120 FERC ¶ 61,099
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.

New York Independent System Operator, Inc. Docket No. ER07-521-000

ORDER ESTABLISHING A TECHNICAL CONFERENCE

(Issued July 27, 2007)

1. On February 5, 2007, the New York Independent System Operator, Inc. (NYISO) filed revisions to its Open Access Transmission Tariff (OATT) and Market Administration and Services Tariff (Tariff) in compliance with the Commission's Final Rule on Long-Term Firm Transmission Rights in Organized Electricity Markets.[1] In order to assist the Commission's evaluation of the NYISO Long-Term Transmission Rights (LTTR) proposal, the Commission directs NYISO to file additional information and the Commission staff to hold a staff-led technical conference to allow NYISO to discuss with staff and interested parties the NYISO proposal and responses to the Commission's questions presented below. The technical conference is intended to supplement the existing record and thereby facilitate the Commission's decision-making process. To facilitate preparation for the technical conference, the Commission directs NYISO to submit a written response to the questions addressed herein within 21 days of the issuance of this order.[2] The Commission, by separate Notice(s), will establish dates and technical conference details.

[1] *Long-Term Firm Transmission Rights in Organized Electricity Markets,* Order No. 681, FERC Stats. & Regs. ¶ 31,226 (August 1, 2006), *order on reh'g and clarification,* Order No. 681-A, 117 FERC ¶ 61,201 (November 16, 2006) (together, LTTR Rule).

[2] Any other party to this proceeding that wishes to submit comments on these issues and questions may do so also within 21 days.

2. On July 20, 2006, as amended August 1, 2006, the Commission issued Order No. 681, in which it adopted seven guidelines that provide a framework for the provision of LTTRs. Order No. 681 provided latitude to transmission organizations and stakeholders to find ways to comply with the guidelines. We noted that "while proposals to comply with this Final Rule must satisfy each of the guidelines, we believe each of the guidelines may be satisfied in any number of ways, and we do not intend that the guidelines predetermine any particular design."[3] At the same time, Order No. 681 anticipated that guideline (7) (no required auction participation) presented particular challenges for some regions.[4] The Commission is unable to determine on the basis of the existing record whether the NYISO proposal complies with guidelines (5) (reasonable needs standard) and (7) of the LTTR Final Rule. Given the import of the issues, the Commission believes it necessary to provide context for its questions with the expectation that NYISO will provide full responses addressing the issues raised, both in its written responses to our questions and at the conference as directed herein. We encourage parties to this proceeding to participate in the conference.

Discussion

Guideline (5)

> Load-serving entities must have priority over non-load serving entities in the allocation of long-term firm transmission rights that are supported by existing transmission capacity. The transmission organization may propose reasonable limits on the amount of existing transmission capacity used to support long-term firm transmission rights.

3. Recognizing that transmission capacity is limited, the LTTR Rule provided for transmission organizations to propose reasonable limits on the amount of transmission capacity made available for LTTRs, such as minimum daily peak load or 50 percent of maximum daily peak load. The LTTR Rule also protects transmission rights used to satisfy native load service obligations. Order No. 681 provided preference for LSEs to obtain LTTRs, and such preference serves as a tiebreaker between LSEs and non-LSEs when the transmission system is limited. Order No. 681 also states that the transmission organization and its stakeholders should be given flexibility to determine the level at which an LSE may nominate long-term firm transmission rights as long as that level does not fall below the reasonable needs of the LSEs.

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[3] Order No. 681, FERC Stats. & Regs. ¶ 31,226 at P 103.

[4] In particular, *see id.* at P 118-119 and P 388-392.

4. The Commission does not have adequate information in the record to determine whether the allocation of LTTRs to LSEs meets the reasonable needs of each LSE as required under guideline (5), and whether the quantity is allocated in a non-discriminatory manner. This is, in part, because NYISO has not explained its proposed definition of an LSE's "reasonable needs" and how that relates to total transmission capacity. While it may be that NYISO is making available a sufficient amount of its total transmission system capacity for LTTRs, whether that capacity reasonably provides for the needs of individual LSEs, as contemplated in the LTTR Rule, is not discernable. The Commission, while permitting flexibility, specifically tied the measurement of reasonable needs directly to the load serving obligations of each LSE. It is also unclear whether each LSE is receiving LTTRs in a manner that is not unduly discriminatory, for example, in the same proportion as its load obligation.[5]

5. Accordingly, NYISO should respond within 21 days to the following and be prepared to clearly demonstrate at the technical conference how its proposal meets the reasonable needs requirement of the LTTR Rule.[6] In this regard, the Commission directs NYISO to provide:

1) The definition of "reasonable needs" that NYISO proposes to use and whether it would be useful and practical for NYISO to base its LTTR allocations on a reference year or baseline quantity;

2) Detailed illustrations that show, under the existing proposal, how NYISO meets the reasonable needs requirement of guideline (5);

3) An explanation of how NYISO's proposed multiple methods of allocating LTTRs to LSEs treat all LSEs comparably, *e.g.*, how LTTRs allocated through conversions of expired grandfathered contracts are not preferential as compared to those afforded LSEs based on their zonal load ratio share. NYISO should explain how all LSEs will have the opportunity to meet their reasonable needs over transmission paths that they have historically used.

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[5] By way of example and to further illustrate the type of showing that should be made, PJM in defining reasonable needs used an approach that is based on an LSE's zonal base load, its historical resources, and its historical reference year, and each LSE is allocated a quantity of LTTRs equal to its zonal base load. *See PJM Interconnection L.L.C.*, 117 FERC ¶ 61,220 at P 6 (2006).

[6] In order to bring these matters to a close as soon as practicable, parties to this proceeding should be prepared to address the NYISO's responses at the technical conference and be prepared to explore avenues by which the proposal could be modified to satisfy the reasonable needs of LSEs.

4) Verification that feasibility limitations will not prevent an LSE from meeting its reasonable needs with LTTRs.[7]

5) An explanation and illustration of how particular Point of Injection and Point of Withdrawal paths will be determined under NYISO's proposal for LTTR auction allocation rights (AARs) that are allocated on a zonal load ratio share basis.

Guideline (7)

The initial allocation of the long-term firm transmission rights shall not require recipients to participate in an auction.

6. In general, a transmission organization can satisfy guideline (7) by adopting a process by which LTTRs are directly allocated to LSEs without the use of an auction. However, in Order No. 681, the Commission noted that guideline (7) does not preclude a transmission organization from using an auction to allocate long-term firm transmission rights. It only precludes requiring an LSE to submit a winning bid in an auction in order to acquire long-term firm transmission rights.[8] Although it restricted the use of auctions, the LTTR Final Rule recognized that an auction mechanism can be an important component of the LTTR allocation process, and described the allocation procedure used by PJM for short-term rights as an acceptable use of an auction. Under the PJM approach, each LSE is first allocated point-to-point auction revenue rights on the basis of LSE nominations. The LSE then may participate in the annual auction as a "price taker" and may, at its option, convert its auction revenue rights directly into point-to-point firm transmission rights (FTRs) that correspond to the sources and sinks of the auction revenue rights. Both PJM and the Midwest ISO have since adapted this process to the allocation of LTTRs.[9]

7. Because NYISO uses an auction first to price allocated rights, and then transfers the auction revenues to market participants, it exposes LSEs to some degree of price uncertainty, and may not be in compliance with guideline (7). For example, if an LSE were required to participate in an auction as a price taker (which is equivalent to placing a bid with no upper bound), but had no assurance of receiving revenues that reasonably approximate its costs, the LSE may be assured of winning its bid, but the cost that it would incur to obtain its LTTRs

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[7] *See PJM*, 117 FERC ¶ 61,220 at P 87.

[8] Order No. 681, FERC Stats. & Regs. ¶ 31,226 at P 385.

[9] *See generally, PJM*, 117 FERC ¶ 61,220 (2006) and *Midwest Independent Transmission System Operator, Inc.* , 119 FERC ¶ 61,143 (2007).

would be unknown until after-the-fact — and that cost could be large. Conversely, if the LSE had to place an explicit price bid in the auction, the bid would limit its cost exposure, but the LSE would face the possibility that its bid may not be accepted; and as a result, it would not receive LTTRs. The NYISO's compliance filing fails to demonstrate how either of these outcomes is consistent with guideline (7), unless some additional rule is included to offset the uncertainty accompanying the LTTRs' auction price.

8. For these reasons, the Commission is concerned that the NYISO proposal in its present form may not be in compliance with guideline (7) and that other approaches merit consideration. Indeed, in the NYISO proposal and the comments of stakeholders, two basic methods have been identified for compliance with guideline (7): (1) the NYISO proposal to directly allocate LTTRs but then use auction prices, either the current annual auction or past auction prices or congestion prices and a premium to value the rights going forward; and (2) the proposal by New York Association of Public Power (NYAPP) for a direct allocation approach for LTTRs. Either of these approaches, if modified, could be compliant with the LTTR Final Rule; however, the Commission does not have sufficient information to make a final determination. Hence, the Commission directs staff to explore these proposals at the technical conference.

9. With regard to the direct allocation proposal, the technical conference will examine the technical/computational issues associated with a direct allocation approach. The Commission is interested in further explanation of the technical barriers preventing a direct allocation process for LTTRs, and the advantages and disadvantages of such a process:

1) Provide more detail on why the two-tier transmission service charge (TSC) structure is computationally intractable. Are there possible simplifying assumptions that would make the problem computationally tractable? What changes would be required in the billing and accounting procedures so that they can credit or allocate the purchase price of an LTTR directly to the LSE paying the purchase price?

2) Are there any examples now of LSEs that have directly allocated grandfathered TCCs and also obtained auction revenues? If yes, how is the TSC crediting done for such LSEs' auction revenues, and why would it be different for the case of directly allocated LTTRs?

3) Are there other ways to directly allocate LTTRs that are easier to implement yet ensure that the value of the LTTR will cover the cost of the long-term transmission rights and achieve price certainty?

10. Parties, such as NYAPP, present alternative allocation methods that bypass the proposed auction price mechanism discussed above. Both the direct allocation TCC proposal and the NYISO proposal for valuing LTTRs raise potential issues that the Commission would like discussed at the technical conference. We remain uncertain about whether, under either

of these proposals, certain LSEs would obtain LTTRs more valuable than the grandfathered rights that were due to expire, or would obtain allocated rights at prices below market levels. The Commission would like the record to be expanded to include a discussion of the scope of this issue and the uncertainty as to what problems would arise if an LSE receiving a direct allocation does not receive a credit of auction revenues against its TSC.

1) In order to assess the impact of NYISO's Fixed Price TCC proposal on LSEs, NYISO should provide an illustration of the potential costs of converting existing grandfathered agreements (GFAs) to LTTRs for a representative sample of LSEs (including those with a source at Niagara and sink in Long Island). Specifically, NYISO should, and other parties may, provide an estimate of the current value of these GFAs, based on: (a) recent TCC auction prices (*e.g.*, last year); and (b) congestion prices during the same time period at the injection and withdrawal points of the GFAs. NYISO should also estimate the change in the cost of transmission service (*e.g.*, moving from pancaked rates to the TSC) for these LSEs, as well as the auction revenues that the LSEs may receive. (To protect the market confidentiality of these calculations, the identity of individual LSEs need not be revealed).

2) Because some of the current GFAs are clearly valuable rights, it is likely that in a full direct allocation approach, similar to that used by PJM, many LSEs would seek to nominate those paths within their eligible source and sink points. Hence, if all LTTR megawatts in NYISO were to be awarded through direct allocation, eligible nominations for LTTRs would likely need to be pro-rationed unless some additional priority was given to certain nominations. Therefore NYISO is to provide the Commission with an illustration of how current GFAs might be equitably treated in the allocation process if all LSEs were eligible for direct allocation.

3) With regard to the NYISO proposal for Fixed Price TCCs, it is not clear why this option is limited to LSEs with expiring GFAs. What are the problems associated with making such an option available to all LSEs?

4) NYISO states that it is currently limited by its manual auction process and that certain enhancements to existing procedures that are retained in this LTTR proposal, as well as further enhancements to the LTTR allocation process, cannot be made prior to the implementation of the End-State Auction, which is several years away. What are the enhancements to the LTTR proposal that NYISO believes it would be able to make upon implementation of the End-State Auction, and what is NYISO's detailed schedule for implementing the End-State Auction?

<u>The Commission orders</u>:

(A) NYISO is directed to file no later than 21 days from the date of this order a written response to the questions that are expressed in the body of this order.

(B) The Commission staff is directed to convene a technical conference to address the issues raised above with regard to the NYISO LTTR filing.

(C) Any other party to this proceeding that wishes to submit comments on these issues and questions may do so within 21 days from the date of this order. Parties to this proceeding may also submit comments on these issues and questions and the issues raised in the technical conference no later than 10 days from the date of the technical conference.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.