

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

New England Power Pool and
ISO New England, Inc.

Docket No. ER02-2330-029

ORDER ON COMPLIANCE FILING

(Issued December 21, 2004)

1. On July 1, 2004, the New England Power Pool Participants Committee (NEPOOL) and ISO New England Inc. (ISO-NE) (collectively, the Filing Parties), submitted a filing in response to the Commission's order issued in this proceeding on January 28, 2004.¹ The Filing Parties' compliance filing consists of a study completed by ISO-NE regarding two alternatives to full nodal pricing for load (Pricing Study). The two alternatives analyzed in the Pricing Study are: (i) a reconfiguration of ISO-NE's existing load zones; and (ii) the implementation of nodal pricing on a voluntary "special case" (SCNP) basis. Based on the findings set forth in the Pricing Study, the Filing Parties seek approval, in principle, of their proposed SCNP approach, which they state they will submit for Commission approval in the form of proposed tariff revisions, on a date consistent with ISO-NE's implementation of its new ancillary services markets in 2005. For the reasons discussed below, we will accept the Filing Parties' compliance filing, subject to conditions.

I. Background

2. In their initial filing instituting this proceeding, on July 15, 2002, the Filing Parties proposed to implement a standard market design for the New England wholesale markets. Included in the Filing Parties' proposed market design was a congestion management

¹ New England Power Pool and ISO New England, Inc., 106 FERC ¶ 61, 059 (2004) (January 28 Order).

system based on Locational Marginal Pricing (LMP). We accepted the Filing Parties' filing, in part, subject to conditions.²

3. Under the LMP methodology approved in the NE-SMD Order, ISO-NE establishes prices for generators on a nodal basis but relies on zonal pricing for loads, due to the existing infeasibility of implementing nodal pricing.³ In the NE-SMD Order, we found that the Filing Parties' proposed nodal/zonal approach to pricing represented a reasonable initial approach to congestion pricing over an interim period, subject to the implementation of full nodal pricing within the 18 month phase-in period proposed by the Filing Parties.⁴ On rehearing, we further modified this timetable by directing the Filing Parties to offer nodal pricing to load customers to the extent it was feasible to do so.⁵

4. On October 30, 2003, the Filing Parties, joined by the New England Conference of Public Utility Commissioners (NECPUC) (collectively, the Joint Movants), requested that our policy in favor of full nodal pricing for load be reconsidered. In support of their request, the Joint Movants asserted that there were better and less costly alternatives to full nodal pricing. The Joint Movants argued, among other things, that full nodal pricing, if implemented, would adversely affect the efficiency of ISO-NE's markets by increasing price volatility and reducing market liquidity. In lieu of this approach, the Joint Movants stated that they were committed, as were NEPOOL's stakeholders, to exploring alternatives to full nodal pricing and were prepared to do so in the form of a comprehensive study and analysis. The Joint Movants further proposed that the Filing Parties be permitted to make a filing no later than July 2004 reflecting the results of their study.

5. In the January 28 Order, we stated that we would not remove our nodal pricing requirement, as of that date, prior to the completion of the study proposed by the Joint Movants. However, we also stated that if the Filing Parties can demonstrate, in their study, that other pricing methods can achieve the same or a comparable level of

² See New England Power Pool and ISO New England, Inc., 100 FERC ¶ 61,287 (NE-SMD Order), *order on reh'g*, 101 FERC ¶ 61,344 (2002) (NE-SMD Rehearing Order).

³ In their initial filing in this proceeding, the Filing Parties asserted that it would not be feasible to implement nodal pricing for loads without improved metering and reporting capabilities. The Filing Parties estimated that it would take approximately 18 months to re-map customer loads to specific nodes.

⁴ See NE-SMD Order at P 72.

⁵ See NE-SMD Rehearing Order at P 86.

transparency that would be expected from the implementation of full nodal pricing, while providing other benefits (*e.g.*, lower costs, enhanced liquidity, and regulatory consistency *vis a vis* state pricing policies), we would consider such an approach acceptable.

II. The Pricing Study and the Filing Parties' Requested Authorizations

6. As noted above, the Pricing Study examines two alternative pricing options: (i) the reconfiguration of ISO-NE's load zones and (ii) SCNP. With respect to the first of these two options, the Pricing Study examined an alternative set of zones for the New England region, based on the thirteen regional boundaries currently utilized by ISO-NE in its Regional Transmission Expansion Plan (RTEP). Specifically, the Pricing Study examined whether these alternative RTEP zones, if relied upon for pricing, would demonstrate statistically different price levels and patterns for energy. The Pricing Study finds that the annual average nodal prices, by region, fell within \$1.25/MWh of the hub price, with only two exceptions applicable to a portion of the Connecticut Zone (covering the Norwalk/Stamford region) and the southern portion of the Maine Zone. The Pricing Study also finds that price differences over the course of the one-year period studied were, on average, less than \$1.51/MWh. In addition, the Pricing Study evaluates the impact of Reliability Must Run (RMR) resources and Special Constraint Resources (SCR) on LMP.

7. Based upon these analyses, the Pricing Study determines that ISO-NE's existing eight load zones are adequate for pricing energy.⁶ While the Pricing Study identifies nominal price differences, for example, it finds that these differences were slight enough to support the conclusion that splitting off the appropriate regions in Connecticut and Maine is not warranted at this time. The Pricing Study also notes that a reconfiguration of these current load zones would require several changes that could have an adverse impact on bilateral arrangements, financial transmission rights (FTR) positions, and/or current state pricing policies. The Pricing Study concludes that addressing these issues would impose additional costs and would take between nine to twelve months to implement.

8. While rejecting the establishment of new zones, at this time, the Pricing Study does recommend that analysis of alternative load zones be considered on a regular basis (it recommends every two years) or when changes to system conditions occur (*e.g.*, to

⁶ We note that in an order issued subsequent to the Filing Parties' filing, herein, we accepted ISO-NE's proposal to create a separate Installed Capacity (ICAP) region and a corresponding energy load zone for Southwest Connecticut (SWCT Zone), in Docket No. ER03-563-000, *et al.* (Devon Power Proceeding). See Devon Power LLC, *et al.*, 109 FERC ¶ 61,156 (2004).

account for load growth, transmission system changes, additional generation in constrained areas, the introduction of new markets, etc.).

9. The Pricing Study determines that by contrast to the reconfiguration of ISO-NE's existing zones, implementing SCNP would: (i) promote price transparency; (ii) encourage efficient price responsive demand; (iii) enhance system reliability; and (iv) better integrate demand response directly into ISO-NE's market design. The Pricing Study concludes that, relative to full nodal pricing, SCNP has lower implementation costs, reduces liquidity problems, and creates fewer conflicts with existing state pricing policies and bilateral contracts.

10. The Pricing Study also addresses SCNP eligibility issues. Specifically, the Pricing Study finds that in order to be eligible to participate in SCNP, an individual end-use metered customer should be at least 5 MW in size, connected to a single node, and be in compliance with certain technical and administrative criteria.⁷ The Pricing Study further recommends that all participants in SCNP be required to satisfy metering and telemetering requirements at their own expense and recommends that once in the program, customers not be allowed to switch back to zonal pricing for at least twelve months.

11. The Pricing Study finds that under SNCP, participants should be allowed to select either a non-dispatchable or dispatchable option. A participant that chooses the dispatchable option would be considered an ICAP resource available for dispatch by ISO-NE and eligible for ICAP credit. The Pricing Study finds that this dispatchable option would increase the amount of price-sensitive demand as well as aid system operators in maintaining reliability. The Pricing Study further finds that non-dispatchable loads will increase price-sensitive demand in New England, as they are able to self-dispatch in response to price variation.

12. Based on the findings set forth in the Pricing Study, the Filing Parties recommend that New England adopt SCNP for load as an alternative to full nodal pricing. The Filing Parties also request that the Commission reconsider and remove its requirements to implement full nodal pricing for load. Finally, the Filing Parties request an order authorizing the Filing Parties to begin work on the specific market rules and procedures

⁷ ISO-NE defines an end-use customer as a firm or individual that purchases products for its own consumption and not for resale (*i.e.*, an ultimate consumer). SCNP would not allow the aggregation of retail customers to reach the 5 MW minimum level. Though participants stated that they would like to have the option for such aggregation, it was determined that for an interim period aggregation will not be allowed. ISO-NE states that it is committed to revisiting this requirement in the future.

necessary to implement SCNP consistent with the timetable associated with ISO-NE's implementation of its new ancillary services markets in 2005.⁸

13. In support of their filing, the Filing Parties assert that their proposal to remove the requirement that the region implement full nodal pricing for load has received broad stakeholder within NEPOOL, *i.e.*, a 96 percent vote of approval.

III. Notice of Filing and Responsive Pleadings

14. Notice of the Filing Parties' filing was published in the *Federal Register*,⁹ with interventions and protests due on or before July 21, 2004. Motions to intervene were timely filed by the Connecticut Department of Public Utility Control (Connecticut DPUC) and the NEPOOL Industrial Customer Coalition (NICC). A protest was filed by the Connecticut DPUC. Comments were filed by NICC. On August 5, 2004, the Filing Parties submitted an answer to the protest and comments submitted by NICC and the Connecticut DPUC.

IV. Discussion

A. Procedural Matters

15. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,¹⁰ the notices of intervention and timely, unopposed motions to intervene noted above serve to make the entities that filed these requests parties to this proceeding. Rule 213(a) of the Commission's Rules of Practice and Procedure¹¹ prohibits an answer to a protest, unless otherwise permitted by the decisional authority. We will accept the answer filed by the Filing Parties, given the complex nature of the issues raised in this proceeding and because this answer has aided the Commission in clarifying certain issues, as discussed below.

⁸ As identified in the Pricing Study, the required rule changes would include revisions to NEPOOL's market rules (Market Rule 1) and manuals (including M-11, which addresses market operations, M-20, which addresses ICAP, and M-36, which addresses forward reserves markets). In addition, ISO-NE would be required to implement metering and software changes, provide training for participants, and make certain revisions to its settlement procedures.

⁹ 69 Fed. Reg. 43,257 (2004).

¹⁰ 18 C.F.R. § 385.214 (2004).

¹¹ *Id.* at § 385.213(a)(2).

B. Analysis

16. For the reasons discussed below, we will accept the Filing Parties' filing and the Pricing Study, included therein, subject to conditions. Specifically, we will approve, in principle, the use of SCNP in New England under the timetable discussed below. As such, we will rescind the requirement set forth in the NE-SMD Order that the Filing Parties implement full nodal pricing for load.

1. The SCNP Option

17. While the implementation of full nodal pricing for load is and should remain an important objective for ISOs and RTOs, where appropriate, we agree with the Filing Parties that SCNP, as outlined in the Pricing Study, represents an acceptable alternative under the facts and circumstances at play in the New England wholesale markets. Among other things, SCNP will provide price signals at specific nodes and thus represent a significant improvement in relation to ISO-NE's existing zonal prices. SCNP nodal prices will also reflect the actual marginal bid cost of delivering energy to a specific node. In contrast to ISO-NE's current zonal pricing approach, SCNP will send more accurate and transparent price signals to SCNP participants, which in turn will encourage more price responsive demand among SCNP participants.

18. We also agree that SCNP may have certain cost advantages in relation to full nodal pricing. Specifically, while the transition from a zonal pricing structure to a full nodal pricing structure would involve certain transactions costs borne by all participants (*e.g.*, costs associated with the installation of the necessary meters and software upgrades), SCNP will require participating loads alone, *i.e.*, the loads benefiting from nodal-based settlement, to pay these transaction costs. As proposed by the Filing Parties, moreover, SCNP will also be a voluntary program that will allow customers with loads above 5 MWs to decide for themselves whether the benefits of nodal pricing exceed the costs.

2. The Zonal Reconfiguration Option and Full Nodal Pricing

19. We agree with the Filing Parties that SCNP is a preferable pricing alternative to either zonal reconfiguration or full nodal pricing. We also agree that ISO-NE's existing eight load zones (and the ninth zone recently approved in the Devon Power Proceeding)¹² are adequate, at this time, for pricing energy. We also agree that the reconfiguration of these current load zones into 13 zones (*i.e.*, the boundaries which currently comprise

¹² Devon Power LLC, *et al.*, 107 FERC ¶ 61,240, *order on reh'g*, 109 FERC ¶ 61,154 (2004).

ISO-NE's RTEP regions) would impose additional costs and burdens on participants that have not been justified.

20. NICC argues that the zonal reconfiguration options addressed by the Pricing Study should be resolved by the Commission not in this proceeding, but in the Devon Power Proceeding, in conjunction with the resolution of ISO-NE's locational installed capacity proposal. However, our findings here are consistent with our rulings in the Devon Power Proceeding and thus need not be deferred.

3. Other Alternatives to SCNP

21. The Connecticut DPUC asserts that the Pricing Study is deficient because it does not contain a comprehensive study regarding the alternatives to full nodal pricing and SCNP. The Connecticut DPUC argues that the Pricing Study neither provides data regarding the price differentials between nodes nor presents evidence that nodal price signals would have a meaningful effect on generation or transmission siting. Moreover, the Connecticut DPUC asserts that the Pricing Study fails to consider the costs and benefits of SCNP. The Connecticut DPUC asserts that while it does not support splitting Connecticut into two zones, as approved by the Commission in the Devon Power Proceeding, the establishment of these zones could, in fact, accomplish most of what is intended by nodal pricing.

22. We find that the Pricing Study provides an appropriate analysis of alternatives to SCNP and full nodal pricing for load. We also find that SCNP offers a pricing scheme that, for participating parties, provides a level of transparency similar to that provided by full nodal pricing for load; at the same time, SCNP does not burden non-participants with the transactions costs associated with full nodal pricing.¹³

4. Benefits and Costs Attributable to SCNP

23. The Connecticut DPUC argues that smaller customers will exert pressure to participate in SCNP and that increased participation will drive prices up for other

¹³ In their October 30, 2003 filing, in Docket No. ER02-2330-019, the Joint Movants asserted that implementation costs for full nodal pricing for load would be at least \$30 million. *See supra* P 4.

customers and discourage retail competition.¹⁴ The Connecticut DPUC also argues that participants in the ISO-NE load response program may migrate to SNCP, undermining reliability in Connecticut, particularly in the Southwest Connecticut region. The Connecticut DPUC notes that the Pricing Study provides no discussion or analysis of the effect of SCNP on load response program participation and argues that the Commission should require that this information be included in a subsequent study prior to any approval of SCNP.

24. The Connecticut DPUC also asserts that as customers at lower cost nodes switch to nodal pricing, costs to non-participants will be driven up. The Connecticut DPUC argues that standard offer suppliers will face a greater risk of losing customers and will reflect this in their bids to supply standard offer service, thus increasing the cost of standard offer service. The Connecticut DPUC asserts that regulators will have to decide whether to reflect the wholesale nodal cost in retail rates or keep rates the same over the entire zone. The Connecticut DPUC asserts that if retail rates do not match nodal costs, the price signals nodal pricing are intended to provide will be hidden from customers. The Connecticut DPUC also argues that nodal pricing could drive up administrative costs and retail rates for non-participants. Finally, the Connecticut DPUC argues that SCNP, if adopted, should be mandatory, not optional, for all customers above 5MW.

25. With respect to the issue of aggregation, we agree with the Filing Parties. The concerns expressed by Connecticut DPUC are premature; concerns regarding specific future aggregation proposals are best addressed when they are proposed. With regard to the migration of loads from the load response programs to SCNP, we also agree that SCNP can reasonably be expected to provide greater price transparency to participants and thus provide appropriate levels of load response. Nodal prices paid under SCNP will more accurately signal the actual costs of delivering energy to SCNP customers at their nodes.

26. Currently, load response programs in New England rely on zonal prices, which are calculated as the load-weighted average of the locational marginal prices at the nodes that comprise the load zone. SCNP will allow participants to see real time prices for the individual nodes where they actually take energy, rather than as a weighted average price over the entire zone. As a result, SCNP should allow participants to make appropriate and node-specific decisions regarding their consumption. Thus, though parties may

¹⁴ The proposal, as filed, does not allow customers smaller than 5 MW and does not allow the aggregation of retail customers to reach the 5 MW minimum level. ISO-NE and NEPOOL state that during discussions related to the SCNP proposal some participants stated that they would like to have the option for such aggregation in the future. In response, ISO-NE committed to revisiting this requirement in the future, after experience with SCNP is gained.

remove themselves from New England's load response programs, they do so in order to participate in SCNP, which provides greater price transparency and thus increased opportunity to tailor their consumption based on more accurate price signals.

27. With regard to the Connecticut DPUC's concerns over standard offer service, the Pricing Study states that as customers at lower cost nodes migrate to nodal settlement, those loads would be excluded from the calculation of the zonal LMP, resulting in increased weighted average zonal prices. However, the Pricing Study estimates that the price increases will be small – about \$0.0001/kWh. Standard offer service rates are determined via a competitive bidding process and thus any expected impact from the implementation of SCNP will be reflected in standard offer bids. However, as the expected impact on non-participants is expected to be nominal, the impact on standard offer service bids or retail rates, in turn, should not be burdensome.

28. Finally, in response to the Connecticut DPUC's concern that SCNP will discourage retail competition, we agree with the Filing Parties that SCNP will help to increase retail competition. Participation in SCNP by retail customers in Connecticut can occur only through a competitive retail supplier. As such, SCNP will encourage, not discourage, competitive retail activity.

5. SCNP Implementation Timetable

29. NICC argues that the Filing Parties' SCNP proposal fails to provide a timeframe for its implementation and urges the Commission establish a reasonable target date. The Filing Parties respond in their answer that the Commission should allow the region flexibility to determine the most reasonable, feasible timeframe for SCNP implementation. The Filing Parties note, in this regard, that ISO-NE's Independent Market Advisor has advised that before SCNP can be implemented, the implementation of ISO-NE's new ancillary services markets should be completed, sometime between June and October 2005.

30. We agree with the Filing Parties that a specific target date for the implementation of SCNP should not be established at this time. We also agree that the implementation of SCNP should generally track the implementation of ISO-NE's new ancillary services markets within the timeframe outlined by the Filing Parties in their answer. However, we also recognize the legitimate concerns raised by NICC. Accordingly, we will require the Filing Parties to make a compliance filing on or before June 30, 2005 addressing its plans and its proposed timetable for implementing SCNP.

The Commission orders:

(A) We will accept the Filing Parties' compliance filing, subject to conditions, as discussed in the body of this order.

(B) The Filing Parties are hereby directed to make a compliance filing on or before June 30, 2005, as discussed in the body of this order.

By the Commission. Commissioner Kelly not participating.

(S E A L)

Magalie R. Salas,
Secretary.