2010, after several deadlines for the fourth Forward Capacity Auction have passed. Therefore, while we would encourage submission of any proposed revisions prior to February 20, 2010, we will not make this a requirement, and will continue to hold ISO-NE only to its commitment to file revisions by February 20, 2010. Importantly, while acknowledging that relevant Forward Capacity Auction deadlines may pass prior to this submittal, the Filing Parties have committed that a February 20 filing will allow sufficient time so that the Commission can act on any new rules and those rules can be in place before the Installed Capacity Requirements and Informational Filings must be made for the 2013-2014 Power Year and the fourth Forward Capacity Auction. In addition, we find that any proposal to delay the submission of new resource qualifications and certain de-list bids for the fourth Forward Capacity Auction should be vetted through the stakeholder process.

53. Regarding the scope of the stakeholder process, we agree with ISO-NE and NEPOOL that the primary focus of the pending stakeholder process should be to address issues related to Local Sourcing Requirements and the establishment of Capacity Zones. Regarding the other issues that NEPGA highlights for stakeholder consideration, we find that NEPGA has not demonstrated that these additional priorities are of such importance that the Commission must formally expand the planned stakeholder process as requested. As such, we will not make consideration of these additional issues a requirement at this

²⁹ *ISO New England Inc.*, 125 FERC ¶ 61,102, at P 114 (2008).

time. However, we agree with NEPOOL that decisions regarding the complete scope of the issues to be explored are better determined in the regional stakeholder process.

54. Finally, contrary to Dynegy's request, we will not condition the acceptance of the instant filing as requested by NEPGA and PSEG. The Commission finds the proposed revisions just and reasonable without conditions.

The Commission orders:

(A) The Filing Parties' proposed tariff sheets are hereby accepted and made effective February 16, 2009, as requested.

(B) ISO-NE is required to make a compliance filing within 30 days of the date of this order with regard to the participation of local transmission control centers in the determination as to whether to accept or reject monthly Capacity Supply Obligation Bilateral contracts, as discussed above.

(C) ISO-NE is required to make a compliance filing within 30 days of the date of this order to clarify that the language of section III.13.5.1.1.3 does not require parties to disclose their negotiated price associated with the Capacity Supply Obligation Bilateral to ISO-NE, but simply provides parties the optional ability to use the settlement software, and to file revisions to the language of that section as appropriate, as discussed above.

By the Commission. Commissioner Kelliher is not participating.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.