

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeem G. Kelly.

New York Independent System Operator, Inc.

Docket No. ER03-836-001

ORDER ON REHEARING

(Issued May 7, 2004)

1. This order addresses the request for rehearing filed by the New York Independent System Operator, Inc. (NYISO) of the Commission's order issued in this proceeding on July 1, 2003 (July 1 Order).¹ At issue is whether NYISO must, as directed in the July 1 Order, submit a timetable for implementing a self-supply option for operating reserves,² given NYISO's argument that its Real-Time Software (RTS) will provide an equivalent mechanism for self-supply. As discussed below, we will deny NYISO's request for rehearing.

2. This order will benefit customers by assuring that they may self-supply operating reserves, even if they choose not to submit a bid in the Day-Ahead market.

I. July 1 Order

3. In the July 1 Order, the Commission accepted for filing revisions to NYISO's Market Administration and Control Services Tariff (Services Tariff). More specifically, the Commission found sufficient improvement in competitive conditions in the 10-Minute Non-Synchronized Reserves (NSR) market to warrant substantially removing a then-existing bid cap. As described in the July 1 Order, the bid cap would be replaced by the mitigation tools used in other NYISO markets.

¹ New York Independent System Operator, Inc., 104 FERC ¶ 61,002 (2003).

² This option will be referred to alternatively as "self-supply option" or "self-supply."

4. Nevertheless, the Commission expressed concern about the lack of a self-supply option in the tariff revisions.³ Noting that we had previously directed NYISO to develop a self-supply option, we emphasized that customers must be allowed to self-supply their own operating reserves, in order to decrease the likelihood that they will be held captive to the NSR supplier's market power.⁴ However, we further acknowledged that NYISO must modify its software to allow self-supply and that NYISO was in the process of completely redeveloping its RTS.⁵ Accordingly, instead of requiring NYISO to immediately implement self-supply, we directed it to submit, within 60 days of the date of July 1 Order, a timetable for full implementation of a self-supply option.⁶

II. NYISO's Rehearing Request

5. On rehearing, NYISO argues that, once in effect, its RTS will include a self-supply option that satisfies the July 1 Order and that no further self-supply mechanism is necessary. NYISO explains that the RTS will institute multi-settlement ancillary services markets, including Day-Ahead and Real-Time reserves markets, which eliminate limitations on the ability of market participants to fully satisfy their reserve obligations through self-supply. NYISO further explains that, following implementation of the multi-settlement system, a load serving entity (LSE) will be able to fully cover its reserves obligation by self-scheduling operating reserves in the Day-Ahead Market. A market participant that wants to ensure its generation will provide operating reserves can offer the reserves into the Day-Ahead Market at a very low or negative availability bid. According to NYISO, this ability to self-schedule a unit to provide operating reserves in the Day-Ahead Market will ensure that a market participant with sufficient qualified reserves can self-supply, in order to satisfy its reserve obligation.

6. In short, NYISO contends that the RTS will enable market participants to fully satisfy their operating reserve obligations with the operation of their own generation resources (either owned or under contract). NYISO states that the self-supply of operating reserves would be financial only in the sense that market participants would financially settle any imbalance between the reserves supplied and their required share. NYISO maintains that if a market participant has generation, or rights to generation in a specific location, it will be able to self-supply operating reserves under the RTS (by

³ Id. at P 17.

⁴ Id. (citing New York Independent System Operator, Inc., 91 FERC ¶ 61,218, 61,799-800 (2000)).

⁵ Id.

⁶ Id.

bidding into NYISO's market at appropriately low levels) just as effectively as it could under any alternative self-supply mechanism.

7. NYISO argues that, together, the RTS operating reserves markets and NYISO's mitigation measures will provide protection against NSR market power. NYISO further states that the July 1 Order recognized that competitive conditions have improved in NYISO's ancillary services market. NYISO argues that continuing concerns about NSR market power are properly addressed through NYISO's mitigation measures.

8. Finally, NYISO argues that, in any case, self-supply is not needed as a "competitive check" within NYISO's RTS framework.⁷ NYISO states that it has no financial interest in the sale of operating reserves and that, because it is under close scrutiny of a market monitor, it has every incentive to administer its system efficiently.

III. Discussion

9. The Commission will deny NYISO's rehearing request. In requiring a self-supply option, we intend for a participant to be able to satisfy its NSR obligation by making available a qualified resource. A participant would not need to offer that resource for sale in NYISO's NSR auction, and therefore, would not have to offer a supply bid. By contrast, NYISO's version of self-supply under the RTS would involve a two-step process. In the first step, a participant would be required to pay its share of NYISO's cost of procuring NSR in its NSR auction. In the second step, which NYISO contends would achieve the financial equivalent of self-supply, a participant would have to sell its capacity into the NSR auction and use the resulting revenues to offset its share of NSR purchase costs. In other words, the participant would have to submit a supply bid. While NYISO argues that the participant could ensure that its resource is accepted in the NYISO auction by offering a very low bid price in the auction, NYISO's proposal would be financially equivalent to self-supply only if: (1) the participant successfully estimated the price bid necessary for its resource to be accepted in the NSR auction; and (2) the participant's revenues from the sale of NSR in the auction matched its share of the NSR purchase costs. These conditions might often, but might not always, be met. Accordingly, participants might not always achieve the financial equivalent to self-supply.

10. Our chief concern in directing NYISO to adopt a self-supply option for operating reserves is the potential lack of competitive alternatives for NSR. It was this concern that caused us to authorize a bid cap (which the July 1 Order substantially removed) and must-offer requirement for resources east of the Central-East constraint. Competitive developments in the NSR market, comprehensive mitigation measures, and the

⁷ NYISO's Request for Rehearing at 17.

redesigned markets (that co-optimize energy and reserves, establish location-specific reserves requirements and demand for reserves) may diminish the value of self-supplying. However, we remain committed to the principle, especially since the bid cap in NYISO's Services Tariff has been substantially removed, that a market participant should have the option of self-supplying without bidding, when it believes that it can self-provide at a lower cost than NYISO. NYISO must provide customers with the option of self-supplying their own operating reserves within a reasonable time period, although we will not require that implementation of NYISO's RTS be delayed in order to implement self-supply of NSR. We will require the NYISO to submit, within 60 days of the date of this order, a timetable setting forth a schedule for full implementation of a method for allowing customers to self-supply their own operating reserves.

11. Moreover, any such self-supply will not harm other NYISO customers. Rather, it will displace the most costly resources that would otherwise be procured by NYISO, and thus, it will reduce the NSR costs borne by other customers. We believe that market participants should be able to self-supply a particular qualified resource to provide a given level of operating reserves in the Day-Ahead market, as long as they bear the costs of that decision. NYISO believes that such an option, in light of limited transmission, is unlikely to be economically attractive. Perhaps so, but the decision should be that of the participant.

12. Based upon the foregoing, we will deny NYISO's rehearing request.

The Commission orders:

(A) NYISO's rehearing request is hereby denied.

(B) NYISO is hereby directed to submit, within 60 days of the date of this order, a timetable setting forth a schedule for full implementation of a method for allowing customers to self-supply their own operating reserves.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.