

135 FERC ¶ 61,170  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Marc Spitzer, Philip D. Moeller,  
John R. Norris, and Cheryl A. LaFleur.

New York Independent System Operator, Inc.

Docket Nos. ER11-2224-001  
ER11-2224-006

ORDER ON REHEARING

(Issued May 19, 2011)

1. In this order, the Commission grants, in part, and denies, in part, requests for rehearing of its January 28, 2011 order.<sup>1</sup> In the January 28, 2011 Order, the Commission accepted and suspended for the earlier of five months or a date set by subsequent Commission order the New York Independent System Operator Inc.'s (NYISO) proposed revisions to its Market Administration and Control Area Services Tariff (Services Tariff) to update the Installed Capacity (ICAP) demand curves for capability years 2011/2012, 2012/2013, and 2013/2014.<sup>2</sup> The Commission grants rehearing with respect to NYC tax abatement, denies rehearing on other matters, and directs compliance. In addition, the Commission denies rehearing of its March 9, 2011 Order. As a result, and as determined by previous orders issued in this proceeding, the current demand curve rates will remain in effect at the start of the 2011/2012 capability period that begins on May 1, 2011 until a date determined by a further Commission order that rules on compliance filings.

**I. Background**

2. NYISO administers the ICAP monthly spot market, which utilizes NYISO-determined annual demand curves for each of the three NYISO ICAP zones: the

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<sup>1</sup> *New York Indep. Sys. Operator, Inc.*, 134 FERC ¶ 61,058 (2011) (January 28, 2011 Order); Errata Notice issued February 17, 2011.

<sup>2</sup> NYISO's capability year consists of the summer capability period that runs from May 1 through October 31 and the November 1 through April 30 winter capability period.

New York Control Area (NYCA or “rest-of-state”), New York City (NYC), and Long Island (LI).<sup>3</sup> The demand curves apply for each of three 12-month periods beginning May 1 of each year. Section 5.14.1.2 of the Services Tariff requires NYISO to perform a triennial review to determine whether the parameters for the ICAP demand curves should be adjusted and to file revised ICAP demand curve rates with the Commission. Each demand curve is a downward sloping straight line of a range of ICAP prices that vary with the amount of ICAP supply relative to the minimum ICAP requirement,<sup>4</sup> that is, the more ICAP supply exceeds the minimum ICAP requirement, the lower the ICAP price, and vice versa. The price on the ICAP demand curves corresponding to 100 percent of the minimum ICAP requirement is determined based upon the estimated localized levelized cost per kW-month to develop a new peaking unit, i.e., the cost of new entry (CONE), net of energy and ancillary services revenues. The maximum price for each ICAP demand curve is 1.5 times net CONE applicable for each of the three ICAP zones. The minimum ICAP demand curve price is zero when supply reaches the ICAP level equal to certain defined excess ICAP percentages above the minimum requirement. The foregoing three ICAP prices (maximum price, 100 percent of minimum ICAP requirement price, and minimum price) are set forth in section 5.14.1.2 of the Services Tariff.

3. On November 30, 2010, NYISO filed proposed revisions to its Services Tariff that implement revised ICAP demand curves for capability years 2011/2012, 2012/2013, and 2013/2014, with a proposed effective date of January 28, 2011. NYISO’s proposed revisions, *inter alia*, revised certain cost components and parameters of CONE to establish revised ICAP demand curve prices. As relevant to the rehearing requests at issue here, these cost components include deliverability costs, interconnection costs, energy and ancillary services revenues, and New York City property taxes. The parameters at issue include the escalation factor attributed to inflation, the assumption for expected level of average excess capacity, the level of interconnection costs in the NYC

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<sup>3</sup> As defined by section 2.18 of the Services Tariff, “rest-of-state” refers to the region within the NYCA and located outside of the two defined localities of NYC and LI. The term “rest-of-state” is often used interchangeably with NYCA.

<sup>4</sup> For reliability purposes, NYISO is required to have an amount of ICAP equal to 15.5 percent above peak demand (Installed Reserve Margin, IRM). *See N.Y. State Reliability Council, L.L.C.*, Docket No. ER11-2392-000 (January 24, 2011) (delegated letter order). The ICAP requirement is designated in megawatts for the entire NYCA and separate location-specific ICAP requirements for load-serving entities in New York City (NYC), and Long Island (LI) that reflect the existence of transmission constraints in those two areas.

zone, and an adjustment used to take into account the differences between the levels of available capacity in the summer and winter.

4. In the January 28, 2011 Order, the Commission accepted the proposed revised rates and suspended their effectiveness to become effective the earlier of June 28, 2011, or a date set by a subsequent Commission order in this proceeding, subject to the conditions set forth in the order to refile the rates to reflect the directives of the January 28, 2011 Order. The Commission directed NYISO to include deliverability costs in the calculation of CONE, to remove its assumption of property tax abatement in the calculation of the NYC CONE, to either support proposed levels of average excess capacity or provide support for an alternate proposal, and to provide additional support for its assumption of interconnection costs for the proxy peaking unit in NYC. While accepting NYISO's winter/summer adjustment with respect to the issue of quantity available, the Commission directed NYISO to revise its winter/summer adjustment to reflect the assumption for the level of excess capacity. The Commission also accepted NYISO's proposed demand curve design curve parameters and other assumptions.

5. The Commission required NYISO to submit a compliance filing reflecting the required changes within 60 days of the order, i.e., by March 29, 2011. However, due to the difficulties of implementing the new demand curves in mid-season, the Commission directed NYISO to indicate in its compliance filing when it anticipates implementing the new demand curves, but no later than November 1, 2011, the date of the start of the six-month winter capability period. Accordingly, the Commission stated that "the currently effective demand curves will remain in effect until superseded."<sup>5</sup>

6. NYISO and other parties filed for expedited clarification and emergency rehearing of the January 28, 2011 Order with respect to the length of the suspension period and the rate in effect during that period. The Commission denied those requests in its March 9, 2011 order.<sup>6</sup> The instant order addresses the remaining requests for clarification and rehearing of the January 28, 2011 Order.

7. On February 25, 2011, the New York City Suppliers<sup>7</sup> filed a request for rehearing of the January 28, 2011 Order. On February 28, 2011, requests for rehearing were filed

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<sup>5</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 168.

<sup>6</sup> *New York Indep. System Operator, Inc.*, 134 FERC ¶ 61,178 (2011) (March 9, 2011 Order).

<sup>7</sup> For purposes of this proceeding, the New York City Suppliers are: Astoria Generating Company, L.P., the NRG Companies, and TC Ravenswood, LLC.

by Multiple Intervenors<sup>8</sup> and New York State Consumer Protection Board; NYISO; the City of New York and New York State Consumer Protection Board (Consumer Protection Board); New York State Public Service Commission (New York PSC); and Indicated New York Transmission Owners (NYTO).<sup>9</sup>

8. On March 28, 2011, NYISO filed revisions to section 5.14.1.2 of the Services Tariff to establish that the currently effective ICAP demand curves will remain in effect on and after May 1, 2011 until a date set by further Commission order. The Commission accepted the revisions on April 4, 2011.<sup>10</sup> As a result of this order, the suspension period ending June 28, 2011 as set by the January 28, 2011 Order is eliminated.

## **II. Requests for Rehearing**

### **A. System Deliverability Upgrade Costs**

#### **1. NYISO's Proposal and the Commission's Ruling**

9. Pursuant to section 5.12.1 of the Services Tariff and section 25 of Attachment S of the NYISO Open Access Transmission Tariff (NYISO Tariff), a new generator must be determined to be deliverable throughout the capacity zone in which it interconnects in order to participate in the capacity market. If it is determined to not be deliverable, the developer is responsible for the cost of System Deliverability Upgrades necessary to achieve full deliverability as allocated pursuant to the provisions of the Attachment S. System Deliverability Upgrades are in addition to the cost of System Upgrade Facilities required to interconnect for the basic Energy Resource Interconnection Service to sell energy and ancillary services in the NYISO markets. Previous demand curves included the cost of System Upgrade Facilities in CONE; however the deliverability requirements had not yet been established during the prior demand curve reset.

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<sup>8</sup> Multiple Intervenors is an unincorporated association of approximately 55 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State.

<sup>9</sup> The Indicated New York Transmission Owners are: Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., Long Island Power Authority, New York Power Authority, New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and Rochester Gas and Electric Corporation.

<sup>10</sup> *New York Indep. System Operator, Inc.*, 135 FERC ¶ 61,002 (2011) (April 4, 2011 Order).

10. In its November 30, 2010 filing, NYISO proposed that deliverability costs be excluded from the CONE of the rest-of-state proxy unit located in the Capitol Zone. NYISO argued that inclusion of these costs would suppress the desired economic signals because the resultant increased value of net CONE would effectively shift the deliverability costs to capacity buyers, inclusion would provide a windfall to existing generators that are grandfathered from deliverability requirements, and it would skew retirement signals.

11. In the January 28, 2010 Order, the Commission disagreed with NYISO and directed NYISO to revise its demand curve for NYCA and, if necessary, NYC and LI, to reflect the estimated cost of System Deliverability Upgrades. The Commission reasoned that deliverability costs are a required cost of investment for interconnection customers in order to participate in the New York capacity market and be “economically viable” as required for the choice of demand curve peaking unit; and thus, are included in the “current localized levelized embedded cost of a peaking unit” that the Services Tariff provides should be included in the formulation of the demand curve.<sup>11</sup> The Commission stated that System Deliverability Upgrades meet this tariff requirement of “current, localized, and embedded” costs.

12. The Commission rejected arguments that inclusion of deliverability costs skews intended economic signals or runs contrary to Commission objectives when it accepted the deliverability provisions contained in Attachment S of the NYISO Open Access Transmission Tariff. With respect to the latter argument, the Commission concluded that inclusion of System Deliverability Upgrade costs does nothing to decrease the incentive to locate in areas where capacity is deliverable because the developer, in determining where to locate, will still evaluate profitability over the life of the project. All costs of constructing a generator are initially borne by the developer and inclusion of such costs in CONE does not alter this cost allocation.

13. The Commission also rejected arguments that capacity buyers will, in effect, subsidize developers and that windfalls will occur if System Deliverability Upgrade costs are included. The Commission concluded that the proper inclusion of actual costs of new entry into the demand curve cannot be characterized as a “windfall” and stated that markets often provide infra-marginal revenues to non-marginal resources. The Commission further stated that exclusion of these costs results in a net CONE that does not accurately reflect the developer’s costs and thus may discourage investment.

14. Finally, the Commission agreed with NYISO and the Independent Market Monitoring Unit (MMU) that creation of a new capacity zone could provide better

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<sup>11</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 53 (citing NYISO Services Tariff section 5.14.1.2).

locational signals, but concluded that this argument does not support the exclusion of required deliverability costs from the determination of net CONE.

## 2. Requests for Rehearing

15. NYISO, the City of New York and the Consumer Protection Board, and Multiple Intervenors seek rehearing on the Commission's decision to include the cost of System Deliverability Upgrades in the ICAP demand curves. These parties argue that the Commission erred in failing to consider the impacts to consumers that will result from including System Deliverability Upgrade costs in the peaking unit's CONE in contravention of the Commission's consumer protection responsibility under the Federal Power Act.<sup>12</sup> The City of New York and the Consumer Protection Board and Multiple Intervenors state that the inclusion of System Deliverability Upgrade costs in net CONE, unjustly allows new entrants to recover these costs from customers and contravenes prior acceptance of cost allocation provisions for System Deliverability Upgrades.<sup>13</sup>

16. The parties further argue that the inclusion of System Deliverability Upgrade costs in CONE skews price signals.<sup>14</sup> NYISO states that including these costs in CONE will increase the probability that developers who locate in areas where they incur high System Deliverability Upgrade costs will be insulated from the economic consequences of their decisions. Multiple Intervenors argue that the inclusion of these costs will put an upward pressure on capacity prices and thereby send an economic signal that additional capacity supply resources are necessary and new investment is warranted, which they state is entirely contrary to the current substantial levels of excess capacity existing and projected to persist in New York for the foreseeable future. Multiple Intervenors argue that the Commission dismissed concerns that inclusion of System Deliverability Upgrade costs will create windfall profits to existing generators. Multiple Intervenors argue that existing generators insulated from System Deliverability Upgrade costs gain an additional competitive advantage because they will be compensated as though they incurred these

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<sup>12</sup> NYISO Request for Rehearing at 33 (citing *Pennsylvania Water & Power Co. v. FPC* 343 U.S. 414, 418 (1952); *Williams Pipeline Co.* 21 FERC ¶ 61,260, at 61,582 (1982)).

<sup>13</sup> City of New York and Consumer Protection Board February 23, 2011 Request for Rehearing at 23 (citing *New York Indep. Sys. Operator*, 122 FERC ¶ 61,267 (2008) and *New York Indep. Sys. Operator*, 126 FERC ¶ 61,046 (2009) (Deliverability Orders)).

<sup>14</sup> NYISO argues that the Commission's ongoing proceeding in Docket No. ER04-449-023, which is examining the criteria for the creation of new capacity zones, provides the appropriate forum to evaluate economic signals to locate capacity—a view that NYISO states is acknowledged by the Commission, the MMU, and other parties.

costs. The parties argue that the fact that the developer initially pays these costs is irrelevant because, under the January 28, 2011 Order, the developer will subsequently receive full recovery for these costs.

17. NYISO states that the Commission's decision contravenes the orders on deliverability where the Commission found that it was reasonable and consistent with a beneficiary-pays approach to require developers to be primarily responsible for paying for those transmission system upgrades necessary to achieve deliverability.<sup>15</sup> NYISO also cites the Patton affidavit that "including [System Deliverability Upgrade] costs in the Demand Curves is not an efficient means of providing long-term economic signals to prospective investors in new resource."<sup>16</sup>

18. NYISO argues that the January 28, 2011 Order incorrectly finds that excluding deliverability costs results in a net CONE that does not accurately reflect the developer's costs and thus, may discourage investment. In support, NYISO states that it presented evidence that projects can be cited in regions where deliverability constraints exist such as NYC without incurring System Deliverability Upgrade costs; and therefore, these costs are not necessarily a required cost of new entry and should not be included in CONE.<sup>17</sup> The City of New York and the Consumer Protection Board cite the testimony of John Beck of Consolidated Edison Company of New York, who pointed to load Zone J locations where a developer could site a generating facility without incurring any System Deliverability Upgrade costs and who also explained that the size of the generating facility can be determinative as to whether any deliverability costs are imposed.<sup>18</sup>

19. In addition, NYISO, Multiple Intervenors, and the City of New York and the Consumer Protection Board all advocate that the Commission account for deliverability costs through the creation of new capacity zones.

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<sup>15</sup> NYISO February 28, 2011, Request for Rehearing at 35 (citing NYISO 122 FERC ¶ 61,267, at P 46 (2008)).

<sup>16</sup> *Id.* at 35 (citing November 30, 2010 filing, Affidavit of David B. Patton at P 18).

<sup>17</sup> *Id.* (citing NYISO January 6, 2011 Answer at 19-20 referring to Hudson Transmission Partner and Bayonne Energy Center projects in Class Years 2008 and 2009 respectively).

<sup>18</sup> City of New York and Consumer Protection Board February 28, 2011 Request for Rehearing at 26-27 (citing New York Transmission Owners January 10, 2011 Answer, Beck Affidavit at P 9, 19-22).

### 3. Commission Determination

20. The Commission denies rehearing and continues to maintain that System Deliverability Upgrade costs should be included in the determination of CONE. Parties incorrectly argue that we have failed to consider the interests of consumers. The demand curve construct protects consumers by establishing a price schedule for capacity that reasonably reflects net entry costs. Excluding costs incurred by entrants would suppress the prices below a competitive level and harm consumers by failing over the long-term to support efficient entry and exit by private investors. The actual price paid (in contrast to estimated net CONE) depends on the supply offered. Market power mitigation rules require competitive offers from all existing capacity suppliers and the resulting market clearing prices may be well below net CONE during surplus conditions. Consistent with section 5.14.1.2 of the Services Tariff, the demand curve shall include the “current localized levelized embedded cost of a peaking unit,” and as we noted in the January 28, 2011 Order, System Deliverability Costs are incurred by new peaking units and satisfy this requirement.

21. Moreover, our decision to require the inclusion of System Deliverability Costs in the determination of CONE is appropriate and fully consistent with our prior Deliverability Orders regarding cost responsibility. As we stated in the January 28, 2011 Order, System Deliverability Upgrade costs incurred by a developer are a part of localized, embedded costs and as such should be included in CONE, just as System Upgrade Facilities are included.<sup>19</sup> A requirement that a developer must pay interconnection costs, just as it must pay all other entry costs, is not a prohibition on reflecting those entry costs in the CONE. All entry costs, including interconnection costs, must be recoverable from the market. Including interconnection costs does not guarantee their recovery, just as there is no guarantee for any particular cost recovery, but pricing capacity using the demand curve is premised on the view that an efficient entrant would expect to recover all costs over the life of the resource. A requirement that entrants pay for interconnection costs is not a requirement that they be denied a market opportunity to recover those costs.

22. We disagree that the inclusion of System Deliverability Upgrade costs will mute economic signals for generators to locate in deliverable areas and will create windfall payments. ICAP market payments should induce entry where it is most efficient and efficient entry is not necessarily entry in deliverable areas. For example, a new rest-of-state generator located north and west of the UPNY/SENY interface may not be able to deliver to Zones G and I (Lower Hudson Valley); and as a result, would not be able to participate in the rest-of-state capacity market without obtaining a deliverability

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<sup>19</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 57.

determination that may result the need for the cost of System Deliverability Upgrades.<sup>20</sup> We conclude that it is appropriate for economic signals to account for deliverability costs in this case since they are relevant to an efficient siting decision given the current zone boundaries. In the event that a new capacity zone is created, system deliverability costs may not be relevant in a future demand curve reset process. However, at this time, and in this proceeding, we are not attempting to judge the merits of creating a new capacity zone; that is under consideration in Docket No. ER04-449-023. Moreover, we lack an adequate record in this proceeding to make the factual determinations necessary to decide if and where new zone(s) should be added.

23. The Commission addressed the windfall argument in the initial ICAP demand curve order stating that all suppliers are entitled to the same treatment in the ICAP market and that the difference in profit potential among resources is a market signal the Commission would expect to encourage new generation.<sup>21</sup> We also emphasize that properly accounting for all appropriate System Deliverability Upgrade costs attributable to new entry does not confer a “windfall” on existing suppliers that do not incur such System Deliverability Upgrade costs. Existing suppliers do not need to actually incur *any* new entry costs to receive the market clearing price set by the ICAP demand curves. The market clearing price determined by the demand curve appropriately is the competitive price received by all existing suppliers even though the demand curves are also designed, *inter alia*, to incent or dis-incent future new entry of ICAP depending on whether there is excess capacity, i.e., available ICAP that exceeds the minimum ICAP requirement. That is, the ICAP rates defined by the demand curves currently apply to sales of all existing ICAP, but will also generally apply to new ICAP that enters the market in the future. Therefore, Multiple Intervenors’ argument that receipt of a competitive market clearing price in the ICAP market confers a windfall on any such existing supplier whose capacity clears in the market is not justified just because some suppliers who receive such prices do not incur a particular cost used to design the net CONE upon which the demand curve prices are based.

24. Finally, we reject the argument that a lack of a current need for new investment to add additional ICAP is reason enough to exclude consideration of System Deliverability Upgrade costs. As noted previously, the ICAP demand curves are price schedules reflecting a range of prices based on the net CONE that, when all competitive ICAP supply offers are factored in, determine a competitive market clearing price for all ICAP suppliers. The demand curves yield prices that vary relative to the amount of competitive

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<sup>20</sup> *Id.* P 8, 54-55. *See also* NYISO November 30, 2010 Filing, NERA Report at 73-74.

<sup>21</sup> *New York Indep. Sys. Operator, Inc.*, 103 FERC ¶ 61,201, at P 81 (2003).

ICAP offered in the market and are designed to encourage or discourage new entry depending on whether or not there is a surplus or deficiency of ICAP in the market. As designed, the demand curves yield actual market clearing prices under surplus conditions that are below net CONE and, therefore, discourage new entry and encourage exit as long as the surplus conditions exist. Conversely, if the surplus conditions no longer exist and there is less ICAP available than needed to meet the minimum ICAP requirement, the demand curves are designed to yield prices that exceed net CONE and, therefore, encourage new entry. Thus, because the surplus of ICAP already is factored into the design of the demand curves to produce lower rates that discourage new investment, the lack of the current need for new investment does not support achieving even lower prices by lowering the entire demand curve in a way that understates the competitive cost of new entry.

25. Accordingly, we deny rehearing and affirm our ruling that NYISO should include the estimated cost for System Deliverability Upgrades in the calculation of net CONE for NYCA and, if necessary, for other capacity zones.

**B. New York City Tax Abatement**

**1. NYISO's Proposal and the Commission's Ruling**

26. At the time of the 2008 demand curve reset proceeding, the New York City Industrial and Commercial Incentive Program granted, as a right, reductions in real property taxes to new industrial and commercial projects, including power plants. The Commission took that reduction into consideration and it was incorporated in the calculation of the NYC CONE. Subsequently, a revised program was established that effectively removed the tax abatement for new generating facilities in New York City. On August 3, 2010, the Board of Directors of the New York City Industrial Development Authority (NYCIDA) revised the Uniform Tax Exemption Policy (UTEP) to induce the development of in-City peaking generating units by creating a temporary tax abatement for qualifying units. In its November 30, 2010 filing, NYISO stated that generation projects that satisfy certain specified criteria are eligible for 12 years of exemption from property tax and exemption from recording taxes, mortgage recording taxes, and sales and use taxes.<sup>22</sup> NYISO added that, unlike the former program, the NYCIDA program is discretionary on the part of NYCIDA. NYISO's proposed NYC demand curves assume full tax abatement for the NYC peaking unit.

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<sup>22</sup> First Amendment to Third Amended and Restated Uniform Tax Exemption Policy of the New York Industrial Development Agency, approved August 3, 2010, as amended November 9, 2010 (UTEP), *see* January 28, 2011 Order, 134 FERC ¶ 61,058 at P 65.

27. NYISO argued that the criteria for tax abatement are clear, that it is in New York City's economic interest to grant abatement, and that New York City will likely act in a manner consistent with this interest. Protesters argued in favor of the incorporation of property taxes into the calculation of net CONE without recognition of the tax abatement because the tax abatement is discretionary, it is unclear how it will actually be applied, it results in nearly a 40 percent understatement of NYC demand curves, it will chill potential investment in new resources in New York City, and it will eviscerate NYISO's buyer market power mitigation rule. New York City Suppliers asserted that the proxy unit would not satisfy either of the objective heat rate criteria set by NYCIDA.

28. In the January 28, 2011 Order, the Commission found NYISO's proposal to assume full tax abatement for the NYC peaking unit was not just and reasonable and did not accept it. The Commission reasoned that property taxes are legitimate costs that are normally included in the cost of new entry, that the tax abatement in this case is discretionary, and that whether the LMS 100 proxy unit meets the specific requirements for tax abatement is unclear.

## 2. Requests for Rehearing

29. Parties that seek rehearing of the Commission decision to include property tax in the calculation of the NYC demand curve assert that the Commission erred in that: (1) the record does not support a conclusion that tax abatement will not be granted; (2) the Commission did not consider consumer impacts and the resultant outcomes of its decision; and (3) the Commission wrongly granted credence to claims that an LMS 100 peaking unit would not qualify under the UTEP criteria.

30. NYISO, the City of New York and the Consumer Protection Board, and NYTOs state that the Commission has not met its obligation to offer a reasoned explanation for its tax abatement decision and has not engaged in reasoned decision-making.<sup>23</sup> They contend that the Commission's determination can only be supported by evidence that there is no chance, or it is highly unlikely, that a developer would receive the abatement and state that no such evidence exists in the record. NYISO maintains that the Commission found only that it is unclear a developer would receive the abatement because it is discretionary; and therefore, assuming a developer will not receive tax abatement is unreasonable based on the evidence in the record. NYISO also states that the January 28, 2011 Order effectively imposed an unlawfully high burden of proof on NYISO where Commission and judicial precedents are clear that proposed rates need only be just and reasonable.<sup>24</sup> NYISO contends that the November Filing made a

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<sup>23</sup> NYISO February 28, 2011 Request for Rehearing at 7.

<sup>24</sup> *Id.* at 19.

reasonable assumption that NYCIDA would grant tax abatements, consistent with the its stated interests, which the Commission rejected because NYISO did not prove with absolute certainty that 100 percent of the abatements would always be granted—a standard, that according to NYISO, is more than the “just and reasonable” showing required.

31. The City of New York and Consumer Protection Board state that the Commission misperceived the scope of NYCIDA’s discretion. The discretionary nature of the tax abatements available under the UTEP does not warrant elimination of the tax abatement from the calculation of the net CONE. The City of New York and Consumer Protection Board state that NYCIDA’s discretion in granting tax abatement and other benefits is not unbounded or limitless. Thus, although NYCIDA can exercise discretion, its decisions are subject to the same type of scrutiny by the courts as are the Commission’s decisions. City of New York and Consumer Protection Board contend, therefore, there is no basis for any concern that NYCIDA’s ability to exercise discretion, in and of itself, will invariably and irreversibly lead to the denial of tax abatement benefits to eligible peaking generating units that are similar to the In-City proxy peaking unit.<sup>25</sup>

32. Although it is not a certainty that 100 percent abatement will be granted to each peaking plant, NYISO maintains that there is no evidence in the record suggesting that a developer would not receive an abatement, or even that the abatement would be unlikely. NYISO states that one must determine an “expected value” associated with the uncertainty factor that takes into account the probabilities of the different outcomes. NYISO asserts that even the New York City Suppliers, who objected to full abatement, acknowledged a likelihood that the NYC peaking plant would receive a significant abatement of property taxes.<sup>26</sup> The City of New York and Consumer Protection Board state that even if the Commission chose to discount the evidence offered by the City of New York in support of a full tax abatement, the totality of evidence presented indisputably demonstrated that the Commission should have found that some level of tax abatement would be appropriate.

33. The New York PSC states that rather than rejecting any tax abatement outright at this time, it proposes a compromise approach. The New York PSC recommends that the Commission accept NYISO’s proposal as filed, i.e., with an assumption of tax abatement,

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<sup>25</sup> City of New York and Consumer Protection Board February 28, 2011 Request for Rehearing at 19-20.

<sup>26</sup> NYISO February 28, 2011 Request for Rehearing at 17 (citing New York City Suppliers December 21, 2010 Protest at 46-47, 51-52, Answer of the New York City Suppliers January 14, 2011 Answer at 7-8).

until and unless, a final determination is made by New York City that an LMS 100 peaking unit should be denied tax abatement or is ineligible for abatement under the NYC tax abatement program.<sup>27</sup> In the event New York City makes either determination, the New York PSC maintains that the Commission's direction would be that the NYISO promptly file an increase in the Demand Curves as appropriate going-forward. According to the New York PSC, this would signal to prospective investors that they will be able to adequately recover their costs. Such an approach, according to the New York PSC, is consistent with the intended design of the demand curves to incent new entry when needed, which was a key component of the New York PSC's support for the initial implementation of the demand curves, and explicitly recognized by the Commission.

34. NYISO asserts that the Commission did not adequately consider consumer impacts. NYISO contends that the January 28, 2011 Order did not address the resultant outcomes that would follow its conclusion as required by the Federal Power Act (FPA) to protect consumers against unjust and unreasonable rates.<sup>28</sup> NYISO also asserts that because the granting of the full tax abatement is likely (although not an absolute certainty), establishing an ICAP Demand Curve that assumes no abatement will substantially overcompensate New York City suppliers and contravene the Commission's own principles for establishing a just and reasonable ICAP Demand Curve and its own policy of giving deference to state and local governmental bodies on matters that fall within the expertise or jurisdictional prerogatives of the respective body.<sup>29</sup>

35. NYISO, the New York PSC, and NYTOs state that the January 28, 2011 Order disregarded, without explanation, the rationales offered by NYISO and others<sup>30</sup> that it would be irrational to assume that the NYCIDA, as an economic development agency,

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<sup>27</sup> New York PSC February 28, 2011 Request for Rehearing at 5 (citing *Sithe New England Holdings, LLC v. FERC*, 308 F.3d 71, 77 (1st Cir. 2002) (finding that the Commission has considerable discretion in regulating ICAP charges and is not bound to ensure generators receive "just and reasonable" ICAP rates under the Federal Power Act)).

<sup>28</sup> NYISO February 28, 2011 Request for Rehearing at 7.

<sup>29</sup> *Id.* at 7, 13-14 (citing *New York Independent System Operator, Inc.*, 131 FERC ¶ 61,170 at P 137 (2010)).

<sup>30</sup> *Id.* at 9 (citing *e.g.* NYISO January 6, 2011 Answer at 20, and NYTOs January 10, 2011 Answer at 12-17).

would exercise its discretion in a way that would inflate NYC capacity prices.<sup>31</sup> NYISO contends it is readily foreseeable that doing so would harm economic development and contravene both the stated public policy goals of the UTEP, New York City, and the statutory purpose of NYCIDA.

36. NYISO asserts that while new LMS 100 peaking units are not entitled to tax abatements as a matter of right, NYCIDA testified that its discretion was constrained by the UTEP and that it was reasonable to assume that denials would be unusual.<sup>32</sup> NYISO contends that the City of New York also described that New York State law applicable to all Industrial Development Agencies, including the NYCIDA, requires that it have a policy that delineates how and when it could deviate from its policy.<sup>33</sup> NYISO maintains that the UTEP provides those guidelines and prevents the NYCIDA from arbitrarily denying a request for abatement.<sup>34</sup>

37. With respect to eligibility of a peaking plant, NYISO maintains that the LMS 100 heat rates and parasitic load information provided to the City by Mr. Perri was different from the information that was later included in his affidavit on behalf of the New York City Suppliers because it was intended to cast doubt on whether such a unit would qualify under the UTEP criteria.<sup>35</sup> NYISO states that it explained that the LMS 100 unit would satisfy the second of the UTEP's two objective criteria, and thus be eligible for abatement.<sup>36</sup> NYISO states that it is not reasoned decision-making for the Commission to base a conclusion of zero abatement on a party's disagreement with NYISO and the NYCIDA, which the Commission characterizes as a "debate" regarding the eligibility of the LMS 100 unit under the UTEP.<sup>37</sup> NYISO maintains that the Consultant's Report,<sup>38</sup>

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<sup>31</sup> *Id.* (citing City of New York December 21, 2010 Comments at 18, n. 34); NY PSC Request for Rehearing at 4 (citing N.Y. GEN. MUN. LAW § 917 (McKinney 1999)).

<sup>32</sup> *Id.* at 11 (citing City of New York January 6, 2011 Answer at 17-18).

<sup>33</sup> *Id.* (citing City of New York December 21, 2010 Comments, Babis Affidavit at P 8, 11,14).

<sup>34</sup> *Id.* (citing City of New York December 21, 2010 Comments, Babis Affidavit at 11).

<sup>35</sup> *Id.* at 12 (citing City of New York January 6, 2011 Answer at 13 and Exhibit A).

<sup>36</sup> *Id.* (citing NYISO January 6, 2011 Answer, Affidavit of Christopher D. Ungate at PP 7-11 ("Ungate Affidavit")).

<sup>37</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 88.

the Consultant's Affidavit, and the City of New York's pleadings including affidavits, fully support a finding that the peaking plant would qualify for full tax abatement under the UTEP. NYISO maintains that the Perri Affidavit only provided an example of how one particular unit, PSPG's South Pier Project might not qualify and did not contend that every LMS 100 unit would fail to qualify.<sup>39</sup>

38. NYISO contends that the Commission should not rely on the data included in the Perri Affidavit because they were introduced after the completion of the Consultant's Report and stakeholder process. NYISO states that the only reasonable conclusion, based on the evidence provided in the Consultant's Report, the Consultant's affidavit (the Ungate Affidavit), and the City of New York's pleadings including the NYCIDA's affidavits, is that new peaking plants in NYC would generally be expected to qualify for full property tax abatement. NYTOs state that the Commission should have permitted at least partial abatement. To the extent that the Commission relied on the New York City Suppliers' focus on the particular circumstances of an individual unit, NYISO states that the Commission departed, without a reasoned explanation, from its own precedent and from its own finding in the January 28, 2011 Order that the hypothetical LMS 100 plant should be used to set the NYC demand curve.

39. NYISO states that if the evidence proffered in the record left questions unanswered, it was unreasonable for the Commission not to seek additional input on tax abatement questions. To the extent that the Commission believed that a genuine dispute over an issue of material fact existed, NYISO maintains it should have<sup>40</sup> set the matter for a paper hearing, convened a technical conference, or taken some other step to resolve the factual dispute. None of these potential alternative approaches would have delayed establishing new demand curves beyond the period contemplated by the January 28, 2011 Order.

40. With regard to the question of NYCIDA's discretion in granting a tax abatement, the testimony of Maureen Babis, Executive Director of NYCIDA, stated that NYCIDA will not arbitrarily ignore or deviate from the specific UTEP requirements for eligibility

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<sup>38</sup> See NYISO November 30, 2010 Filing at *Independent Study to Establish Parameters of the ICAP Demand Curve for the New York Independent System Operator* at 73 (September 3, 2010, as revised September 7, 2010 and November 15, 2010) (NERA/S&L Report); see also NYISO January 6, 2011 Answer, Ungate Affidavit at PP 7-11.

<sup>39</sup> See New York City Suppliers December 21, 2010 Protest, Perri Affidavit at P 9, 10.

<sup>40</sup> NYISO February 28, 2011 Request for Rehearing at 17.

for the tax abatement. She stated that any decision by NYCIDA that deviates from the assistance provided by UTEP will not be arbitrarily made and will be explained to the NYCIDA Board of Directors. Ms. Babis further stated that to ignore or deviate in every case from the specific set of requirements for peaking units adopted by the NYCIDA Board defies credulity and is inconsistent with the manner in which the NYCIDA and its Board operate.<sup>41</sup> In addition, the City of New York stated that granting tax abatements is consistent with New York City's publicly stated policy goals such as reducing greenhouse gas emissions, promoting clean and renewable generation, maintaining and creating jobs, and repowering older less efficient facilities.<sup>42</sup> Further, the Babis Affidavit stated that it is in New York City's economic interest to grant abatements to peaking units.<sup>43</sup> Indeed, according to New York City, for more than 25 years, no new electric generating facility has been constructed in the City without receiving a full tax abatement for an extended period.<sup>44</sup>

### 3. Commission Determination

41. We grant rehearing on the question of the inclusion of property tax in the calculation of the NYC net CONE as discussed below. We find that, upon further review of the record and a change in circumstances, NYC net CONE should reflect the assumption that the LMS 100 proxy peaking unit will receive property tax abatement. In rejecting NYISO's proposal to assume tax abatement in the calculation of NYC net CONE, the Commission was primarily concerned with the discretionary nature of the tax abatement program as compared with the previous as-of-right program that it replaced.

42. Since the parties filed their requests for rehearing, New York has changed its law. On May 18, 2011, New York State enacted legislation (New York Assembly Bill 7511) that eliminates the UTEP's discretion by returning the NYC tax abatement to an as-of-right program.<sup>45</sup> The new law also eliminates the need to consider the UTEP heat rate and other criteria by defining eligible peaking units in such a way as to mandate the assumption that tax abatement will apply to any new peaking unit in NYC. The new law states that it is amending the tax law "for the purpose of making peaking units eligible for

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<sup>41</sup> City of New York January 5, 2011 Answer, Attachment B, Affidavit of Maureen Babis at P 4 (re-submitted March 11, 2011).

<sup>42</sup> City of New York December 21, 2010 Comments at 18.

<sup>43</sup> City of New York December 21, 2010 Comments at 18, Babis Affidavit at P 13.

<sup>44</sup> City of New York, *et al.* February 28, 2011 Request for Rehearing at 14.

<sup>45</sup> 2011 N.Y. Laws Chapter 28, (May 18, 2011).

benefits, as of right, under the industrial and commercial abatement program.”<sup>46</sup> Thus, under this law, “an applicant who has performed industrial construction work in any area on a peaking unit, shall be eligible for an abatement of real property taxes.” The new law defines a “peaking unit” to mean the peaking unit that NYISO’s tariff designates as such (*i.e.*, an LMS 100 peaking unit for NYC) or that has average annual operating hours of less than 18 hours per start.<sup>47</sup> Accordingly, the developer of an LMS 100 peaking unit in NYC shall be eligible for 100 percent tax abatement for a fifteen-year period provided a building permit is issued on or before April 1, 2015.

43. We find that this development ameliorates the concerns that the Commission had with the discretionary nature of the UTEP and the UTEP eligibility criteria; and now believe, therefore, that NYCIDA would grant tax abatement to a NYC peaking unit in accordance with the enacted legislation. We find that the inclusion of the tax abatement assumption in calculating the NYC net CONE is appropriate, and we direct NYISO to revise the demand curve accordingly. Therefore, NYISO is directed to file tariff revisions within 30 days of the date of this order to include revised demand curve prices in tariff section 5.14.1.2 that reflect the effect of full NYC tax abatement as applicable for a peaking unit installed in New York City.

### **C. Expected Level of Average Excess Capacity**

#### **1. NYISO’s Proposal and the Commission’s Ruling**

44. Section 5.14.1.2 of the Services Tariff requires NYISO to adjust CONE to reflect an assumed level of average excess capacity to account for the expectation that NYISO will not permit the quantity of capacity to fall below the minimum required amount. Section 5.14.1.2 provides “the periodic review shall assess...the likely projected Energy and Ancillary Services revenues of the peaking unit...under conditions in which the available capacity would equal or slightly exceed the minimum Installed Capacity requirement...” The assumed level of excess capacity affects both the determination of projected energy and ancillary services revenues and the amount of projected capacity revenues realizable in the spot capacity market, which revenues are netted from CONE to produce net Cone used in the demand curves. A higher assumed level of excess capacity decreases revenue offsets and thus results in a higher net CONE, while a lower assumed level of excess capacity has the opposite effect.

45. In its November 30, 2010 filing, NYISO proposed a level of average excess capacity equal to one-half the capacity of the designated peaking resource for each

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<sup>46</sup> *Id.* § 1.

<sup>47</sup> *Id.* § 2.

locality, i.e., 95 MW for NYC and LI and 207 MW for NYCA.<sup>48</sup> In doing so, NYISO assumed that “the timing of [new] entry could reasonably coincide with the time at which the excess [capacity] is anticipated to fall to zero,”<sup>49</sup> which would lead to an average excess capacity equating to one-half the capacity of a new entrant designated peaking resource. NYISO stated that this assumption was consistent with the Services Tariff and the Consultant’s concept of the average excess capacity adjustment, and so “concerns that NYISO’s estimates... do not reflect ‘real world’ conditions or unreasonably assume that NYISO and investors will have ‘perfect foresight’ are therefore misplaced.”<sup>50</sup> NYISO also determined that the use of the designated peaking resource for calculating the average excess capacity adjustment is reasonable because it is consistent with the Services Tariff and because it is the efficient addition to maintain reliability. NYISO stated that its proposed average excess capacity adjustments were “lower than those in the previous demand curve reset in part because NYISO and the Consultant determined that it is appropriate to set the level in relation to the size of the peaking unit used to establish the demand curves rather than on a larger combined cycle unit (as was done in the 2007 reset).”<sup>51</sup>

46. In the January 28, 2011 Order, the Commission found that NYISO’s proposed average excess capacity adjustments were unsupported and, therefore, could not be found to be just and reasonable. Therefore, the Commission found that the levels of average excess capacity adjustments used in the last reset proceeding should be maintained for this reset or, in the alternative, NYISO could propose to use a new level of average excess capacity provided NYISO fully supported that proposal. The Commission affirmed the appropriateness of considering a level of excess capacity in the determination of energy and ancillary services revenues and in adjusting CONE in recognition that likely actual capacity revenues will be below those modeled at equilibrium due to expected excess capacity in the New York market.<sup>52</sup> The Commission stated that a level of available capacity that slightly exceeds the minimum ICAP requirement should apply uniformly to all estimates that depend on the level of installed

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<sup>48</sup> Stated as a percentage, NYISO proposed average excess capacity adjustments of 1 percent, 1.1 percent, and 2.1 percent in NYCA, New York City, and Long Island, respectively.

<sup>49</sup> NYISO November 30, 2010 Transmittal Letter at 17.

<sup>50</sup> *Id.* at 18-19.

<sup>51</sup> *Id.* at 19.

<sup>52</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 115-16.

capacity. Further, the Commission noted that the current state of significant capacity surplus in the NYCA is not relevant to the specification of the demand curves.

## 2. Requests for Rehearing and Clarification

47. NYISO, the City of New York, Multiple Intervenors, NYTOs, and the New York State Consumer Protection Board request rehearing of the Commission's rulings regarding the average excess capacity adjustment.

48. NYISO and load-side entities request that the Commission reverse its determination that NYISO must either provide additional support for proposed excess capacity levels or continue to use the excess capacity levels that are incorporated in the currently effective ICAP Demand Curve. NYISO asserts that the Commission should accept as just and reasonable either NYISO's proposal in its November 30, 2010 filing or the levels of average excess capacity that were included in the MMU's testimony attached to the November 30, 2010 filing.<sup>53</sup> The MMU proposed an assumption of average level of excess capacity equal to the size of the peaking resource (i.e., 195 MW). Load-side entities generally request that the Commission accept the proposal included in the November 30, 2010 filing.

49. NYISO and load-side entities argue that NYISO's proposal in the November 20, 2010 filing is reasonable and supported and that the proposed levels of average excess capacity strike a balance between the extremes of under-compensating and over-compensating suppliers. NYISO argues that it is reasonable for NYISO to assume that previous levels of assumed average excess capacity may have contributed to the current capacity surplus. NYISO cautions that it is very important to determine whether the excess capacity assumption is too high and may, therefore, perpetuate a capacity surplus that generates unnecessary costs for consumers. Further, NYISO and the load-side entities argue that setting the excess capacity level necessarily involves judgment and the proposal reflects the reasoned judgment of NYISO and the MMU. According to the parties, the Commission is required by section 205 of the FPA to accept NYISO's proposal as long as it is within the zone of reasonableness, and the Commission should not supplant the judgment of the filing party with its judgment or the judgment of intervenors.<sup>54</sup>

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<sup>53</sup> NYISO November 30, 2010 Filing, Attachment 1 at P 27-28.

<sup>54</sup> New York Transmission Owners, February 28, 2011 Filing at 12 (citing *Entergy Service, Inc.*, 130 FERC ¶ 61,026, at P 42 (2010); *Cal. Indep. Sys. Operator Corp.*, 128 FERC ¶ 61,103, at P 318 (2009); *PJM Interconnection, L.L.C.*, 127 FERC ¶ 61,197, at P 38 (2009)).

50. NYISO and load-side entities contend that the proposal included in the November 30, 2010 filing is reasonable and supported because NYISO's proposed levels of average excess capacity comport with the Services Tariff, which specifies that the capacity level should "equal or slightly exceed the minimum ICAP requirement." These parties add that objections to NYISO's assumption regarding timing on the grounds that such conditions might not occur in the market are not pertinent in light of the fact that the Services Tariff requires only that the ICAP Demand Curves incorporate a level of excess capacity that would equal or slightly exceed the minimum ICAP requirement.

51. NYISO and load-side entities further contend that the use of the capacity of the peaking plant is reasonable and supported because it is consistent with the other factors used to establish the ICAP Demand Curve, is the most efficient addition to maintain reliability, and is consistent with surplus conditions in New York State. Parties add that NYISO's proposed use of the peaking plant to calculate the average excess capacity, which represents a change from NYISO's use of the capacity of the combined cycle plant in the prior reset, is reasonable because the peaking plant has a smaller capacity than the combined cycle plant, appropriately reflects the size of an efficient addition to maintain reliability, and is consistent with the reality that there is now and is expected to continue to be a significant capacity surplus in New York State. NYISO requests, at a minimum, that the Commission recognize that it is just and reasonable to use the peaking unit to determine the level of excess.

52. NYISO and load-side entities assert that the January 28, 2011 Order, contrary to precedent, applied an impermissibly stringent burden of proof. First, NYISO and load-side entities argue that the Commission erred because the Commission did not limit the scope of its inquiry to whether NYISO's proposal was just and reasonable, but instead required NYISO to prove that its proposal was superior to what was accepted in previous orders. Second, NYISO and load-side entities state that NYISO's support in this reset is at least comparable to NYISO's support in the previous reset, including because of support in this reset derived from NYISO's assumption regarding timing of new entry.

53. NYISO states that if the Commission refuses to accept NYISO's proposal on rehearing, it should accept the MMU's proposal. NYISO states that it does not believe that the MMU's recommendations for NYC or LI were unjust, unreasonable, or inadequately supported. NYISO adds that the MMU's proposal specifically addresses issues regarding timing of entry. In addition, NYISO avers that NYISO and the MMU were in conceptual agreement regarding the use of the peaking plant to establish the level of excess. NYISO also asserts that the MMU's proposal, like NYISO's proposal, sends more accurate price signals and is more consistent with both the Services Tariff's requirements and the other ICAP Demand Curve parameters than the alternatives favored by supply-side protestors.

54. NYISO argues that it would be a fundamental error if the Commission were to require NYISO to rely on "observed" levels of capacity to estimate excess capacity

levels. NYISO argues that this would be inconsistent with the Services Tariff. NYISO also argues that such an approach would be circular and could inadvertently perpetuate capacity surpluses or deficiencies.

55. Finally, NYISO and load-side entities argue that the currently effective excess capacity levels lack evidentiary support in the record in this proceeding for use over the for the next three capability years. NYISO and load-side entities also contend that using the currently-effective adjustments would be internally inconsistent because they are based on the capacity of a combined cycle unit.

56. IPPNY and NYISO each request clarification regarding the Commission's direction in paragraphs 122 and 129 of the January 28, 2011 Order that NYISO should use a "level of excess capacity consistently throughout the analyses used to develop the demand curves." IPPNY requests that the Commission clarify that the same excess capacity variable must be used in every instance where this factor is applied, for all 30 years, to calculate the net CONE of each respective proxy unit, including when determining the capacity risk factor adjustment, energy and ancillary service revenues, System Deliverability Upgrade costs, and Transmission Congestion Contract offset components of the net CONE calculations. NYISO requests that the Commission clarify that NYISO need not alter the level of excess capacity used to determine energy and ancillary services revenue offsets, and requests rehearing in the event the Commission meant to direct otherwise. NYISO argues that the Commission failed to articulate any changed circumstances that would form a basis for denying what had been previously found to be just and reasonable in the prior reset. NYISO also contends that requiring NYISO to change the energy and ancillary services revenue offsets would make the January 28, 2011 Order internally inconsistent.<sup>55</sup>

57. IPPNY also requests that the Commission clarify that NYISO must set the excess capacity variable "in accordance with the following factors: lumpiness of capacity additions, NYISO Tariff/process protections against a capacity shortage including the consistent reliability signals in New York State; the fact that a merchant generator's entry commitment must be made years in advance of actual conditions; the fact that merchant entry is not coordinated; and the fact that forecasting is imperfect and may be affected by, *inter alia*, economic slowdown."<sup>56</sup>

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<sup>55</sup> NYISO February 28, 2011 Request for Rehearing at 40-41 (arguing that, since paragraph 136 accepted NYISO's proposed energy and ancillary services revenue estimates, the January 28, 2011 Order would be internally inconsistent if paragraphs 122 and 129 were meant to require changes to NYISO's proposed energy and ancillary services revenue estimates).

<sup>56</sup> IPPNY February 24, 2011 Request for Rehearing at 10-11.

### 3. Commission Determination

58. The Commission denies the requests for rehearing and clarification for the reasons discussed below. The arguments on rehearing do not resolve the issue that prevented the Commission from finding NYISO's proposal to be just and reasonable with respect to the expected level of average capacity. NYISO's proposed excess capacity adjustments were, and continue to be, unsupported and therefore cannot be found to be just and reasonable.

59. On rehearing, NYISO and load-side entities caution against under- or over-compensation of suppliers based on the average excess capacity adjustment. To the extent that parties believe that the January 28, 2011 Order did not consider such concerns, they are in error. As further discussed below, it is precisely because the record lacked a demonstration regarding those concerns that the Commission found the proposal to be unsupported.

60. On rehearing, NYISO and load-side entities contend that NYISO's original proposal comports with the Services Tariff, and therefore is just and reasonable. In the January 28, 2011 Order, citing the Services Tariff, the Commission affirmed the appropriateness of considering a level of excess capacity in the determination of energy and ancillary services revenues and in adjusting CONE in recognition that likely actual capacity revenues will be below those modeled at equilibrium due to expected excess capacity in the New York market.<sup>57</sup> However, this tariff requirement to consider a level of excess capacity does not relieve NYISO of the obligation to provide support for the specific level it proposed. NYISO must justify its proposal and explain how it fits within a zone of reasonableness such that the resulting rates are just and reasonable. NYISO cannot support its proposal by simply stating that the proposal is based on its judgment.

61. NYISO does not explain how the proposal in the November 30, 2010 filing comports with the purpose of the excess capacity adjustment as recognized by NYISO and the Commission in prior proceedings.<sup>58</sup> Instead, NYISO simply proposes an assumed level of excess capacity and simply asserts that this assumption is consistent with the Services Tariff. Indeed, NYISO states in the November 30, 2010 filing that it need not consider issues regarding the usage of its assumption for computing the level of

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<sup>57</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 115.

<sup>58</sup> See, e.g., *New York Indep. Sys. Operator*, 111 FERC ¶ 61,117, at P 41, 46-48 (2005) (finding that the net revenue offsets should reflect revenues expected when supply is modestly greater than the minimum requirement so that capacity is less likely to fall below the minimum requirement as capacity conditions fluctuate over time); 122 FERC ¶ 61,064 at P 31-34 (2008); *order on reh'g*, 125 FERC ¶ 61,299, at P 36-39 (2008).

the average excess capacity adjustment.<sup>59</sup> It is precisely because the tariff does not specifically define what is meant by an excess capacity level “slightly above” the minimum that NYISO must provide support for whatever level it proposes to use. Since the issues that NYISO does not consider are central to the purpose for which NYISO proposed, and the Commission accepted, the adjustment in the first instance, the Commission cannot find such a proposal to be just and reasonable without support for the underlying assumptions.

62. Using the capacity of the proxy peaking resource to calculate the average excess capacity does not in and of itself satisfy NYISO’s burden of proof. This is because the capacity of the designated peaking resource is simply the measure upon which the November 30, 2010 filing would apply NYISO’s assumption regarding timing of new entry; and therefore, does not provide sufficient support for the proposal in the November filing. The capacity of the designated peaking resource is immaterial if the associated proposal is not supported as just and reasonable. A measure such as the capacity of the designated peaking resource could be reasonable provided that the associated proposal is supported as just and reasonable.

63. Regarding the Commission’s rejection of NYISO’s proposal in the November 30, 2010 filing to adjust its computed 0.6 percent assumed level of excess capacity for NYCA to 1.0 percent NYISO reiterates its original justification that “it is unrealistic to assume that, over time, an average level of excess below 1 percent would be reasonable.” NYISO then repeats that the tariff only requires it to incorporate a level of excess capacity to “equals or slightly exceed” the minimum. This statement is unsupported. NYISO provides no insight into the considerations it took into account in setting this claimed 1 percent minimum or whether it intends this minimum to be applicable to each locality in subsequent resets. Indeed, given the seemingly arbitrary nature of the decision to set a minimum of 1 percent, raises questions regarding the reasonableness of NYISO’s other proposed adjustments for NYC and LI.

64. NYISO and load-side parties assert that the Commission required NYISO to prove that its proposal was superior to what was accepted in previous orders and that the Commission applied an impermissibly stringent burden of proof. We disagree. In the November 30, 2010 filing, NYISO raised the fact that its proposal was lower than it had been in the previous reset proceeding. In proposing its new average excess capacity adjustments in the November 30, 2010 filing, NYISO introduced a new assumption regarding the timing of entry to the adjustments, and further modified the adjustment by using the capacity of a peaking plant. Given such changed positions, NYISO could not

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<sup>59</sup> NYISO November 30, 2010 Filing at 18-19 (stating that “concerns that NYISO’s estimates. . . unreasonably assume that NYISO and investors will have ‘perfect foresight’ are . . . misplaced”).

rely on support from prior proceedings, as the Commission noted. The Commission must determine whether an applicant has sufficiently supported a proposed change in rates. That ruling, therefore, did not require a showing of superiority of its current proposal to the prior-approved excess capacity assumption.

65. Further, contrary to NYISO's assertion, the Commission was also clear regarding the intent of the average excess capacity adjustment to not rely on "observed" levels of average excess capacity. This is consistent with prior orders regarding the ICAP Demand Curves.<sup>60</sup> The average excess capacity adjustment is meant to account for those factors that are present at or slightly above the equilibrium, thus assuring that the resulting rates are just and reasonable. This purpose is irrespective of current conditions. The Commission clarified this purpose in the January 28, 2011 Order.<sup>61</sup>

66. The Commission finds NYISO's arguments regarding evidentiary support in the record for using the previously-approved excess capacity levels to be in error. The Commission has found the existing rates to be just and reasonable. NYISO has the initial burden of showing that its proposed revisions are just and reasonable. Rule 205 of the Commission's Rules of Practice and Procedure<sup>62</sup> states that a person must make a tariff or rate filing in order to change any specific rate, rate schedule or tariff. We reiterate that NYISO may provide additional support for the November 30, 2010 filing or NYISO may propose and support a different figure for the assumed level of average excess capacity.

67. Finally, we turn to the requests for rehearing related to the Commission's statements in Paragraph 122 and 129 of the January 28, 2011 Order. The Commission found in the January 28, 2011 Order that NYISO did not support the use of a different excess capacity adjustment for the first three years as compared to the remainder of the nominal life of the hypothetical peaking unit. NYISO also provided no support for the use of different adjustments over the life of the proxy unit in its request for clarification. We can find no reason for different adjustments, and therefore will require NYISO to use the same excess capacity variable for all 30 years. Additionally, as we found in the January 28, 2011 Order, the assumed level of excess capacity should apply uniformly throughout the analyses used to develop the demand curves. In this regard, we clarify that our acceptance of the energy and ancillary service revenue estimates was intended to be based on the use of a consistent excess capacity assumption as is used in the determination of the other elements of the demand curve. Therefore, we re-affirm our

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<sup>60</sup> See, e.g., *New York Indep. Sys. Operator*, 111 FERC ¶ 61,117, at P 41-48 (2005).

<sup>61</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 115-116.

<sup>62</sup> 18 C.F.R. § 385.205 (2011).

finding in the January 28, 2011 Order that the same excess capacity variable must be used in every instance where this factor is applied, including when determining the capacity risk factor adjustment, energy and ancillary services revenues, System Deliverability Upgrade costs, Transmission Congestion Contract offsets, and the Winter/Summer adjustment.

68. IPPNY also proposes a list of factors and requests that the Commission clarify that NYISO must set the excess capacity variable in accord with these factors. We deny IPPNY's request for clarification. As an initial matter, we note that the factors included in IPPNY's list are not discrete, independent factors. For example, IPPNY lists, *inter alia*, the "lumpiness of capacity additions," the lack of coordination of merchant entry, and the potential for forecasting to be affected by economic slowdowns. In fact the "lumpiness of capacity additions" is not separate and distinct from the latter two factors, but rather, a consequence of them. In any case, NYISO does not indicate that it evaluated these factors, and the Commission finds that, while the factors noted by IPPNY could be appropriate for supporting a reasonable excess capacity adjustment to be used in developing the ICAP Demand Curves, and indeed certain of these have been previously noted by the Commission, the Commission need not establish an explicit, limited list of factors to be accounted for in order for NYISO to reasonably support its proposed excess capacity adjustments and, therefore, will not do so.

#### **D. Estimated Energy and Ancillary Services Revenues**

##### **1. NYISO's Proposal and the Commission Ruling**

69. In the January 28, 2011 Order, the Commission accepted the energy and ancillary services revenue estimates developed by NYISO's Consultant, NERA, including its price estimation models. Energy and ancillary services revenues are derived by simulating the NYISO dispatch models. The dispatch model simulations require estimates of energy prices that NYISO obtains from the Consultant's econometric price model that estimates the relationship between energy prices and the reserve margin. In response to protests regarding the econometrics of the price model estimations by the Consultant, the Commission stated that although the Consultant could have made changes to its estimation methods or data choices that would have produced higher or lower revenue estimates, the Commission concluded that the estimates were objective and reasonable.<sup>63</sup>

70. Specifically, in his affidavit, New York City Suppliers' witness Richard Carlson recommended that the NYISO Consultant re-estimate its pricing model using a longer period of historical data and adding lagged prices as an independent variable to address

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<sup>63</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 136.

certain statistical problems.<sup>64</sup> These changes, according to Dr. Carlson, would result, in absolute value terms, in a smaller estimated relationship between market clearing prices and the reserve margin.<sup>65</sup> Consequently, Dr. Carlson's alternative estimation produces lower estimates for energy prices, and the lower estimated energy prices generate lower estimates of energy and ancillary services revenues when they are used in the dispatch model. Lower estimates for energy and ancillary services revenues translate into higher estimates of net CONE for the proxy unit. In the end, this process would result in a higher ICAP demand curve than that proposed by NYISO.

71. In response, NERA's witness, Jonathan Falk, disagreed that the Consultant's econometric analysis required correction as described by Dr. Carlson. He emphasized that during the stakeholder process, revisions suggested by Dr. Carlson on behalf of the New York City Suppliers were discussed on various occasions and some were incorporated into the Consultant's analysis while others were not.<sup>66</sup> Mr. Falk maintained that the different econometric views held by NERA and Dr. Carlson reflected different professional judgments and that no statistical error demanded the particular corrections recommended by Dr. Carlson. In fact, Mr. Falk argued that the statistical measures recommended by Dr. Carlson resulted in a model that gave results that were simply implausible—that energy profits of an efficient peaking unit were virtually unaffected by excess reserve margins between -5.0 and +17 percent and that this was sufficient reason to reject his recommended econometric changes.<sup>67</sup>

## 2. Request for Rehearing

72. The New York City Suppliers request rehearing of the Commission's acceptance of NYISO's estimate of the net energy and ancillary services revenues earned by the

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<sup>64</sup> The problems addressed concern multicollinearity (whether variables are independent of one another) and "heteroscedasticity" (whether there are error terms that are independent and identically distributed).

<sup>65</sup> The Consultant's estimation indicated that a one percent increase in the reserve margin translated into approximately a one percent decrease in energy prices while the Carlson estimation indicated that the same percent increase in the reserve margin would have a smaller 0.2 percent decrease in energy prices.

<sup>66</sup> NYISO January 6, 2011 Answer, Attachment 4 at P 7. *Also see* New York City Suppliers December 21, 2010 Protest, Attachment B at P 46-68, for detail on the model development through the stakeholder process concluding with the acceptance of some but not all of the suggestions made by Dr. Carlson.

<sup>67</sup> NYISO January 6, 2011 Answer, Attachment 4 at P 9.

proxy unit. The New York City Suppliers continue to maintain that the estimated energy and ancillary services revenues were projected on the basis of a flawed statistical analysis performed by the Consultant.<sup>68</sup> They request that the Commission direct NYISO to recalculate estimated energy and ancillary services revenues using a corrected statistical analysis such as that offered by their witness Carlson. The New York City Suppliers reiterate their previous criticisms and claim that 80 pages of expert testimony and hundreds of pages of supporting work papers required a more serious evaluation of admittedly arcane econometric issues rather than an award of a “gentleman’s C” in accepting NYISO’s estimates. Although they would agree with Mr. Falk that there is room for a difference of opinion on modeling issues, they maintain that issues they raise point to modeling approaches that are clearly wrong. New York City Suppliers state that, more importantly, the Commission’s “tepid” endorsement of the NYISO statistical modeling approach invites flawed future analyses. If the Commission does not require a re-calculation of energy and ancillary services revenues as they request, the New York City Suppliers ask that the Commission emphasize that NYISO will be held to a higher standard of statistical analysis in the future.

### **3. Commission Determination**

73. We deny rehearing on this point. The Commission’s acceptance of the price estimation model developed by the Consultant that is used to estimate energy and ancillary services revenues is not an endorsement of any particular statistical methods, set of historical data, or set of explanatory variables or their measurement. New York City Suppliers continue to emphasize that the NYISO econometric analysis that supports the estimates of energy and ancillary services revenues is not merely a reflection of a different modeling approach but statistical error that is readily fixable. We do not agree and remain convinced that the NYISO models rely on a statistical analysis that yields objective results that are just and reasonable. The Commission firmly supports high standards of statistical analyses. We observe in the current reset process improvements in data and statistical analyses compared to those previously used, and we expect future improvements as NYISO and its consultants gain more experience with this complex exercise.

74. This issue presents the Commission with dueling price models that have different implications for how energy prices might respond to reserve margins. The statistical dispute involves two issues: (1) the relevant historical period over which the estimation should be based; and (2) whether the addition of lagged prices should be added as an explanatory variable.<sup>69</sup> The NERA estimation used data from a three-year period while

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<sup>68</sup> New York City Suppliers February 25, 2011 Request for Rehearing at 2.

<sup>69</sup> The New York City Suppliers advocate a longer historical period because it includes greater variation in prices which may reduce the multicollinearity problem.

(continued...)

the New York City Suppliers argue that the estimation should use a six-year historical period encompassing the years that were previously used to estimate prices. According to previous testimony provided by Dr. Carlson for the New York City Suppliers,<sup>70</sup> estimation over the longer data period alone changes the coefficient for the reserve margin from -1.03 to -0.17. With the addition of the lagged dependent variable over the six year period, the estimated coefficient for the reserve margin declines further to -0.07.<sup>71</sup> If the lagged dependent variable is added without the additional historical data, the coefficient for the reserve margin changes from -1.03 to -0.22. Thus, either or both of the New York City Suppliers' proposed changes yields an estimated coefficient for the reserve margin that indicates little relationship between energy prices and the reserve margin while the NERA estimate is approximately -1.0.

75. The consequence of this difference is graphically illustrated in Figure 16 of Dr. Carlson's Affidavit<sup>72</sup> where the net revenues for a proxy LMS 100 unit at different excess reserve margins are shown based on the two models. In contrast to the NYISO model, the model advocated by the New York City Suppliers indicates that profits are unresponsive to changes in excess reserve margins between -5.0 percent and +17.0 percent, an outcome Mr. Falk rejects as implausible.<sup>73</sup> Although all parties agree that different statistical approaches will yield different outcomes, we agree with Mr. Falk that a conclusion that energy prices do not respond to changes in supply when demand is fixed, as suggested by the model results advocated by the New York City Suppliers, is not reasonable. We therefore deny rehearing on this issue. We see no justification to require NYISO to re-calculate energy and ancillary services revenues based on a statistical model that implies little or no price response. We agree with the New York City Suppliers that greater variation in the dependent variable that may come from using a longer historical period and greater attention to approaches for addressing problems with heteroscedasticity may yield more robust econometric estimations. Nevertheless, we find the choices made by NYISO and its Consultant for this demand curve reset period and the process by which those choices were vetted in the stakeholder process produced results that are just and reasonable.

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They favor the addition of the lagged price variable to address the heteroscedasticity problem.

<sup>70</sup> New York City Suppliers December 21, 2010 Filing, Attachment B at P 31.

<sup>71</sup> *Id.* P 36.

<sup>72</sup> New York City Suppliers December 21, 2010 Filing, Attachment B at 67.

<sup>73</sup> NYISO January 6, 2011 Answer, Attachment 4 at P 9.

## **E. Escalation Factor**

### **1. NYISO's Proposal and the Commission Ruling**

76. NYISO establishes ICAP demand curves for the upcoming three capability periods, 2011/2012, 2012/2013, and 2013/2014. NYISO provides that the demand curves for the latter two years of the period will be adjusted for inflation by applying an escalation factor to the 2011/2012 demand curves. In the past NYISO has used the Handy-Whitman Index, a historical analysis of power plant development costs, to determine a projected escalation factor. In its November 30, 2010 filing, NYISO proposed to use a factor equal to the average of three inflation forecasts for the 2010-2014 period developed by: (1) the Survey of Professional Forecasters; (2) the U.S. Office of Management and Budget; and (3) the U.S. Congressional Budget Office. NYISO stated that the lack, to date, of a strong economic recovery and the uncertainty created by inaction on carbon legislation led it to conclude that historic equipment escalation rates will not be sustainable. Based on this analysis, NYISO proposed a 1.7 percent escalation factor for the second and third years of the reset period.

77. In the January 28, 2011 Order, the Commission accepted NYISO's 1.7 percent escalation factor as a reasonable adjustment to the ICAP demand curves for the 2011/2014 period. The Commission stated that deciding on an escalation factor necessarily entails judgment and the particular industry-specific and general inflation factors that underlie NYISO's proposal are just and reasonable. The Commission stated that, while it was not suggesting that use of the Handy-Whitman Index is inappropriate, in this particular case, we found that NYISO's judgment in relying on alternate sources was reasonable. The Commission stated that historical increases in that index do not necessarily justify forecasting a growth rate equal to the historical growth rate.

### **2. Requests for Rehearing**

78. New York City Suppliers assert that the Commission erred by accepting NYISO's proposal to replace the previously approved Handy-Whitman Index-based escalation rate of 7.8 percent with a 1.7 percent factor derived from general measures of consumer price inflation without any industry-specific adjustment. New York City Suppliers argue that in 2008, the Commission rejected the proposition that the escalation factor should be based solely on a general inflation factor and stated in the 2008 Reset Order that the Commission does not believe that "a general inflation factor, on its own, sufficiently accounts for expected changes in power plant construction costs."<sup>74</sup> They also point to

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<sup>74</sup> NYC Suppliers January 25, 2011 Request for Rehearing at 11 (citing *New York Indep. System Operator, Inc.*, 122 FERC ¶ 61,064 at P 54 (2008 Reset Order), *order on reh'g.*, 125 FERC ¶ 61,299 (2008)).

Commission comments that the Handy-Whitman Index provides “a transparent, reliable and unbiased measure of cost increases,”<sup>75</sup> and that the use of this measure for the escalation rate would “facilitate capacity market stability that will foster the locational construction of new resources and promote conditions conducive to long-term contracts for capacity resources. Further, New York City Suppliers state that, in the 2008 reset proceeding, the Commission accepted NYISO’s proposal to use the Handy-Whitman Index, because the index “is specifically tailored to the [utility] industry, is widely used by the industry and thus is an appropriate data source for NYISO’s purposes,” and because it “accounts for all elements of engineering, procurement, and construction costs.”<sup>76</sup>

79. New York City Suppliers assert that the January 28, 2011 Order does not explain the Commission’s decision to reverse course and approve the use of an escalation rate based solely on general measures of consumer price inflation that do not take into account relevant technology- and location-specific cost differences. New York City Suppliers further contend that the Commission relied only upon a faulty understanding of exactly what NYISO proposed;<sup>77</sup> the Commission did not make any finding that its previous policy was flawed or has led to results that are unjust, unreasonable, or unduly discriminatory; there is nothing in the record to support the finding that a general inflation measure like the consumer price index would provide a reliable or accurate measure of the costs of a new proxy peaking unit constructed in New York<sup>78</sup> and, in contrast, New York City Suppliers and others raised material issues of fact demonstrating that the costs for natural gas-fired turbine peaking units, like the proxy unit, have continued to escalate well in excess of the general inflation rate and are expected to continue to do so for the foreseeable future.

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<sup>75</sup> New York Suppliers February 25, 2011 Request for Rehearing at 11 (citing *PJM Interconnection, L.L.C.*, 129 FERC ¶ 61,090, P 38 (2009)).

<sup>76</sup>*Id.* (citing *New York Indep. Sys. Operator*, 125 FERC ¶ 61,299 at P 35).

<sup>77</sup> New York City Suppliers point to the January 28, 2011 Order’s characterization of NYISO’s proposal as being based on “industry-specific and general inflation factors.” New York City Suppliers February 25, 2011 Filing at 13 (citing January 28, 2011 Order, 134 FERC ¶ 61,058 at P 150).

<sup>78</sup> New York City Suppliers state that neither the NERA Report nor the Meehan affidavit make any recommendation regarding the appropriate escalation rate and that the Commission cannot rely on the affidavit from NYISO witness Ungate because he provides no numerical estimate of projected future cost increases or explanation as to why these costs would or should correspond to increases in consumer prices.

80. The New York City Suppliers argue that the Commission erred in ignoring evidence that clearly demonstrates that NYISO's proposed escalation rate is inadequate and does not reflect the technology- and location-specific cost differences that are relevant to estimating cost increases for constructing a new proxy peaking unit in the NYISO footprint.

81. The New York City Suppliers reiterate arguments made in their initial protest in this proceeding, that the Commission should have required NYISO to produce "substantial evidence" that forecasts of consumer price inflation are reliable or accurate measures of increases in the costs of constructing a new proxy peaking unit in New York. Absent such evidence, the New York City Suppliers argue that the Commission cannot make a determination that NYISO's proposed escalation rate would perform as well or better than the proven and Commission-approved Handy-Whitman Index. According to New York City Suppliers, the Commission's decision is not based on reasoned decision-making and therefore, the Commission should grant its request for rehearing of the January 28, 2011 Order and require NYISO to replace its proposed escalation rate with an escalation rate of 7.8 percent based on the Handy-Whitman Index.

### **3. Commission Determination**

82. We deny rehearing on this issue. The Commission reaffirms its decision to use the 1.7 percent escalation factor as proposed by NYISO as a reasonable adjustment to the ICAP demand curves for the 2011-2014 period. The primary question to be considered here is not what constitutes the best overall method for determining an escalation factor generally; but rather whether the method proposed by NYISO in this instance is just and reasonable. We believe that, in the circumstances of this case, NYISO's use of projection of general inflation rates, as compared to historical Handy-Whitman Index values, is an appropriate measure for adjusting the capacity demand curve.

83. First, we note that contrary to the assertion of the New York City Suppliers, the Commission reviewed Levitan & Associates, Inc.'s testimony, along with all other testimony and evidence submitted in the proceeding, and based its decision to accept NYISO's proposal on that review. For example, NYISO submitted affidavits from Mr. Meehan in which he concludes that a 1.7 percent escalation is reasonably consistent with the long-term assumptions that are reflected in the NERA report.<sup>79</sup> Specifically, Mr. Meehan testified that NYISO employed the Handy-Whitman Index during the 2007 ICAP demand curve reset as the forecast escalation rate, explaining that the time of the 2007 reset both commodity and equipment prices were rising rapidly and it was reasonable to expect continued near term increases in those costs. He further explained

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<sup>79</sup> NYISO January 6, 2011 Answer, Attachment 1, Affidavit of Eugene T. Meehan at 17.

that in 2007, NYISO applied the escalation rate based on a linear trend, given the “fundamental changes in equipment and raw material costs over the last few years.”<sup>80</sup> Moreover, Mr. Meehan noted that, according to Mr. Ungate’s testimony, combustion turbine equipment prices are stable to reach the conclusion, that in this case, a higher escalation factor is not warranted for the near term. Mr. Meehan notes that the 1.7 percent value proposed by NYISO has a minimal effect on the carrying charge and ICAP demand curve. Thus, the Commission was persuaded by the reasoned conclusions that Mr. Meehan made for NYISO’s the escalation factor for capacity years 2011-2014.

84. Mr. Ungate explained in sufficient detail that there is not an upward trend in combustion turbine equipment prices, and that it is reasonable at this time to anticipate stability in combustion turbine equipment prices.<sup>81</sup> Mr. Ungate cited the Gas Turbine World 2010 GTW Handbook for forecasts of lower prices for new gas turbines in 2010 of approximately 9 or 10 percent with expected level prices in 2011 and 2012. He explained that these equipment costs are about 40 percent of the cost of a new peaker with labor costs accounting for the majority of the remaining costs. Thus, he concluded that an inflation rate between 1.5 and 2.0 percent was reasonable and he included data supporting his conclusion. The Meehan and Ungate Affidavits demonstrate that it was reasonable and in no way inconsistent with the NYISO’s position in the prior ICAP demand curve reset for NYISO to use general inflation forecasts to establish the escalation factor for Capacity Years 2011-2014. Thus, the Commission was persuaded by the reasoned explanations Mr. Ungate gave in his expert opinion.

85. Second, we note that our policy has been to accept a proposed escalation factor if we can find that it is within a zone of reasonableness, and is based upon substantial evidence that is essentially a judgment informed by an analysis of cost and inflation trends.<sup>82</sup> However, because market conditions often change over time, the escalation factor can reflect a reasonable judgment as to the rate at which costs are expected to increase going forward, not necessarily the rate at which they increased in the past (since those cost increases are already included in the net CONE estimates for the 2011/2012

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<sup>80</sup> *Id.* at 5-6, (citing 2008 ICAP Demand Curve Reset Filing in Docket No. ER08-283, Attachment 6 at P 6-9).

<sup>81</sup> NYISO January 6, 2011 Answer, Attachment 3, Affidavit of Christopher D. Ungate at P 24-30.

<sup>82</sup> In its 2008 Reset Order, accepting NYISO’s previous ICAP demand curve parameters, the Commission accepted NYISO’s choice of an escalation factor as essentially a judgment informed by an analysis of cost and inflation trends. 2008 Reset Order, 122 FERC ¶ 61,064 at P 54.

capability year).<sup>83</sup> The Commission believes that using a forecast growth rate is advantageous for determining a short-term inflation adjustment because it takes into account the lack of a strong economic recovery, and that historic equipment escalation rates are not sustainable over the next few years.

86. Substantial evidence means “such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.”<sup>84</sup> Consistent with this definition, NYISO has produced substantial evidence in the record, and the Commission has reasonably relied upon that evidence to support its finding, that in light of upcoming economic conditions, the proposed 1.7 percent escalation factor is reasonable and will result in meaningful savings to electricity consumers. NYISO’s inflation adjustment falls within the zone of reasonableness and is supported by substantial evidence.

87. Substantial evidence, in this context, means that NYISO must establish that their proposed escalation rate is: (1) within the zone of reasonableness; and (2) informed by an analysis of cost and inflation trends. Record evidence shows that NYISO has done just that. Therefore, we reject New York City Suppliers’ argument that the Commission lacked substantial evidence to make this determination.

88. Third, we reject the New York City Suppliers claim that the Commission’s decision to accept NYISO’s proposed escalation factor was based on a faulty understanding of what NYISO proposed. They assert that the Commission’s characterization of NYISO’s proposal as being based on “industry-specific” and “general” inflation factors is simply incorrect as NYISO did not include any industry specific measure of inflation in its calculation. We disagree. It is New York City Suppliers that have mischaracterized how NYISO arrived at its proposed escalation factor. As we explained in our discussion herein of NYISO’s basis for developing inflation estimates, the Commission recognizes NYISO’s documented consideration of the Handy-Whitman Index in forming its determination for the annual escalation rate.<sup>85</sup>

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<sup>83</sup> See NYTOs December 21, 2010 Filing, Appendix B, Affidavit of Michael Cadwalader at P 17-18.

<sup>84</sup> *Universal Camera Corp. v. National Labor Relations Bd.*, 340 U.S. 474, 477 (1951) (quoting *Consolidated Edison Co. v. Labor Bd.*, 305 U.S. 197, 229 (1938)). The Court also stated that substantial evidence “must do more than create a suspicion of the existence of the fact to be established. . . it must be enough to justify, if the trial were to a jury, a refusal to direct a verdict when the conclusion sought to be drawn from it is one of fact for the jury.” *Id.* (quoting *Labor Bd. v. Columbian Enameling & Stamping Co.*, 306 U.S. 292, 300 (1939)).

<sup>85</sup> See generally, NYISO January 6, 2011 Answer at 31. See also Meehan Affidavit at P 16; Ungate Affidavit at P 27.

However, as NYISO explained, economic circumstances have materially changed thereby warranting the use of inflation projections based on current and expected circumstances rather than historical circumstances tracked by the Handy-Whitman Index. Further, as supported by the conclusion of Mr. Meehan, if the Commission were to require NYISO to use the Handy-Whitman Index, it would be necessary to adjust the economic carrying charge in a manner that would likely result in lowering the proposed ICAP demand curves, which runs counter to New York City Suppliers' proposal to increase the escalation factor and, therefore, increase the demand curves.

89. Finally, the Commission's determinations with respect to PJM and ISO-NE are not binding here. As NYISO pointed out in its Answer, the Commission has never required that the three system operators adopt identical capacity market structures.<sup>86</sup> Each uses different demand curves that are based on different sets of complex and interrelated assumptions.<sup>87</sup> NYISO's escalation factor is the product of an extensive stakeholder process that focused on the particular characteristics and circumstances of the NYISO's capacity market design and tariff requirements.<sup>88</sup> Accordingly, the New York City Suppliers present no compelling arguments in their request for rehearing that would justify a reversal of the Commission's decision to increase the reset 2010/2011 ICAP demand curve by a 1.7 percent escalation factor in the January 28 Order.

## **F. NYC Interconnection Costs**

### **1. NYISO's Proposal and the Commission's Ruling**

90. In the January 28, 2011 Order, the Commission found merit in IPPNY's concerns with level of interconnection costs used by NYISO in determining CONE for the NYC locality. The Commission agreed that NYISO should use System Deliverability Upgrade costs in the estimate of interconnection costs, if applicable, and further directed NYISO

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<sup>86</sup> See NYISO Answer at 30 *citing Wholesale Competition in Regions with Organized Electric Markets*, Order No. 719, FERC Stats. & Regs. ¶ 31,281, at P 59 (2008), *order on reh'g*, Order No. 719-A, 74 Fed. Reg. 37,776 (Jul. 29, 2009), FERC Stats. & Regs. ¶ 31,292 (2009), *order on reh'g*, Order No. 719-B, 129 FERC ¶ 61,252 (2009) (following the Commission's established policy of allowing different ISOs/RTOs to have market designs that best suit their regional circumstances by declining to develop standardized requirements for demand response resources, instead allowing "each RTO and ISO, in conjunction with its stakeholders, to develop its own minimum requirements").

<sup>87</sup> See *In-City Incumbent Generators*, Levitan Affidavit at P 73.

<sup>88</sup> NYISO January 6, 2011 Answer at 3.

to address in its compliance filing IPPNY's arguments that that the costs of System Deliverability Upgrade Facilities that NYISO used are unrealistic, and to provide support for the estimate it has used.

## 2. Request for Rehearing

91. On rehearing, NYISO states that the Commission should not have required NYISO to reexamine interconnection costs of the NYC peaking unit. Doing so, NYISO states, would require reexamination of costs based on data available after the demand curve reset process had been concluded and on data not yet approved by stakeholders.<sup>89</sup> NYISO asserts that it used the appropriate data available to calculate the interconnection costs, including system upgrade facilities costs, in the NYC's peaking unit's CONE. Additionally, NYISO states that it provided sufficient support for its interconnection costs estimates, which it states were based on historical NYC average System Upgrade Facility costs, that the January 28, 2011 Order did not find unjust and unreasonable.<sup>90</sup> NYISO further states that the more recent project-specific data used by IPPNY shows only that the interconnection costs vary widely by project in NYC and does not support the Commission's conclusion. On this basis, NYISO asks the Commission grant rehearing with respect to the directive to reexamine and provide additional support for its estimates.<sup>91</sup>

92. The NYTOs state that the choice of location of a generation facility is the choice of the developer and that there are locations within NYC that do not require System Deliverability Upgrade costs. As such, the NYTOs state that to the extent a generator incurs deliverability costs in NYC it is because it made the choice to forgo the location without deliverability costs and therefore, there is no basis for the Commission to have rejected NYISO's proposal on the level of interconnection costs in NYC.<sup>92</sup> NYTOs state that the Commission failed to address the issues raised in its determination. In reiterating the arguments of the NYTOs, the City of New York and Consumer Protection Board state that the Commission erred in remanding this issue to NYISO for further consideration.

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<sup>89</sup> Citing *New York Indep. Sys. Operator*, 122 FERC ¶ 61,283, at P 37-38 (2005).

<sup>90</sup> NYISO February 28, 2011 Request for Rehearing at 38.

<sup>91</sup> NYISO February 28, 2011 Request for Rehearing at 39, citing *KeySpan-Ravenswood v. FERC*, 348 F.3d 1053, 1056 (D.C. Cir. 2003).

<sup>92</sup> NYTOs February 28, 2010 Request for Rehearing at 10 (referring to the South Pier and Berrains III projects that incurred System Deliverability Upgrade costs due to their choice of location).

### 3. Commission Determination

93. We deny rehearing on the issue of interconnection costs used in developing the NYC demand curve. With respect to System Deliverability Upgrade costs, the Commission directed that they be included in the calculation of the demand curve, if applicable.<sup>93</sup> As such, the Commission stated that the cost of System Deliverability Upgrades are to be determined and applied, *to the extent they are present*, in the calculation of CONE for each of the capacity zones—NYCA, NYC, and LI.<sup>94</sup> As reaffirmed earlier in this order on rehearing, it was not error to direct NYISO to revise its demand curves to include System Deliverability Upgrade costs, *if applicable*, for each zone. The Commission will review NYISO's compliance response to determine what, if any, change is required in the NYC demand curves.

94. Regarding System Upgrade Facility cost issues raised by IPPNY, the Commission directed NYISO, on compliance to address IPPNY's arguments regarding the level of interconnection costs used in developing the NYC CONE and to provide support for the estimates it used.<sup>95</sup> Given that the historical precedents NYISO used to develop the System Upgrade Facility cost estimates were from 2001 and escalated to 2010, the Commission wants to ensure that the numbers remain realistic.<sup>96</sup> The Commission did not direct NYISO to modify its estimate for System Upgrade Facility costs in NYC, but only to address the issues raised by IPPNY that the estimate of interconnection costs for NYC are unrealistic. We continue to believe that it is necessary for NYISO to show that its estimates of System Upgrade Facility costs are reasonable. Therefore we deny rehearing.

#### G. Winter/Summer Adjustment

##### 1. NYISO's Proposal and the Commission's Ruling

95. As the January 28, 2011 Order noted, a greater amount of capacity is normally available in the winter than in the summer, and as a result, winter prices are typically lower than summer prices. To ensure that average annual revenue over time is adequate, the Services Tariff requires: "the periodic review shall assess...the appropriate translation of the annual net revenue requirement of the peaking unit...into monthly

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<sup>93</sup> January 28, 2011 Order, 134 FERC ¶ 61,058 at P 140.

<sup>94</sup> *Id.* P 53, 140.

<sup>95</sup> *Id.* P 140.

<sup>96</sup> *See* NYISO January 6, 2011 Answer, Attachment 3 (Ungate Affidavit) at P 19.

values that take into account seasonal differences in the amount of capacity available in the ICAP Spot Market Auctions.<sup>97</sup> Accordingly, in its original filing in this docket, NYISO proposed a winter/summer adjustment that provided an upward adjustment to the demand curves as it has in previous demand curve reset filings. The proposed adjustment was based on NYISO's estimate of the additional capacity *available* in the winter compared to the summer, and the resulting effect on winter versus summer revenue. The NYTOs proposed an alternative adjustment, based on an estimate of the additional capacity that would be *sold* into the markets in the winter compared to the summer.

96. The January 28 2011 Order accepted NYISO's proposed winter/summer adjustment as just and reasonable and consistent with the requirements of the Services Tariff with respect to the issue of quantities of capacity *available* versus quantities *sold*. However, to be consistent with other aspects of the demand curve reset analysis, the Commission directed NYISO to revise the winter/summer adjustment to reflect the assumption for the level of excess capacity that the Commission required be included in the revised demand curves to be filed in NYISO's subsequent compliance filing.<sup>98</sup>

## 2. Request for Rehearing

97. NYISO seeks clarification regarding the directive of the January 28, 2011 Order that NYISO revise the winter/summer adjustment to reflect the level of excess capacity given that the Commission accepted NYISO's proposed adjustment. According to NYISO, excess capacity levels were not a factor in its calculation of its proposed winter/summer adjustment, because the amount of available capacity is determined using historical levels obtained from NYISO's annual Load and Capacity Reports. NYISO requests that the Commission clarify that the January 28, 2011 Order only requires that NYISO apply its accepted winter/summer adjustment methodology when establishing revised ICAP Demand Curves. If the Commission did intend for NYISO to revise its winter/summer adjustment methodology, NYISO requests that the Commission more clearly explain what it expects NYISO to do, so that NYISO may fulfill its compliance obligations. In the alternative, NYISO requests rehearing that the Commission did not explain its directive to include the excess capacity given that the winter/summer adjustment is based on the amount of available capacity and is not properly calculated using a level of excess capacity.

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<sup>97</sup> Services Tariff, section 5.14.1.2.

<sup>98</sup> January 28 Order, 134 FERC ¶ 61,058 at P 161.

### 3. Commission Determination

98. We deny NYISO's requested clarification and request for rehearing, but will clarify what it is expected to do to comply with the January 28, 2011 order with respect to this issue. The NYISO ICAP Manual describes the formulas used to calculate the monthly ICAP Reference Point price for a given location so as to reflect the winter/summer adjustment.<sup>99</sup> The monthly ICAP Reference Point price is the price on the demand curve at the Minimum Installed Capacity Requirement. While the Commission accepted, in the January 28, 2011 Order, the methodology as reflected in the formula for making the winter/summer adjustment, it did not accept the numerical values to the extent they rely on a level of excess capacity. While NYISO states that the level of excess capacity is not a factor in the winter/summer adjustment, as discussed below, we are not convinced by NYISO's explanation that it should not be considered.

99. The formula for the monthly ICAP Reference Point price includes the term, WSR, which is the ratio of (i) the sum of the winter Dependable Maximum Net Capabilities (DMNCs) of all ICAP providers, to (ii) the sum of the summer DMNCs of all ICAP providers. As the value for WSR increases, the calculated value for the monthly ICAP Reference Point price increases, thereby increasing the height of the demand curve. NYISO's November 30, 2010 Filing used a value for WSR based on the most recent ratio of actual winter-to-summer DMNCs as reported in the most recent annual Load and Capacity Data posted on its web site.<sup>100</sup> However, to be consistent with other aspects of the demand curve reset analysis, the numerator and denominator, respectively, of WSR should reflect assumptions about the level of excess capacity in the winter and summer that are consistent with (though not necessarily identical to) the average level of excess capacity used to calculate the other components of net CONE. Such consistency would ensure that all elements of the demand curve model use consistent assumptions of what excess capacity levels will be for all elements that reflect capacity conditions, such as estimates of energy, ancillary service and capacity revenues used in determining net CONE, and for the starting point for determining what additional capacity would be available in the winter compared to the summer.

100. Accordingly, we direct NYISO to include, in its compliance filing, values for WSRs in the relevant locations that are consistent with the assumed average levels of excess capacity used to calculate the other components of net CONE, or to explain why the values for WSR calculated based on recent actual data reasonably approximate the

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<sup>99</sup> See section 5.5 of NYISO ICAP Manual 4.

<sup>100</sup> NYISO November 30, 2010 Filing, Attachment 3, *Proposed NYISO Installed Capacity Demand Curves for Capability Years 2011/2012, 2012/2013, and 2013/2014* Rev. 10/30/2010, Appendix A.

ratio of winter-to-summer DMNCs that would arise under the assumed average level of excess capacity.

### **III. Request for Rehearing of the March 9, 2011 Order (Docket No. ER11-2224-006)**

101. In the March 9, 2011 Order, the Commission denied requests for clarifications and rehearing of the January 28, 2011 Order regarding the suspension of the proposed demand curve rates. The Commission rejected NYISO's request to clarify that the rates in effect during the suspension period were intended to reflect the 1.7 percent escalation factor of its November 30, 2010 filing. The Commission stated that the currently effective demand curves (i.e., 2010/2011 capability year) remain in effect without escalation until the earlier of June 28, 2011 or a date set by subsequent Commission order. However, the Commission reiterated the ruling in the January 28, 2011 Order that NYISO may wish to defer implementation of the revised compliance demand curves if it does not wish to implement them during the summer Capability Period. In the January 28, 2011 Order, the Commission stated that any such deferral should not extend beyond November 1, 2011, the start of the winter capability period.

102. On April 8, 2011, Ravenswood filed a request for rehearing of the March 9, 2011 Order. Ravenswood asks that the Commission first clarify that if the Commission does not issue an order on NYISO's March 29, 2011 compliance filing<sup>101</sup> to the January 28, 2011 Order prior to the end of the suspension period (June 28, 2011), then the rates in effect will be superseded by the rates proposed in NYISO's November 30, 2010 filing until replaced by rates required by the January 28, 2011 Order. Ravenswood states that the rates in effect during the suspension period cannot remain in effect beyond June 28, 2011, and that the rates filed by NYISO in the November 30, 2010 Filing will go into effect on June 28, 2011 as a matter of law if the Commission does not act on the March 29, 2011 compliance filing by June 28, 2011.

103. Second, Ravenswood seeks rehearing of the Commission's statement that NYISO may choose to defer the effective date of the proposed 2011/2012 NYC demand curve rate beyond the five month suspension period.<sup>102</sup> It also seeks rehearing of the Commission's determination that the 2010/2011 demand curve rate is to remain in effect during the suspension period without escalation and argues, rather, that it should be escalated by the 7.8 percent escalation rate approved from the prior demand curve reset.

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<sup>101</sup> See Docket Nos. ER11-2224-004 and ER11-2224-005 (collectively, March 29, 2011 Compliance Filing).

<sup>102</sup> Citing March 9, 2011 Order, 134 FERC ¶ 61,178 at P 18.

### Commission Determination

104. Ravenswood's request for clarification was effectively rendered moot by the Commission's April 4, 2011 Order. In the April 4, 2011 Order, in light of the fact that the Services tariff specifically limits the existing demand curve rates to the period ending April 30, 2011, the Commission accepted NYISO-proposed revisions to the Services Tariff to establish that the existing demand curve rates applicable to the 2010/2011 Capability Year will be effective May 1, 2011, until a date set by Commission Order. Thus, by this action, the November 30, 2010 filing's proposed rates were superseded and the suspension of those originally-filed rates for the period set by the January 28, 2011 Order was rendered moot. Further, with the original proposed demand curve rates having been superseded by rates effective May 1, 2011, coupled with NYISO's discretion to defer implementation of the compliance rates (which are to be further revised as a result of today's rulings) beyond June 28, 2011, action on compliance can occur at any time without conflict with section 205 suspension authority. Therefore, Ravenswood's claim that there is uncertainty over which demand curve rate will be in effect is without merit as the rates are clearly stated in the Services Tariff and will not be revised without further action by the Commission.

105. Second, we find that Ravenswood's request for rehearing of the statement in the March 9, 2011 Order, that NYISO may defer implementation of the revised compliance rates until the winter Capability Period and, therefore, beyond June 28, 2011, to be a collateral attack on the January 28, 2011 Order which first rendered that pronouncement. Ravenswood is not seeking rehearing of a determination made by the Commission in the March 9, 2011 Order. Rather, in its request for rehearing of the March 9, 2011 Order, it is seeking to change a determination made in the January 28, 2011 Order regarding the implementation of the revised set of demand curves and the rate that is to be in effect beginning May 1, 2011. Ravenswood did not seek rehearing of the ruling in the January 28, 2011 Order and may not do so later under the guise of seeking rehearing of the March 9, 2011 Order. In any event, because the existing rates remain in effect beyond May 1, 2011, and therefore must remain in effect beyond what is now the irrelevant date of June 28, 2011, until superseded by revised rates that comply with the Commission's directives (including new directives by today's order), the Commission was not acting to extend the suspension period of the original filed rates. The Commission may authorize the filing entity to defer implementation of compliance rates that must reflect Commission directives and, indeed, has done so recently in other NYISO proceedings in order to prevent hardship.<sup>103</sup>

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<sup>103</sup> See, e.g., *New York Indep. Sys. Operator, Inc.*, 134 FERC ¶ 61,186 (2011); *New York Indep. Sys. Operator, Inc.*, 135 FERC ¶ 61,072 (2011).

106. Finally, we find that, for the same reasons we rejected NYISO's proposal to implement rates during the original suspension period that reflect its proposed 1.7 percent escalation factor, Ravenswood's proposal to implement a different escalation factor, 7.8 percent, during the same period is without merit, and accordingly we reject it.

The Commission orders:

(A) The requests for clarification and rehearing in Docket No. ER11-2224-001 are granted in part and otherwise denied, as discussed in the body of this order.

(B) The requests for clarification and rehearing in Docket No. ER11-2224-006 are hereby denied, as discussed in the body of this order.

(C) NYISO is directed to file revised tariff records and supporting documentation as directed in the body of this order, within 30 days of the date of this order

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.