

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

New York Independent System Operator, Inc.

Docket No. ER06-1014-000

ORDER CONDITIONALLY ACCEPTING TARIFF REVISIONS AS MODIFIED
AND DIRECTING COMPLIANCE FILING

(Issued July 14, 2006)

1. On May 16, 2006, the New York Independent System Operator, Inc. (NYISO) submitted proposed revisions to its Market Administration and Control Area Services Tariff (Services Tariff) and Open Access Transmission Tariff (OATT) (collectively, Tariffs) to eliminate the Temporary Extraordinary Procedures (TEP) and to establish a framework and time limits for non-TEP price corrections. More specifically, the proposed revisions to the Tariffs specify: (1) the criteria for determining that an Energy or Ancillary Services price has been calculated in error and requires correction; (2) the manner in which NYISO will calculate corrected prices; and (3) procedural requirements and time limits that NYISO must follow when correcting prices. We will conditionally accept NYISO's proposed revisions for filing, as modified, to be effective July 15, 2006, as requested. In addition, we will require NYISO to commence filing in this proceeding, as of January 31, 2007, and every six months thereafter, periodic informational reports detailing its price corrections for the period July 1, 2006, through December 31, 2006, and for every six-month period thereafter, and discussing its progress in reducing or eliminating pricing errors.

I. Background

2. Nearly seven years ago, NYISO filed for authorization to implement the TEP to permit price modifications after the normal posting time periods contained in its Tariffs. The Commission authorized the TEP because NYISO would be simultaneously implementing bid-based markets for energy and generation-based ancillary services with

a two-settlement system (day-ahead and real-time energy markets) and simultaneous co-optimization of energy and ancillary services.¹

3. On May 9, 2005, the Commission directed NYISO to file tariff revisions to eliminate the TEP and establish a framework and time limits for non-TEP price corrections.² Specifically, NYISO was directed to file a report with the Commission, no later than October 31, 2005, that included a plan and schedule for eventually phasing out the TEP altogether and also for shortening the time periods both for posting notices of price corrections and for correcting prices.

II. NYISO's Proposal

4. NYISO states that the tariff revisions it proposes herein fulfill the Commission's directive to eliminate the TEP and also that its revisions aid market participants by establishing in its Tariffs transparent rules and time limits for non-TEP price corrections. NYISO indicates that it developed the proposed revisions with extensive input from its stakeholders.

5. In its transmittal letter, NYISO indicates that it understands the importance of correctly-calculated prices to the operation of the markets that it administers and that it knows that frequent price errors and corrections undermine confidence in those markets, possibly causing decreased market participation. NYISO contends that it has undertaken "substantial initiatives" to reduce the occurrence of price errors in the first place. NYISO states that, following the implementation of the Standard Market Design Version 2 software in February 2005, it adopted a corporate goal of achieving initial price accuracy greater than 97 percent (less than three percent of hours with a price correction). NYISO reports that, in January 2005, 3.76 percent of hours were corrected, but a year later, in January 2006, that was down to 2.69 percent.³

¹ *New York Independent System Operator, Inc.*, 88 FERC ¶ 61,228, *reh'g denied*, 89 FERC ¶ 61,168 (1999).

² *New York Independent System Operator, Inc.*, 111 FERC ¶ 61,200 (2005) (May 9 Order).

³ Attachment 1 to NYISO's filing is NYISO's "Action Plan for the Reduction and Elimination of Price Errors."

A. Elimination of the TEP

6. NYISO states that, as directed by the Commission in the May 9 Order, it proposes to eliminate the TEP in their entirety from Attachment E of the Services Tariff and from Attachment Q of the OATT. Going forward, NYISO continues, the only price corrections it will be authorized to make are those required under the filed rate doctrine in accordance with the requirements and time limits proposed in its filing. NYISO states that it will be otherwise proscribed from making any price changes beyond the proposed time limits absent a specific directive to do so from either the Commission or a court of competent jurisdiction.

B. Market Clearing Price Errors Requiring Correction

7. In its transmittal letter, NYISO explains that an erroneous Energy or Ancillary Services price can result from either (1) a simple miscalculation in determining the price or (2) the selection of the wrong price-setting resource in determining the price. NYISO indicates that the former type of error occurs less commonly and can happen when the software is programmed incorrectly or when the software fails to produce a meaningful price calculation at all. The latter type, NYISO continues, is the more common error and occurs when, for some reason, NYISO's software fails to calculate the Energy and Ancillary Services prices on a least cost total bid production cost basis, as the Tariffs require. NYISO explains that an example of the second type of error is when an error in real-time metering information causes a generator to appear to have tripped when it actually has not. This would cause the system to be redispatched, and prices to be recalculated, to replace the energy that appears to have been lost. Due to the error, the next most economic unit available will be offered at a higher price than the unit that appears to have tripped; this, in turn, causes an erroneous increase in Energy and Ancillary Services prices during the time interval when the software is looking to the next most economic unit available for replacement energy that is, in fact, not needed to meet demand.

8. NYISO states that the newly proposed provisions in section A of Attachments E and Q establish the criteria for determining that an Energy or Ancillary Services clearing price is inconsistent with the Tariffs and therefore is erroneous. The criteria are that an Energy and Ancillary Services clearing price must be (i) calculated correctly under the relevant provision of the Tariffs and (ii) based on the appropriate price-setting resource.

1. Calculation Errors

9. Section A.1 defines calculation errors. It establishes that an error calculation occurs when, notwithstanding that the correct price-setting resource has been selected, an

Energy or Ancillary Services price is computed inconsistently with the Tariffs, or when no price is calculated or a price is not timely posted on the OASIS.

2. Errors in Selecting Price-Setting Resource

10. Section A.2 defines errors in selecting the price-setting resource. It states that NYISO shall schedule, commit, and dispatch supply resources on a least cost total bid production cost basis and that an Energy or Ancillary Services price must be based on the appropriate price-setting resource. Section A.2 authorizes NYISO to correct a price that it determines to have resulted from an error in selecting the appropriate price-setting resource.

C. Methodology for Correcting Prices

11. NYISO's proposed section B establishes the methods NYISO may use to calculate the correction of an erroneous price. The first paragraph of section B states that NYISO shall recalculate an erroneous price in accordance with the relevant provisions of the Tariffs. If that is not practicable due to "unavailability of necessary data or otherwise, then NYISO is to determine a price "as close as reasonably possible to the price that should have resulted" from the Tariffs "consistent with system operations." For such recalculations, NYISO is to draw, as appropriate, from: (1) prices calculated for electrically similar points; (2) prices in surrounding intervals; (3) Real-Time Commitment prices; (4) Day-Ahead Market prices; or (5) Real-Time Dispatch prices for the affected intervals.

12. Section B also addresses the methodology for correcting prices in the event of a "catastrophic failure" of NYISO's price calculation software. In this event, NYISO shall provide notice of the problem to the Commission and customers as soon as possible and no later than the next business day. Within two additional business days, NYISO must inform the Commission and customers of the nature of the problem and the schedule for determining the procedures NYISO will use to construct prices "as close as possible to the prices" that should have resulted from the application of the Tariffs to prevailing system conditions.

D. Deadlines for Price Reservations and Corrections

13. NYISO's proposed section C establishes deadlines for the reservation and correction of any erroneous prices; it explicitly states that NYISO cannot reserve or correct any erroneous price outside these timeframes, except as directed by Commission or a court of competent jurisdiction. Specifically, section C provides: (1) NYISO shall provide notice reserving a potentially erroneous Real-Time Commitment or Real-Time

Dispatch price not later than 17:00 of the calendar day following the operating day for which the price was calculated; and (2) NYISO shall provide notice reserving a potentially erroneous Day-Ahead Market clearing price prior to the start of the operating day for which the price was calculated. Schedule C also states that NYISO shall correct a price it has timely reserved and determines to be erroneous and shall provide notice of the correction as soon as possible, but not later than five business days after the price reservation deadline. Whenever possible, NYISO will make corrections prior to the reservation deadlines and will provide notice of those corrections along with the reservation notices.

E. Reporting Requirements

14. NYISO's proposed section D establishes that, in the event that NYISO corrects a price, it must provide customers with a brief description of the error, the correction method used, and supporting tariff references as soon as possible but within ten days following the prices correction unless "extraordinary circumstances" necessitate additional time. In that event, NYISO must provide the information no later than 30 days after the prices correction.

15. Additionally, NYISO must provide quarterly reports to customers about the cause of each error NYISO corrects and the steps planned or taken to eliminate or diminish the incidence of the error in future. Finally, NYISO must include in the quarterly report details of any price error discovered after the deadlines for reservation and correction of the error.

F. Liability

16. NYISO's proposed section E establishes that NYISO will not be liable for errors left uncorrected except in cases of gross negligence or intentional misconduct.

III. Interventions and Protests

17. Notice of NYISO's filing was published in the *Federal Register*, 71 Fed. Reg. 32,066 (2006), with motions to intervene and protests due on or before June 9, 2006. The New York State Public Service Commission (New York Commission) filed a notice of intervention. The New York Transmission Owners (New York TOs) filed a timely motion to intervene and comments. Mirant Energy Trading, LLC; Mirant New York, Inc.; Mirant Bowline, LLC; Mirant Lovett, LLC; and Mirant NY-Gen, LLC (collectively, Mirant) filed a timely motion to intervene. AES Eastern Energy, L.P. (AES); the Independent Power Producers of New York, Inc. (IPPNY); and KeySpan-Ravenswood, LLC (KeySpan) filed timely motions to intervene and protests. DC Energy, LLC (DC

Energy) and EPIC Merchant Energy, LP; SESCO Enterprises LLC; and Black Oak Energy, LLC (collectively, Financial Marketers) filed timely motions to intervene and protests. On June 21, 2006, New York TOs filed a motion for leave to answer and an answer.

18. No party disagrees with NYISO's proposal to eliminate the TEP; however, several parties take issue with certain aspects of the proposed price correction procedures. We detail these concerns below.

A. Comments Opposing the Proposed Deadlines

19. IPPNY asks the Commission to require NYISO to make all price corrections within three calendar days of the day on which prices are reserved. IPPNY contends that, while NYISO stated that it has a formal corporate goal of making price corrections in three calendar days or less and has met its goal with an annual average time of 1.98 days through April 2006, the proposal provides NYISO five *business* days to make such corrections, as opposed to the TEP which provided NYISO only five *calendar* days. Financial Marketers complain a five business day wait is unreasonable, creating market uncertainty for a full trading week. Both IPPNY and KeySpan argue that NYISO should be required to make all price changes within three calendar days, while DC Energy suggests two calendar days. Alternatively, IPPNY requests that NYISO be directed to establish, within 60 days of the order, a timeframe by which it will shorten the deadlines.

20. AES notes that NYISO has committed to "assess whether shorter reservation and correction deadlines might be appropriate and report to stakeholders not later than June 30, 2006," adding that there is no clear rationale for maintaining a five business day time frame. AES urges the Commission to require NYISO to file within four months a report setting forth a defined time table to reduce the five business day interval to a shorter time period.

21. DC Energy protests as excessively long NYISO's proposal to have up to 40 hours (until 17:00 of the following operating day) to reserve Real-Time Commitment or Real-Time Dispatch prices for correction. It complains that this long time lag is not adequate even for the short term, as it would impede arbitrage and liquidity. DC Energy requests that the Commission direct NYISO to reserve real-time prices by no later than noon on the following operating day.

22. Financial Marketers also protest this particular provision, complaining that participants will have already made binding bids or offers for day two before they know that the prior day's prices have even been reserved. They request that NYISO be required to reserve prices prior to the bid submission deadline of the next day. Financial

Marketers also argue that it is unreasonable for NYISO, in Section D (Reporting Requirements) to propose to take up to ten days to provide an explanation to customers when a price correction is made.

B. Comments Opposing the Proposed Price Correction Methodology

23. IPPNY urges the Commission to prohibit NYISO from correcting prices in the situation where the revised price would be inconsistent with NYISO's own generation dispatch instructions. IPPNY explains that, as NYISO has acknowledged, here, the software has operated correctly, but is relying on incorrect data (that a generator has tripped when it has not) and has produced incorrect prices that are – nonetheless – the basis for generator dispatch instructions. IPPNY argues that NYISO proposes to correct prices for the interval in which the telemetry error occurred as if the more expensive generation that was dispatched to compensate for the telemetry error had never been dispatched, even though that more expensive generation incurred what IPPNY insists are additional operating costs in response to NYISO's dispatch instructions. IPPNY is concerned that the erroneously dispatched generation will not recover its full bid production costs without having to sacrifice profits earned in other hours. IPPNY argues that, if NYISO is allowed to correct prices when the revised price would be inconsistent with the dispatch instructions and schedules, the Commission should also require the NYISO to compensate suppliers that follow the dispatch instructions.

24. Similarly, KeySpan states that NYISO and the Commission should recognize that price corrections ought to operate in both directions, that is, not only when NYISO sets the market clearing price too high, but also when its sets the market clearing price too low. It maintains that suppliers who are erroneously dispatched because of an error in NYISO's software should receive the higher of the market clearing price or their bids. It contends that this will ensure that no supplier should suffer financial harm for following NYISO's dispatch directions. Finally, AES makes essentially the same argument as IPPNY and KeySpan and requests that the Commission direct NYISO to submit tariff revisions addressing this issue within six months. AES agrees with IPPNY that a separate bid production cost guarantee mechanism should be implemented for the individual hours in which price corrections occur to prevent generators from being financially harmed from following NYISO's dispatch instructions.

25. In addition, IPPNY requests that NYISO be prohibited from correcting prices when it has erroneously dispatched generation longer than three Real-Time Dispatch intervals (approximately 15 minutes). IPPNY states that this will provide an incentive to find ways to prevent errors from occurring in the first place and will also protect against the most extreme cases of subjective re-estimation of what prices should have been.

26. The New York TOs object to IPPNY's proposals to prohibit NYISO from correcting for erroneously dispatched generators; to require separate bid production cost guarantee compensation for those generators; and to prohibit price corrections when generation has been erroneously dispatched for longer than three RTD intervals. The New York TOs state that NYISO's Billing & Pricing Correction Task Force decided to defer action on these proposals and claim that IPPNY is now trying to circumvent the NYISO stakeholder process. The New York TOs urge the Commission to consider IPPNY's proposals in the context of the ongoing efforts of the NYISO stakeholder process, which continues working with its market participants to improve NYISO's initial price accuracy.

27. IPPNY states that the Commission should require NYISO to clarify its price correction procedures with respect to catastrophic failures of its price calculation software (section B). IPPNY requests that the Commission direct NYISO to add language to this provision that clarifies that NYISO will work collaboratively with market participants in developing the procedures that will be used to construct prices under these circumstances, consistent with NYISO's conduct in response to the August 2003 blackout.

28. Financial Marketers state that the proposed methodology for correcting prices in general is arbitrary, standardless, and gives NYISO too much discretion when correcting prices. They point in particular to the list of five elements (in section B) that NYISO may draw upon when correcting prices. Financial Marketers allege that NYISO can choose, after the fact, any element it sees fit to rely on for price corrections. As a result, they argue, market participants have no way of knowing how a price will be determined and no way to challenge a determined price.

C. Comments on Other Proposals

29. The New York TOs comment that, while NYISO's filing makes some improvement with respect to the clarity of its pricing procedures, it should not be viewed as representing an acceptable level of pricing accuracy. The New York TOs note that 97 percent pricing accuracy still represents nearly one full day of price corrections per month. The New York TOs maintain that NYISO's filing does not provide a plan and schedule for shortening the time periods both for posting notices of price corrections and for correction prices, as requested in the May 9 Order.

30. The New York TOs comment that NYISO must continue to work closely with market participants and others to ensure progress, that NYISO should establish a variety of performance measures such as the number of hours with errors per month, and that NYISO should report on the causes of errors that occur and NYISO actions to prevent

their recurrence. The New York TOs request that the Commission direct NYISO to file periodic reports on its progress in improving its pricing and billing procedures. DC Energy agrees that the Commission should require NYISO to report, within six months, on the frequency of price corrections and the time frame for eliminating the post hoc price modification authority altogether.

31. Financial Marketers object to section E, governing liability. They complain that NYISO should face liability for leaving price errors uncorrected and also subject NYISO to potential liability for prices that are improperly corrected. In other words, Financial Marketers contend, both the failure to act and improper actions should qualify for potential liability. In addition, Financial Marketers complain that the standard for liability is too deferential and that the proper standard should be something less than gross negligence or intentional misconduct.

32. IPPNY states that the Commission should require NYISO to make its proposed price correction provisions more transparent to market participants by providing sufficient information to market participants to explain the cause of the error, why NYISO believes it was an error, what actions NYISO took to correct the error, and why the change results in a more appropriate price.

IV. Discussion

A. Procedural Matters

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

34. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2005), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the New York TOs' answer because it has provided information that assisted us in our decision-making process.

B. Commission Determination

35. The Commission will conditionally accept NYISO's proposal to eliminate the TEP and its proposed revisions, modified as discussed below, to be effective on July 15, 2005. The Commission agrees with those commenters who assert that NYISO's proposal should be viewed as an improvement over the TEP, but as not having yet reached an acceptable level of pricing accuracy; the Commission further agrees with commenters that more clearly defined procedures and shorter timelines are appropriate. We therefore

will direct NYISO to make the following modifications to its Tariffs and to make a compliance filing no later than 120 days after the issuance of this order.

1. Deadlines for Reserving and Correcting Prices

36. Several parties complain that NYISO proposes to have five business days to make price corrections, which is more generous than the five calendar days timeline in the TEP. Parties note that NYISO itself states that it has a corporate goal to make price corrections within three days, and that it has been able to attain that goal within an average time of 1.98 days. We agree that NYISO's proposed five business days timeline is excessively long. Further, while some parties suggest that the Commission require NYISO to file a schedule of when it will shorten the deadlines, given NYISO's demonstrated success in making timely price corrections, we see no need to wait to shorten this particular deadline. Therefore, we will direct NYISO to revise its Tariffs to provide for its making price corrections within three calendar days.

37. Parties also complain that NYISO's proposal to have up to 40 hours (until 17:00 of the following operating day) to reserve Real-Time Commitment or Real-Time Dispatch prices for correction is excessively long. One party suggests that NYISO be required to reserve real-time prices by no later than noon on the following operating day while another suggests the bid submission deadline of the following day. We agree with these parties that the proposed deadline for reserving real-time prices is excessively long and so might adversely impact markets. We therefore direct NYISO to work with its stakeholders to reach agreement on a shorter deadline and to file an appropriate modification to its Tariffs.

38. Finally, Financial Marketers suggest that NYISO be required to provide explanations of price corrections to its customers in fewer than the proposed ten days (section D). We will deny this request. We believe that this is a reasonable period of time to produce an explanation of both the error and how it was corrected, and we are not persuaded that any party would be harmed by a ten-day wait.

2. Price Correction Methodology

39. Several parties urge the Commission to prohibit the NYISO from correcting prices in circumstances where the revised price would be inconsistent with NYISO's dispatch instructions and schedules. In the alternative, parties suggest that, if NYISO is allowed to correct prices in this situation, the Commission require NYISO to compensate suppliers that have followed dispatch instructions, such as providing erroneously-dispatched suppliers with the greater of their bids or the market clearing price. These parties argue that to do otherwise would penalize generators for responding in good faith to dispatch

instructions. In addition, IPPNY urges the Commission to not allow price corrections for erroneously dispatched generation longer than three Real-Time Dispatch intervals.

40. AES and New York TOs indicate that NYISO and its participants are still in the process of discussing these issues, and AES requests that the Commission direct NYISO to submit tariff revisions addressing these issues within six months. In light of the fact that a stakeholder process concerning these issues is still ongoing, we will not direct NYISO to make any specific revisions at this time, but rather we will allow the stakeholder process to continue. When the stakeholder process is concluded, NYISO is directed to submit a report as to the outcome of that process. The report should summarize the stakeholders' views as to whether any revisions are needed and why.

41. We will grant IPPNY's request that NYISO be directed to revise Section B to clarify that, in the case of a catastrophic failure of NYISO's price calculation software, NYISO will work collaboratively with market participants in developing procedures that will be used to construct prices under those circumstances, as requested by IPPNY. We agree that this is a reasonable proposal that is consistent with NYISO's actions in response to the August 2003 blackout.

42. We are unconvinced by Financial Marketers' complaint that the language NYISO proposes in section B provides it with excessive discretion and allows NYISO to correct prices as it sees fit, thereby preventing customers from being able to challenge a corrected price. The list of factors from which NYISO may draw is sufficiently specific, and the provision as a whole properly balances the need for flexibility with the requirement that the language of a rate schedule be clear and specific.

3. Other Provisions

43. Several parties allege that NYISO's filing does not include a plan and schedule for shortening the time periods for both reservations and price corrections, as directed in the May 9 Order, and ask the Commission to direct NYISO to file periodic reports on its progress on improving its pricing accuracy and correction frequency. We agree that NYISO needs to continue to work with its participants to ensure further progress in reducing the types of, and frequency of, price errors.⁴ To this end, we will direct NYISO

⁴ DC Energy requests that the Commission reject the proposal to make NYISO's price correction authority "permanent." While we agree that NYISO should make all efforts to reduce error frequency, and the subsequent need for price corrections, we are not persuaded to impose a "sunset" provision on the proposed procedures at this time.

to file in this proceeding, by January 31, 2007 and every six months thereafter until otherwise directed, informational reports listing the price corrections made in the preceding six months. For each individual price correction, NYISO is to provide, at a minimum, the following information: (1) the cause of the pricing error that was corrected; (2) the duration of the price correction; (3) the rate impact of the price correction; and (4) what actions NYISO took to correct the price error, including the factors described in Section B that NYISO relied upon in recalculating prices. NYISO is also to summarize and discuss what actions it undertook during the preceding six months to reduce or eliminate the types of price errors that occurred. These reports are for informational purposes only and will not be viewed as requiring any Commission action.

44. The Commission will accept NYISO's proposed liability language. We are not persuaded by Financial Marketers' argument that NYISO, a non-profit company, should be exposed to further liability with respect to price corrections or that the proposed standard (gross negligence or intentional misconduct) is overly deferential.

45. IPPNY complains that there is a need to make the price correction process more transparent to customers. We agree and find that the reporting requirements outlined in Section D do not provide customers with adequate information. Thus, we direct NYISO to work with market participants to consider what additional information should be provided to customers so that they may have adequate information regarding price errors and corrections and to revise the Tariffs accordingly in the compliance filing that we direct herein.

The Commission orders:

(A) NYISO's tariff revisions are hereby conditionally accepted for filing, subject to NYISO filing additional revisions, within 120 days of the date of this order, as discussed in the body of this order.

(B) NYISO is hereby directed to file in this proceeding, by January 31, 2007, and every six months thereafter until otherwise directed, an informational report detailing price corrections and its progress in reducing or eliminating pricing errors in the prior six months, as discussed in the body of this order.

(C) NYISO is hereby directed to file a report as to the outcome of the stakeholder process concerning compensating generators that have followed dispatch instructions associated with telemetry errors, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.