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March 23, 2007

**VIA ELECTRONIC FILING**

The Honorable Philis Posey  
Acting Secretary  
Federal Energy Regulatory Commission  
Room 1A-East, First Floor  
888 First Street, N.E.  
Washington, D.C. 20426

Re: ISO New England Inc., Docket No. ER07-546-000

Dear Ms. Posey:

Attached for electronic filing in the above-referenced docket is the *Motion for Leave to Answer and Answer of ISO New England Inc.* A copy of the foregoing has been served upon all parties included in the Commission's service list.

If you have any questions or concerns regarding this filing, please feel free to contact me. Thank you for your assistance in this matter.

Respectfully submitted,

/s/ Sherry A. Quirk  
Sherry A. Quirk, Esq.  
Robin E. Remis, Esq.

Counsel for ISO New England Inc.

Attachment  
cc: Official Service List

**UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION**

ISO New England Inc.

)

Docket No. ER07-546-000

**MOTION FOR LEAVE TO ANSWER  
AND ANSWER OF ISO NEW ENGLAND INC.**

Pursuant to Rules 212, 213, and 101(e) of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (“Commission” or “FERC”),<sup>1</sup> ISO New England Inc. (the “ISO”) hereby submits its *Motion for Leave to Answer and Answer* to various pleadings filed in the above-captioned proceeding in response to the ISO’s February 15, 2007 filing (“February 15 Filing”) in which the ISO proposed various tariff provisions to implement the Forward Capacity Market (“FCM”) Settlement Agreement (“FCM Settlement”)<sup>2</sup> approved by the Commission.<sup>3</sup>

**I. BACKGROUND AND INTRODUCTION**

Pursuant to the FCM Settlement, the ISO was required to submit a filing pursuant to Section 205 of the Federal Power Act (“FPA”)<sup>4</sup> on or before February 15, 2007.<sup>5</sup> This schedule was intended to enable the ISO to conduct the first Forward Capacity Auction (“FCA”) in early 2008 as contemplated by the FCM Settlement. The package of proposed market rules and accompanying documents to implement the FCM Settlement was approved by the New England

<sup>1</sup> See 18 C.F.R. §§ 385.212, 385.213, and 385.101(e) (2006).

<sup>2</sup> Explanatory Statement of the Settling Parties in Support of Settlement Agreement and Request for Expedited Consideration, Docket Nos. ER03-563-000 *et al.* (March 6, 2006)(“FCM Settlement”).

<sup>3</sup> *Devon Power LLC*, 115 FERC ¶ 61,340 (June 16, 2006).

<sup>4</sup> 16 U.S.C. § 824d (2000).

<sup>5</sup> FCM Settlement at Section 3.A.

Power Pool (“NEPOOL”) Participants Committee by a vote of 78.74%. Altogether, the filing package exceeded 950 pages.

In response, 44 interventions have been filed, of which 31 include a protest or comments,<sup>6</sup> and 13 make no comment. Given the magnitude of the filing and the complexity of the subjects addressed in it, the vote on the rules and the relatively few protested issues demonstrate a remarkable degree of support among NEPOOL and the states, in favor of the ISO’s proposed implementation of the market design set forth in the FCM Settlement and approved by the Commission.

As noted in the February 15 Filing, pursuant to the terms of the FCM Settlement, the FCM market rules were filed by the ISO under FPA Section 205 to implement the FCM as

<sup>6</sup> Those filings under Docket No. ER07-546-000 include: Motion to Intervene and Preliminary Limited Protest of International Power America, Inc and ANP Northeast Development LLC (“ANP Pleading”) and Supplement to Preliminary Limited Protest of International Power America, Inc. and ANP Northeast Development, LLC (“ANP Supplemental Pleading”); Motion to Intervene and Protest of Brookfield Energy Marketing Inc. (“Brookfield Energy Pleading”); Motion to Intervene and Limited Protest of Capacity Suppliers (“Capacity Suppliers Pleading”); Comments of Cape Light Compact (“Cape Light Pleading”); Motion to Intervene of Comverge Inc. (“Comverge Pleading”); Motion to Intervene of Connecticut Office of Consumer Counsel (“Consumer Counsel Pleading”); Motion to Intervene of Conservation Law Foundation (“CLF Pleading”); Motion to Intervene, Comments and Protest of Conservation Services Group Inc. (“CSG Pleading”); Notice of Intervention, Protest, and Comments of the Connecticut Department of Public Utility Control (“CT DPUC Pleading”); Protest of Comverge, Inc., *et al.* (“DR Coalition Pleading”); Motion to Intervene and Comments of Dominion Resources Services, Inc. (“Dominion Pleading”); Motion to Intervene and Comment of Enernoc, Inc. (“Enernoc Pleading”); Motion to Intervene of Exelon Corporation (“Exelon Pleading”); Motion to Intervene and Protest of FirstLight Parties (“FirstLight Pleading”); Motion to Intervene and limited Protest of H.Q. Energy Services (U.S.) Inc. (“HQUS Pleading”); Motion to Intervene of IRH Management Committee (“IRH Pleading”); Motion to Intervene and Limited Protest of Long Island Power Authority (“LIPA Pleading”); Notice of Intervention and Protest of the Maine Public Utilities Commission (“MPUC Pleading”); Notice of Intervention, Protest, and Comments of Massachusetts Department of Telecommunications and Energy (“Mass DTE Pleading”); Motion to Intervene and Protest of Milford Power Company, LLC (“Milford Pleading”); Motion to Intervene, Protest and Comments of Massachusetts Municipal Wholesale Electric Company and Connecticut Municipal Electric Energy Cooperative (“Public Systems Pleading”); Motion to Intervene and Comments of National Grid USA (“National Grid Pleading”); Motion to Intervene, Protest and Comments of New England Conference of Public Utilities Commissioners (“NECPUC Pleading”); New Hampshire Public Utilities Commission Intervention and Joinder in Protest and Comment (“NH PUC Pleading”); Motion to Intervene and Comments of NEPOOL Participants Committee (“NEPOOL Pleading”); Motion to Intervene and Comments of Northeast Utilities Service Company on Behalf of the NU Companies (“NUSCO Pleading”); Motion to Intervene and Protest of NRG Companies (“NRG Pleading”); Intervention and Protest of NSTAR Electric & Gas Corporation (“NSTAR Pleading”); Motion to Intervene of PPL EnergyPlus, LLC, PPL, Maine, LLC, PPL, Great Works, LLC, and PPL Wallingford Energy LLC (“PPL Parties Pleading”); Intervention and Protest of the PSEG Power Companies (“PSEG Pleading”); and Motion to Intervene and Protest of Vermont Department of Public Service and Vermont Public Service Board (“Vermont Parties Pleading”).

described in Section 11, Parts I through VII and IX of the FCM Settlement.<sup>7</sup> The Commission's inquiry in this proceeding is limited to whether the proposed FCM market rules are just and reasonable under Section 205 and consistent with Section 3.B of the FCM Settlement.

Among the comments and protests, there were twelve general issues raised. Eight of these issues are ripe for review, and the ISO urges the Commission to deny these protests. Four of these issues are not ripe for the Commission's consideration, or are being or should be addressed in a separate proceeding. Clarification of four issues has been sought, and in several instances the ISO would request that the Commission grant the requested clarification.

Among the issues raised in the protests that are ripe for consideration, first, several generators have protested various aspects of the rules related to treatment of de-list bids. However, these provisions are critical for the proper functioning of the FCM because they are intended to, and will, effectively address market power. It is well established that capacity markets are vulnerable to the exercise of market power.<sup>8</sup> The changes sought by generators could undermine the integrity of the market by increasing its vulnerability to the exercise of market power by existing generators. These rules faithfully implementing the relevant provisions of the FCM Settlement that were agreed to by the Settling Parties and approved by the Commission, and the ISO urges the Commission to reject these protests.

Second, International Power America, Inc and ANP Northeast Development LLC ("ANP") allege that the entire Show of Interest ("SOI") process is inconsistent with the FCM Settlement and must be rejected. As thoroughly explained in the February 15 Filing, the SOI and

<sup>7</sup> FCM Settlement at Section 3.A.

<sup>8</sup> See *The New Power Company v. PJM Interconnection, Inc.*, 98 FERC ¶ 61,208 at 61,752 (2002) ("allegations of market power problems have plagued the capacity markets within PJM."). See also Working Paper on Standardized Transmission Service and Wholesale Electric Market Design, at 2, Docket No. RM01-12-000 (March 15, 2002) (The Commission, in identifying prevailing market design flaws noted that in some regions "high fees are being collected for the value of generation capacity that do not clearly incent the construction of new capacity.").

review process is a critical element of the market design, and its implementation is well within the discretion the ISO must have to effect the critical provisions of the FCM Settlement. Similarly, the proposed qualification deposit is a reasonable provision in that it requires those who seek to participate in the FCM to bear the cost of processing their application, thereby weeding out speculative or ill conceived projects that are not likely to advance. Thus, the challenges to these provisions should be rejected. However, ANP's challenge highlights an issue in the February 15 Filing that would benefit from clarification: ANP has complained that requiring Project Sponsors to file Show of Interest Forms prior to the filing of the FCM market rules is unlawful. As made clear in the February 15 Filing, the ISO received and accepted Show of Interest Forms after January 2, up until February 15. The ISO now clarifies that it intends to review all New Capacity Show of Interest Forms where both the Show of Interest and the deposit were received by February 20, 2007.

Third, various parties have raised concerns with the ISO's treatment of the Phase I/II HVDC. The Interconnection Rights Holders ("IRHs") and H.Q. Energy Services (U.S.), Inc. ("HQUS") have disputed the ISO's proposed treatment in the FCM market rules, which requires 24/7 transmission reservations over the Phase I/II HVDC to back capacity imports over that tie. The ISO's objectives in drafting rules that address this issue were to assure that the interface capacity benefits not be double-counted, to avoid reliability concerns, and that entities receiving credit for the capacity value are clearly identified; so that proper accounting can occur. The proposed market rules accomplish these objectives, are consistent with the FCM Settlement, and under Section 205 should be adopted.

Fourth, Demand Response proponents have requested that the market rules be modified to allow summer-only Demand Resources to participate in the FCM on a seasonal basis rather

than on an annual basis. The Settling Parties knowingly designed the FCM as an annual market. Allowing Demand Resources to provide capacity in only the summer months would run counter to the design of the FCM, undermining the core of the market structure agreed to by the parties to the FCM Settlement. Moreover, the proposed rules facilitate participation of such seasonal resources in the FCA by providing for a composite offer<sup>9</sup> of separate resources and also enable such resources to participate in seasonal or monthly reconfiguration auctions. Thus, the proposed market rules are consistent with the annual nature of the FCM design while accommodating the unique characteristics of demand resources. As the market develops, the ISO will review this issue to assure that Demand Resources are fully able to participate.

Fifth, Massachusetts Municipal Wholesale Electric Company (“MMWEC”) and Connecticut Municipal Electric Energy Cooperative (“CMEEC”) (collectively, “Public Systems”) have alleged that the qualification process is a “one size fits all” process that should be modified for certain types of projects. The ISO believes that compliance with the proposed process is not onerous; however, the ISO will review this issue in the future and revisit the market rules if necessary.

Sixth, FirstLight Power Resources Management LLC, FirstLight Hydro Generating Company and Mt. Tom Generating Company LLC (“FirstLight Parties”) allege that the ISO has erroneously excluded pumped storage hydro facilities from the definition of Demand Resources. This argument is far-fetched. The ISO stands by its definition, and does not believe that turning

<sup>9</sup> Composite offers may be created in which resources with summer capability (e.g., air conditioning reduction) may join with resources with available winter capacity (e.g., combined cycle units) to create a composite offer for the entire year. Advocates for Demand Response have argued that such offers will be difficult to negotiate and they will be at a disadvantage. However, these offers represent opportunities for both sides and should be able to be negotiated to the satisfaction of both parties and may result in beneficial partnerships. February 15 Filing at 52-53.

off the pumps of a pumped storage unit during off peak hours remotely qualifies as demand response.

Seventh, the generators and states have requested certain additional reporting requirements. For example, Capacity Suppliers<sup>10</sup> argue that the ISO should increase the transparency of its use of its authority to reject offers or bids for reliability reasons, and argues that it should be required to report certain information concerning such rejections.<sup>11</sup> New England Conference of Public Utilities Commissioners (“NECPUC”) also supports complete transparency in all reliability determinations.<sup>12</sup> However, as explained further below, the ISO’s rules already provide the information that is being requested.

Finally, Brookfield Energy Marketing Inc. (“Brookfield Energy”) argues that the prohibition on capacity exports by Intermittent Power Resources is a new limitation on such resources not contemplated by the FCM Settlement.<sup>13</sup> They state further that the prohibition runs against FERC’s preference to allow de-listing and exports to prevent seams issues, and that the restriction on capacity exports unfairly targets Intermittent Power Resources by placing them at a competitive disadvantage to other resources that are free to sell their capacity to the highest bidder.<sup>14</sup> However, the limitation on exports is needed because intermittent resources cannot meet the requirements necessary to back export contracts..

<sup>10</sup> Boston Generating, LLC (“Boston Generating”), FPL Energy, LLC (“FPLE”), and the Mirant Parties (collectively, “Capacity Suppliers”).

<sup>11</sup> Capacity Suppliers Pleading at 18. *See also* CT DPUC at 34.

<sup>12</sup> NECPUC Comments at 26. *See also* CT DPUC Comments at 34; Capacity Suppliers Pleading at 18.

<sup>13</sup> Brookfield Energy Pleading at 4.

<sup>14</sup> *Id.* at 6.

Among those issues that should properly be deferred, the state parties<sup>15</sup> have strongly opposed Section III.13.2.5.2.5(f) of the proposed market rules, which requires the ISO to conduct a stakeholder process and then submit a filing on the issue of whether de-list bids rejected for reliability should be considered Out-of-Market Capacity for purposes of determining whether to invoke the Alternative Capacity Price Rule.<sup>16</sup> The proposal to expand the application of the Alternative Capacity Price Rule to such de-list bids was offered late in the stakeholder process and while it appeared to the ISO to have promise, there was insufficient time to fully evaluate it. For this reason, the ISO supported a provision in the rules requiring a stakeholder process and a filing by June 30, 2007, and the stakeholders unanimously agreed. However, the state parties maintain that this proposal –and even considering it in a stakeholder process -- is contrary to the FCM Settlement and this provision should be rejected. The ISO disagrees because the question of whether the proposal to be examined is consistent with the FCM Settlement and should be adopted has not been fully vetted by the ISO and the stakeholders and, thus, is not yet before the Commission. Until it is, the merits of the proposal itself are not ripe for Commission review.

The state parties further maintain that the ISO has erred in its February 15 Filing by failing to commit to make a filing by a date certain to replace priority in the queue as the method for resolving overlapping interconnection impacts. The ISO re-affirms its commitment in the February 15 Filing to work with NEPOOL and the states to develop a prioritization of projects, and agrees to accelerate the date for filing a plan with the Commission if the prioritization

<sup>15</sup> See Connecticut Department of Public Utility Control (“CT DPUC”); Massachusetts Department of Telecommunications and Energy (“Mass DTE”); New England Conference of Public Utilities Commissioners (“NECPUC”); Vermont Department of Public Service and Vermont Public Service Board (“Vermont Parties”).

<sup>16</sup> The Alternative Capacity Price Rule is applied when the amount of Out-of-Market Capacity in the entire system or a particular zone is greater than the amount of new capacity required. If this occurs, the Alternative Capacity Price Rule sets the clearing price at the lesser of the cost of new entry (“CONE”) or the price at which the last new capacity offer left the auction. The purpose of the Alternative Capacity Price Rule is to ensure that the Capacity Clearing Price reflects CONE when new entry was prevented because of the presence of Out-of-Market Capacity. February 15 Filing at 108.

process with all stakeholders can be accelerated. The states submit that addressing the queue is required by the FCM Settlement and the ISO is in violation thereof for failing to address this issue in a “reasonable time,” which the states deem to be prior to the second auction. However, what is reasonable depends on the facts and circumstances surrounding the agreement of the parties, and under well settled law, the application of the principle of good faith. In this instance, those facts and circumstances include that the ISO’s inability to complete review by the date sought by the states is unlikely to impact the clearing price in the auction, as discussed more fully in the body of the answer. The ISO believes the time frame set forth in the February 15 Filing is a good faith execution of the intent of the FCM Settlement.

Long Island Power Authority (“LIPA”) has filed a Limited Protest, and has largely repeated arguments made and recently addressed by the Commission in ruling in a separate proceeding on another ISO filing related to Installed Capacity Requirements (“ICR”).<sup>17</sup> In summary, LIPA has argued that the FCM Settlement requires the ISO to establish a method for LIPA to “buy through” congestion in Connecticut to transmit capacity from its Bear Swamp unit in Massachusetts to LIPA over the Cross Sound Cable. In this ruling, the Commission found some merit in LIPA’s arguments and ordered the ISO to make a compliance filing by August 27, 2007. Given that the Commission has already set forth, in the ICR filing, a route for LIPA’s issues to be addressed in the ICR Filing, it is appropriate for the Commission to deny the protest in this case.

Several parties have offered views on the process, form and pricing that should be established for reliability agreements. In the February 15 Filing, the ISO specifically reserved this issue for stakeholder review and a future filing, and no action or guidance is necessary by the

<sup>17</sup> *ISO New England, Inc., et al.*, 118 FERC ¶ 61,157 (2007) (“ICR Order”).

Commission at this time. With respect to these issues, the ISO urges the Commission to stay its hand pending further action.

The ISO requests that the Commission grant clarification of several points. The ISO concurs with the Connecticut Department of Public Utility Control (“CT DPUC”) and the NECPUC on the clarification offered of intra-round bidding in the FCA. Second, Exelon Corporation (“Exelon”) has asserted that the Commission should rule that a unit may retire after submitting an offer. The ISO agrees that a unit may retire after the submission of a de-list bid but prior to taking on an obligation in the FCA, subject to certain timing requirements. The rules so provide, and the ISO confirms. One party also sought clarification concerning treatment of the 1385 Cable, which the ISO clarifies below. Additionally, an issue has been raised about CTR-related benefits that are not allocated on the basis of PPU Entitlements or through other special arrangements and self-supplied resources. The ISO clarifies that such CTRs are allocated to an LSE on the basis of its load serving obligation, and cannot be used to meet a local sourcing requirement.

## **II. MOTION FOR LEAVE TO ANSWER**

In this *Answer*, the ISO responds to the arguments raised in the respective comments and protests filed by various entities. While the Commission’s Rules of Practice and Procedure permit the filing of answers in response to comments,<sup>18</sup> as a general matter, the Commission’s rules prohibit the filing of answers in response to protests.<sup>19</sup> The Commission has the authority, however, to waive this prohibition for good cause.<sup>20</sup> The Commission has found good cause to permit answers to protests, including in situations where the answer would assure a complete

<sup>18</sup> See 18 C.F.R. § 385.213(a)(3) (2006).

<sup>19</sup> See 18 C.F.R. § 385.213(a)(2) (2006).

<sup>20</sup> See 18 C.F.R. § 385.101(e) (2006).

record in the proceeding,<sup>21</sup> provide information helpful to the disposition of an issue,<sup>22</sup> permit the issues to be narrowed or clarified,<sup>23</sup> or aid the Commission in understanding and resolving issues.<sup>24</sup> The ISO believes that this *Answer* will clarify the issues, assure a more complete record in this proceeding, and otherwise assist the Commission in understanding and resolving the issues raised in response to the February 15 Filing. For these reasons, pursuant to Rule 212, the ISO respectfully requests that the Commission grant the ISO's *Motion* to provide the following *Answer*.

### **III. ANSWER**

#### **A. Arguments to be Addressed on the Merits**

##### **1. The Provisions of the Proposed Market Rules Pertaining to Qualification of De-list Bids and Participation in the Forward Capacity Market are Consistent with the FCM Settlement and are Just and Reasonable.**

NRG and Milford allege that the proposed rules are inconsistent with the FCM Settlement and will interfere with the right of existing generators to submit de-list bids that reflect their actual costs, thereby limiting supply and artificially depressing clearing prices. Capacity Suppliers claim that the proposed rules could force generators to offer to sell capacity at levels below their costs and, accordingly, will undermine the FCM. All of these arguments should be rejected. The proposed rules regarding qualification and participation of de-list bids in the FCM are consistent with the FCM Settlement, represent sound market design principles

<sup>21</sup> See, e.g., *Pacific Interstate Transmission Co.*, 85 FERC ¶ 61,378 at 62,444 (1998), *reh'g denied*, 89 FERC ¶ 61,246 (1999).

<sup>22</sup> See, e.g., *CNG Transmission Corp.*, 89 FERC ¶ 61,100 at 61,287 n.11 (1999).

<sup>23</sup> See, e.g., *PJM Interconnection, L.L.C.*, 84 FERC ¶ 61,224 at 62,078 (1998); *New Energy Ventures, Inc. v. Southern California Edison Co.*, 82 FERC ¶ 61,335 at 62,323 n.1 (1998).

<sup>24</sup> See, e.g., *Tennessee Gas Pipeline Co.*, 92 FERC ¶ 61,009 at 61,016 (2000).

necessary to prevent the exercise of market power in the FCM, and, accordingly are just and reasonable.

The de-list bid process in the market rules is fundamental to the success and competitive nature of the FCM. At present, there are about 33,000 MWs of existing capacity receiving capacity credit. The incremental need for capacity to meet ICR each year is likely to be between 500 to 1000 megawatts of capacity per year. If the de-list rules were not in place, it is evident that a generating company with a large portfolio would have a strong incentive to withhold a relatively small amount of existing capacity to force the purchase of additional new capacity to increase the price in the FCM. For example, if existing generators are able to de-list as little as 200 megawatts of capacity, the need for new capacity would increase by at least 20 percent. When viewed from this perspective, the importance of controlling de-listing to prevent economic withholding from increasing the price becomes clear. For the reasons set forth below, the arguments raised in the protests related to the qualification of de-list bids and participation thereof in the FCM should be rejected.

**a. The Proposed Market Rules Comply with the Requirements of the FCM Settlement and Appropriately Mandate that De-list Bids be Binding.**

The FCM Settlement provides that “Existing Capacity wishing to opt out of the capacity market in the Commitment Period may submit a De-list Bid.”<sup>25</sup> To provide transparency to the capacity market, the FCM Settlement requires that de-list bids and certain associated information be published immediately after the submittal deadline, approximately 10 months in advance of the auction. The general rule is that every de-list bid that is accepted for participation in the FCA

<sup>25</sup> FCM Settlement at Section 11.III.D.5.

is binding. Once accepted for participation, such bids may not be withdrawn or modified and will be entered into the auction at the submitted price, absent rejection by the INTMMU.<sup>26</sup>

NRG and Milford take issue with the binding nature of de-list bids on various grounds. They dispute, *inter alia*, the final and binding nature of de-list bids so far in advance of the auction as well as throughout the auction.<sup>27</sup> They argue that generators should be allowed “to reduce their de-list bids after the qualification deadline in order to allow them to reflect changes in their costs, particularly infra-marginal revenues.”<sup>28</sup>

Similarly, Capacity Suppliers argue that generators be permitted to modify de-list bids rejected by the market monitor so that they reflect only those “components accepted by the INTMMU (if it exceeds 0.8 times CONE) and identified in the informational filing. . .”<sup>29</sup> In addition, they argue that:

It is almost certain that ISO-NE and the market participant will disagree on a material issue of fact if a bid is rejected. It is therefore unlikely that the Commission, on the basis of an informational filing and an intervening protest by the market participant, will have a sufficient record to resolve the issue prior to the FCA.<sup>30</sup>

As explained herein, the proposed market rules are consistent with the FCM Settlement and the arguments raised with regard to the binding nature of de-lists bids should be rejected.

<sup>26</sup> It should be noted that there is a limited exception to the general rule that all of the posted information is final, *i.e.*, it is possible that a posted de-list bid may be rejected by the ISO because the unit is needed for reliability. However, this is an exception, not the norm. Those relying on posted de-list bid information will understand that a few bids might be rejected, but otherwise these are the de-list bids that are going into the auction. Furthermore, the clause in the FCM Settlement that “if approved, full information will be posted” should not be interpreted to mean that the initial submittal is not firm on price. The review process extends well beyond the deadline for new capacity, and therefore such an interpretation would also make meaningless this information as a market signal.

<sup>27</sup> NRG Pleading at 6; Milford Pleading at 5.

<sup>28</sup> NRG Pleading at 7. *See also* Milford Pleading at 5-8.

<sup>29</sup> Capacity Suppliers Pleading at 13-14. *See also* NRG Pleading at 15-17.

<sup>30</sup> *Id.* at 9.

The express terms of the FCM Settlement require that “the quantity, price and zone of each De-list Bid above 0.8 times CONE will also be posted one day after the bid qualification deadline; if the bid is approved by the Market Monitor, full information will be posted.”<sup>31</sup> Moreover, the FCM Settlement provides that “the bid qualification deadline for New Capacity and Imports shall be approximately six weeks after the ISO’s posting of De-list Bids, Permanent De-list Bids and Export Bids from Existing Capacity...”<sup>32</sup> While recognizing the posting requirement, NRG and Milford argue that the FCM Settlement “contains absolutely no reference to when bids must become binding,”<sup>33</sup> ignoring the fact that if the bids posted were not binding, the posting requirement would be meaningless. The posting of information associated with de-list bids is intended to serve as a meaningful market signal to potential new capacity and provides an indication of how much capacity and at what price generators might exit the market. Such information would be rendered meaningless if it could be subsequently modified or if bids could be withdrawn after acceptance. If de-list bids were not binding there would be a risk to new capacity of being effectively undercut by subsequently reduced high de-list bids, making it easier for existing generators to reduce competition by lowering prices until competitors are driven out the market.

In addition, permitting a resource to modify a previously submitted de-list bid undermines the integrity of the de-list process by creating an incentive for a resource to overestimate the components of the bid because a bid would never be rejected on the basis of contentious items, errors or inflated estimates: it would simply be corrected and submitted by the ISO.

<sup>31</sup> FCM Settlement at Section 11.III.D.2.

<sup>32</sup> FCM Settlement at Section 11.II.A.

<sup>33</sup> NRG Pleading at 9. *See also* Milford Pleading at 7-8.

NRG and Milford argue that conditions might change after the Existing Capacity Qualification Deadline and therefore generators should be allowed to modify de-list bids to reflect updated cost and revenue information.<sup>34</sup> According to NRG and Milford, permitting such bid modification would “lead to a more efficient market outcome by allowing a seller to stay in the market longer by accepting a lower price for its megawatts as the clock auction declines.”<sup>35</sup> Moreover, they argue that updating bids will not permit the exercise of market power because the INTMMU will have reviewed the initial bid and any lower bid should also pass muster.

These arguments also run afoul of the requirement laid out above that de-list bids be binding. Additionally, if making a more accurate bid is truly the concern of NRG and Milford, they have not explained why updating bids would, in all cases, result in decreases in bids and fail to address the possibility that increases in bids could result. Under the approach proposed by NRG and Milford, a generator could withdraw its de-list bid entirely and participate in the auction as if it had never submitted a de-list bid clearly contradicting the purpose of submitting and posting bids included in the settlement. The FCM Settlement does not authorize such conduct. And, while NRG and Milford argue that future expectations may change between bid submittal and the FCA, and the lag warrants an allowance for revision, this argument is revealed as a red herring when the three year period between the FCA and the Capacity Commitment Period is taken into account.

NRG and Milford argue that “[m]itigation of a non-conforming de-list bid to the level of a price taker is inconsistent with the basic premise of the FCM rules that existing generators must submit de-list bids which reflect actual costs.”<sup>36</sup> They argue that to the extent a submitted de-list

<sup>34</sup> NRG Pleading at 6-10; Milford Pleading at 5-8.

<sup>35</sup> NRG Pleading at 7; Milford Pleading at 6.

<sup>36</sup> NRG Pleading at 11. *See also* Milford Pleading at 9.

bid is not accepted, the generator should be permitted to submit an acceptable bid based upon what the INTMMU has determined to be an acceptable bid. Moreover, they claim that under such an approach, generators would have “absolutely no incentive to submit inflated bids knowing full well that any bid which is inconsistent with a benchmark of going forward and opportunity costs will be rejected.”<sup>37</sup> In support of this position, Capacity Suppliers claim that such mitigation is appropriate and would be analogous to that used in the energy market.

The FCM Settlement does not provide for such price mitigation. Instead it states that the INTMMU “shall review that the proposed bid is consistent with the Resource’s net risk-adjusted going forward and opportunity costs, recognizing, among other things, infra-marginal rents, availability adjustments, and PER deductions.”<sup>38</sup> The FCM Settlement does not provide, as some generators contend, that should a bid be found to be inconsistent with the resource’s going forward costs, the INTMMU shall determine and submit, on behalf of the generator, a bid that is consistent with the resource’s going forward costs. If the parties wished the INTMMU to calculate going forward costs for each unit, such a requirement would have been included in the FCM Settlement.

Finally, the claim that generators would have no incentive to inflate bids knowing that such bids would be rejected if found to be inconsistent with a “benchmark” of costs implies that the INTMMU will have a “benchmark.” This assumption is false; each de-list bid is analyzed on a case by case basis taking into account the substantiation of a specific resource’s actual costs.

**b. The Market Rule Provisions Permitting Existing Units to De-list on the Basis of Ambient Air Temperatures are Just and Reasonable and Should not be Modified.**

<sup>37</sup> NRG Pleading at 13; Milford Pleading at 11. *See also* PSEG Pleading at 11.

<sup>38</sup> FCM Settlement Section 11.III.E.

The proposed market rules permit Existing Generating Capacity Resources to partially de-list their units at 2.0 times CONE to account for possible reductions in output during hot weather due to the physical characteristics of the unit. This provision was included in response to a concern raised by some generators that certain resources, especially combined cycle units, of which there are about 10,000 MW in New England, cannot generate to their 90 degree ratings at higher temperatures. Accordingly, these generators expressed a desire to have an option to only enter the megawatts they believe that they can provide with reasonable certainty in peak conditions.

In their protests, NRG and Milford argue that the market rules should be modified to allow de-list bids for temperature de-rates to be entered into the FCA at less than 2.0 times CONE.<sup>39</sup> They claim that requiring a generator to bid at a uniform price prevents it from reflecting its actual costs in the de-list bid. This claim must be rejected.

The rule at issue enables generators to de-list all or a portion of the possible decrease in output between 90 and 100 degrees Fahrenheit by providing evidence to the ISO during qualification, such as a temperature/output curve, documenting the physical decrease in output. This procedure was included in the rule to provide generators the ability to de-list capacity that would not be physically available. It was deliberately crafted so that the de-listing of this missing capacity would be administrative in nature; no INTMMU review of these de-list bids would be required and the bids would be priced so that they would very likely clear. If the option of de-listing temperature sensitive megawatts based on price quantity pairs is permitted without market monitoring review, generators would have the ability to stay in the market at higher prices and leave at lower prices, facilitating the exercise of market power.

<sup>39</sup> NRG Pleading at 14; Milford Pleading at 13.

The market rules already provide the ability for generators to partially de-list capacity, subject to INTMMU review. This provides the flexibility that the generators request while safeguarding against the unfettered exercise of market power. As explained in the Transmittal Letter:

Allowing generators to price this uncertainty without any review by INTMMU would make this option more attractive to generators, thereby increasing the quantity of such bids and increasing the possibility of the exercise of market power by enabling generators to construct a supply curve of such de-list bids and attempt to manipulate the price.<sup>40</sup>

The proposed approach is merely an attempt to de-list capacity without review by the market monitor.

**c. The Reference Cost Formula Associated with De-list Bids Contained in the Market Rules is Just and Reasonable.**

NRG and Milford take issue with the terms of the proposed formula used to determine risk-adjusted going forward costs and claim that it is not reflective of the actual costs and risks of a particular generator. Consequently, they claim that the proposed reference formula goes beyond the legitimate role of monitoring for the exercise of market power in price formation. This is not the case. The FCM Settlement provisions associated with review of bids and offers by the INTMMU were designed to accurately measure the risk-adjusted going forward costs and opportunity cost for each generator while minimizing the potential for market power, manipulation and withholding.

NRG contests the fact that the terms in the proposed formula take into account historical data. It claims that historical data are a poor indicator of future performance and market expectations and will artificially depress the level of acceptable de-list bids.<sup>41</sup> Rather, it proposes

<sup>40</sup> February 15 Filing at 38.

<sup>41</sup> NRG Pleading at 15-16.

the use of expectations of future market revenues. This proposal should be rejected because there is no objective way to measure future market revenues in this context. If there were a liquid, transparent hub or index for New England energy three years in advance, then such an index could be used rather than historical data. However, absent such an index, historical data is the best indicator of prices in the near future. This practice of using historical data is well-established at the Commission.<sup>42</sup>

NRG argues that if historical data is factored into the proposed formula, it is inappropriate to take into account the historical Equivalent Forced Outage Rate (“EFORd”) for a unit as the basis for outage risk.<sup>43</sup> Specifically, NRG claims that the formula will understate a generator’s costs because the risk of availability penalties due to Shortage Events is much higher than it would be using historical EFORd and such risk is not captured in the proposed formula.

NRG and Milford appear to misunderstand the nature of the outage risk provision, as they mistakenly construe it to measure the uncertainty of a generator’s capacity payment. Unit outage risk actually measures the Day-Ahead Energy Market risk faced by a generator in the capacity market. This is the risk faced by a generator of having to buy back energy in the Real-Time Energy Market at high prices when, after committing to supply energy in the Day-Ahead Energy Market, it is unable to provide the energy in real time because of an outage. EFORd is the best measure of the likelihood a generator would be put into the above mentioned situation because it is the best available measure of outage risk, *i.e.* unavailability, in a given hour. This risk has no relationship to Shortage Events and capacity market payments as argued by NRG. NRG’s

<sup>42</sup> See *e.g.*, *Electric Energy, Inc.*, 113 FERC ¶ 61,245 at P 21 (2005) (Applicants for market-based rate authorization must use the most recent unadjusted 12 months' historical data as a snapshot in time. The Commission noted that "historical data have been proven to be more objective, readily available, and less subject to manipulation than future projections.").

<sup>43</sup> NRG Pleading at 15-17.

contention that the reduction in capacity payments from failure to perform during Shortage Events is a component of going forward costs is incorrect. Indeed, capacity market payments are not going forward costs, but rather going forward benefits. The design of the FCM never requires a generator to pay money to remain in the market. Consequently, measures of revenue in the capacity market are a going forward benefit, not a cost and should not be included in the going forward cost component.

NRG and Milford also argue that “[a] generator seeking to de-list will be forced to price its risk based on unrepresentative assumptions that will seriously skew ISO-NE’s determination of the resource’s net risk-adjusted going forward and opportunity costs.”<sup>44</sup> Therefore, they seek modification of the formula to take into account company-specific factors in the determination of reference costs. The requested modification should be denied. In essence, NRG and Milford would like to include their own assessment of risk, consisting of their company-specific risk tolerance and calculations. This request should be denied because they have not identified any risks that could be avoided by leaving the capacity market that are not already included in the formula.

#### **d. De-list Bids Rejected for Reliability Reasons**

NECPUC states that one way of taking steps to foster the development of new resources in locations where new capacity is required is by having “complete transparency in all reliability determinations.”<sup>45</sup> In related comments, Capacity Suppliers state that “it is important to increase the transparency of how and when [the ability of the ISO to reject bids or offers from suppliers because of local reliability concerns] of the FCM is used.”<sup>46</sup> The ISO agrees that the market

<sup>44</sup> NRG Pleading at 16.

<sup>45</sup> NECPUC Comments at 26. *See also* CT DPUC Comments at 34; Capacity Suppliers Pleading at 18.

<sup>46</sup> Capacity Suppliers Pleading at 16.

should be transparent to foster new entry where needed, which is part of the underlying rationale for Section 11, Part IX of the FCM Settlement which requires that certain determinations be filed with the Commission before an FCA is conducted. Accordingly, Section III.13.8 of the proposed market rules incorporates the reporting requirements of the FCM Settlement.<sup>47</sup> These reporting requirements should provide the transparency sought by NECPUC and Capacity Suppliers and supported by the ISO.

Further, the FCM Settlement provides that where a de-list or export bid “is rejected for reliability reasons [the resource] shall be paid a just and reasonable price (as determined by FERC).”<sup>48</sup> Some parties make arguments regarding the determination of the just and reasonable price. As the ISO stated in the Transmittal Letter:

The “proposed rules do not resolve how such a just and reasonable rate will be determined, the form of the Reliability Agreement providing for such just and reasonable rates, or the process of obtaining such a Reliability Agreement. To accomplish these ends, the ISO anticipates revising Sections I.3.9 and I.3.10 of the Tariff and the existing market rules (many of which are in Appendix A of Market Rule 1) dealing with Reliability Agreements and compensation thereunder. This major effort will also require significant stakeholder review, ISO resources and Commission approval.”<sup>49</sup>

The ISO intends to work with the stakeholders on such issues and believes that the instant proceeding is not the appropriate forum in which to do so.

## **2. The ISO’s Adoption of Show of Interest Forms and Review Is Consistent with the FCM Settlement Market Design**

### **a. There is Good Cause to Waive the 60-Day Notice Period in this Proceeding.**

<sup>47</sup> It should be noted that Section III.13.8 is before the Commission in Docket No. ER07-547-000 and not in the instant docket.

<sup>48</sup> FCM Settlement at Section 11.III.K.

<sup>49</sup> February 15 Filing at 18.

ANP protests the ISO's request for a waiver of the Commission's 60-day prior notice requirement.<sup>50</sup> ANP contends that the Commission requires a 60-day prior notice with respect to all aspects of the ISO's February 15 Filing. ANP cites *Central Hudson Gas Electric Corporation* ("*Central Hudson*"), which held that the Commission would grant waiver of the 60-day prior notice requirement when: (1) a filing is uncontested and does not change rates; (2) a filing reduces rates and charges; or (3) a filing is made to effectuate a contract or settlement.<sup>51</sup> ANP also points to the *Central Hudson* case for the proposition that "absent extraordinary circumstances," the Commission will not grant waiver of notice when an agreement for new service is filed on or after the day service has commenced.<sup>52</sup> ANP argues that the ISO's proposed February 16, 2007 effective date violates the tenets of *Central Hudson* because the February 15 Filing: (1) has a clear rate impact; (2) has the potential to raise rates; and (3) is directly inconsistent with the terms of the FCM Settlement. Contrary to ANP's assertions, based on *Central Hudson* and other FERC precedent, the Commission should grant the ISO's request for a waiver of the notice period.

**(i) Precedent Supports Waiver of the 60-Day Notice Period in the Proceeding**

Section 205(d) of the FPA, which sets forth the general notice requirement for tariff changes, provides that "(t)he Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice...."<sup>53</sup> The Commission has previously determined that good cause is shown "when [1] the parties to the rate have agreed at some point in their

<sup>50</sup> ANP Pleading at 4-7.

<sup>51</sup> *Central Hudson Gas Electric Corporation*, 60 FERC ¶ 61,106 at p. 61,338 (1992), *reh'g denied*, ¶61 FERC ¶ 61,089 (1992).

<sup>52</sup> *Id.* at p. 61,339.

<sup>53</sup> 16 U.S.C. § 824d(d) (2000); 18 C.F.R. §§ 35.3, 35.11 (2006).

negotiations on an effective date and [2] the waiver is in the public interest.”<sup>54</sup> The Commission has exercised its discretion to waive its notice requirement in many instances.<sup>55</sup> Furthermore, the Commission has granted waiver despite the objections of a party when, as in the instant case, as discussed below, the waiver is consistent with the terms of a contract or settlement between the parties.<sup>56</sup>

The ISO has clearly demonstrated that good cause exists to grant the requested waiver since the requested waiver is necessary to implement the FCM Settlement. As explained in the February 15 Filing and below, the Show of Interest Forms and the qualification deposit are just and reasonable, consistent with the FCM Settlement, and necessary to allow the ISO to conduct the necessary analyses for participation in the FCM. The proposed market rules governing those procedures must become effective as of February 16, 2007, in order for the first FCA required by the FCM Settlement to proceed on the tight schedule to which the parties agreed. Accordingly, good cause exists to grant the ISO’s request to waive the 60-day prior notice period requirement.

**(ii) Rate Considerations do not Require Denial of the ISO’s Request for Waiver of the Notice Period**

The February 15 Filing implementing the FCM Settlement is much different than a standard Section 205 filing requesting a cost-of-service rate increase. Thus, the *Central Hudson* case cited by ANP is readily distinguishable on its face. However, even if that case were directly

<sup>54</sup> See *City of Girard v. FERC*, 790 F.2d 919, 925 (D.C. Cir. 1986); see also *San Diego Gas & Electric Co. v. FERC*, 904 F.2d 727, 731 (D.C. Cir. 1990).

<sup>55</sup> See, e.g., *Pacific Power & Light Co.*, 27 FERC ¶ 61,080 (1984); *Dayton Power and Light Company*, 3 FERC ¶ 61,004 (1978), *order on reh’g*, 2 FERC ¶ 61,037 (1979), *aff’d*, *The City of Piqua, Ohio v. FERC*, 610 F.2d 950 (D.C. Cir. 1979); *New York Independent System Operator, Inc., et al.*, 91 FERC ¶ 61,218 (2000); *Mirant Americas Energy Marketing, L.P.*, 105 FERC ¶ 61,359 (2003), *order on compliance filing*, 106 FERC ¶ 61,243 (2004), *order on reh’g*, 112 FERC ¶ 61,056 (2005), *aff’d on waiver of notice issue*, *NSTAR Electric & Gas Corporation v. FERC*, No. 05-1362, Decided March 9, 2007, \_\_\_ F.3d \_\_\_ (D.C. Cir. 2007).

<sup>56</sup> *Northeast Utilities Service Company*, 52 FERC ¶ 61097, at p. 61,486 (1990) citing *Public Service Company of New Mexico*, 43 FERC ¶ 61,469, at p. 62,154, *reh’g denied*, 45 FERC ¶ 61,024 (1988), *affirmed sub nom.*, *San Diego Gas & Electric Company v. FERC*, 904 F.2d 727 (D.C. Cir. 1990). See also, *Southern California Edison Company*, 40 FERC ¶ 61,202 (1987).

on point, such rate considerations as arise here argue in favor of granting the ISO's request for waiver of the 60-day notice period. If the ISO does not have adequate time to perform the transmission analyses of the project proposals outlined on the Show of Interest Forms, the ISO may not be able to identify, prior to the FCA, all of the projects that may not be able to be interconnected to the system. Therefore, substantial investment may be made in some projects that ultimately are not qualified to bid without significant additional investment and construction of transmission upgrades and the resulting delay. Even just a few such incidents and the resulting uncertainty would greatly and unnecessarily chill competition, discourage investment in the market, and ultimately result in a below optimal number of projects proposed and built for the New England capacity market. Thus, there would be fewer competing supply projects than if the ISO were given the necessary review time through the Show of Interest Form process, and the "rates" resulting from the FCAs would almost certainly be greater, not less, as argued by ANP, than if the Commission grants the ISO's request for waiver of the 60-day notice period.

**(iii) Market Participants had Ample Notice and Opportunity to Comment on the ISO's Proposal.**

ANP concludes its argument concerning the required notice with a request that the Commission "afford market participants the opportunity to comment upon" the proposed Show of Interest and Qualification Process Deposit procedures.<sup>57</sup> This request ignores the many months that New England market participants have had to consider issues arising in connection with these proposed procedures in the ongoing FCM stakeholder process since the ISO first introduced the procedures last year. ANP has already had ample opportunity to comment on the ISO's proposals during that process and has there fully exercised its right to comment. Clearly, a further stakeholder process on these proposed procedures would be wasteful of the ISO's and the

<sup>57</sup> ANP Pleading at 7.

parties' resources, and since the arguments made in ANP's protest concerning waiver of the notice period have no merit, as discussed above, those arguments should be rejected.

Similarly, ANP is incorrect when it notes that the qualification process deposit for the first FCA is required by February 20, 2007, "just five (5) days and just (2) business days from now."<sup>58</sup> ANP, in effect, is suggesting that this is a surprise to market participants. However, the ISO introduced the concept of this deposit in the fall of 2006, approximately at the same time that it introduced the concept of the Show of Interest Form and discussed that form in all the meetings described in the February 15 Filing.<sup>59</sup> Thus, market participants have had months to consider and prepare for compliance with the deposit requirement as they have had with regard to the Show of Interest requirements in general.

For all of these reasons the Commission should reject ANP's arguments concerning the waiver of the 60-day notice period.

**b. The Show of Interest Form is Just and Reasonable**

In arguing that the proposed Show of Interest Form process is not just and reasonable, ANP ignores the fact that in order for the ISO to meet the February 2008 deadline for the first FCA set forth in the FCM Settlement, certain actions must take place. The Show of Interest Forms for New Generating Capacity Resources are an essential step in the process leading up to the FCA, and are needed at the earliest possible time to provide the ISO with a meaningful opportunity for their review. ANP is wrong in stating that the ISO will have years to determine whether New Capacity Resources satisfy the criteria for participation in the FCA.<sup>60</sup> As explained at length in the February 15 Filing, the ISO must immediately begin extensive analysis

<sup>58</sup> *Id.*, at 12.

<sup>59</sup> February 15 Filing at 12-13.

<sup>60</sup> ANP Pleading at 7.

of the projects which wish to qualify for the first FCA. Such an analysis must be done prior to the FCA, not afterwards when projects that clear in the FCA must be able to interconnect and operate. The ISO has estimated, for example, that with respect to approximately twelve Show of Interest Forms that require initial interconnection analyses it will take twelve weeks to perform these analyses and, up to twelve weeks to evaluate possible overlapping impacts.<sup>61</sup> In addition,

These analyses are time consuming because power flow and short circuit models must be run for each project individually. Once this is achieved, the ISO must evaluate whether new transmission facilities are needed and determine the feasibility of building such facilities in time for the Capacity Commitment Period. This step will include consultation with affected Transmission Owners and the Project Sponsor as appropriate. With multiple applications, numerous iterations of analyses may be needed in order to evaluate potential cumulative and overlapping impacts between projects.<sup>62</sup>

The ISO has amply demonstrated that the Show of Interest Forms are a just and reasonable means of implementing the FCM Settlement. Indeed, they are a necessary means of implementing the FCM Settlement in a timely fashion.

In its March 8, 2007 supplement to its protest, ANP stated that the ISO devoted approximately 30 pages of the February 15 Filing to an explanation of why the Show of Interest Forms and the ISO's preliminary interconnection analyses was necessary.<sup>63</sup> ANP does not raise a factual question concerning the need for potential suppliers to provide the ISO this information during the proposed time frame in order for the ISO to conduct these necessary analyses. Rather, ANP asserts that even if the proposed "study period" is necessary, "that would not be an excuse to allow the ISO to make up its own rules, and without Commission approval, penalize New Capacity Resources for not complying with those rules."<sup>64</sup>

<sup>61</sup> February 15 Filing at 13.

<sup>62</sup> *Id.*

<sup>63</sup> ANP Supplemental Pleading at 3.

<sup>64</sup> ANP Supplemental Pleading at 4.

The ISO is doing no such thing. The ISO's proposed rules were carefully constructed, and fully considered and approved by New England stakeholders. They have been submitted to the Commission for approval, and if that approval is granted after consideration of the full explanation of the need for those procedures provided by the ISO, the ISO will have authority to enforce them. ANP, in effect, suggests that the Commission never allows or could never allow waiver of the 60-day prior notice period. But, as explained above, that simply is not the case and should not be the decision here.

In its Supplemental Protest, ANP also argues that the 200 Show of Interest Forms filed show only that the ISO created a circumstance that forced market participants prematurely to file applications to prevent the ISO from disqualifying them. Those 200 Forms show no such thing. Which of those 200 forms were purely voluntary and which, if any, were believed by any party to be in any way premature is purely speculative. What that massive filing of forms does clearly indicate is that there is significant interest in participating in the first FCA and few parties, as shown by their conduct, concluded that the required Show of Interest Forms were a significant barrier to their participation. Given that showing of significant interest, the ISO must be provided the time necessary to conduct the required analysis to allow timely implementation of the first FCA established by the FCM Settlement. This response to the Show of Interest requirements verifies the ISO's contention that the Show of Interest process is necessary to allow full consideration of all applications. That some applicants may have filed some placeholder applications, by itself, is neither surprising nor indicative of a problem with the Show of Interest procedures. There simply is not time for the ISO to do the required analysis if the ISO only studies "projects after market participants have had an opportunity to refine their proposals"<sup>65</sup> in

<sup>65</sup> *Id.* at 5.

the overly rigid time frame contemplated by ANP, which is not required by the FCM Settlement. Despite ANP's arguments, over 15,000 MW of supply projects submitted Show of Interest Form and deposits, signaling their intent to be more than a placeholder.

ANP also argues in its Supplemental Protest that the Show of Interest procedures are a barrier to competition.<sup>66</sup> However, as discussed above, it is likely that fewer rather than more viable projects will ultimately participate in FCAs if the ISO's proposed Show of Interest Form procedures are rejected and the ISO thus has insufficient time to review project proposals prior to the FCA. The ISO's proposal enhances competition rather than constitutes a barrier to it.

**c. The Qualification Process Cost Reimbursement Deposit is Just and Reasonable**

For these same reasons, the Commission should find that the Qualification Process Cost Reimbursement Deposit provisions are just and reasonable. The deposit is also a critical component in the process that the ISO requires to identify and qualify the maximum number of viable projects for participation in the FCA by requiring sponsors to pay for the costs of studies related to their project. As stated in the February 15 Filing,<sup>67</sup> the Cost Reimbursement discourages speculative projects that are not likely to advance so that the ISO can concentrate its resources on projects that are likely to qualify for the FCA.

In objecting to the qualification process deposit, ANP concedes that the amount of the \$25,000 deposit for each new capacity resource "may not be significant," but asserts that the amount of the deposit is irrelevant, and the ISO has neither the right nor need to collect it.<sup>68</sup>

ANP also argues that the FCM Settlement does not contemplate that new capacity resources will

<sup>66</sup> ANP Supplemental Pleading at 7.

<sup>67</sup> February 15 Filing at 11.

<sup>68</sup> ANP Pleading at 12.

have to submit financial deposits to the ISO prior to being informed that they qualify for the auction. ANP further argues that the ISO does not explain why it allegedly needs a new and additional deposit to study a facility that it already will be studying when a project developer applies, as it must, to obtain an interconnection under the existing Large Generator Interconnection Procedures. ANP also claims that a market participant has the right to know that the Commission has found a proposal to be just and reasonable before it is compelled to make a financial commitment, whether that commitment is substantial or not. ANP believes that the Commission should provide all new capacity resources the opportunity to make such deposits only on a prospective basis after the Commission issues an order on the ISO's filing.

Initially, it is telling that ANP concedes that the amount of the \$25,000 deposit “may not be significant.”<sup>69</sup> If in fact it is not significant, it should be viewed as a detail which the ISO has ample discretion to address under the FCM Settlement. General settlements by their nature cannot address every possible detail in the implementation of a market as complex as the FCM, and therefore parties who have the task of implementing such settlements, such as the ISO, need to be provided reasonable latitude to develop all the practical details that are necessary for such a complex market to operate effectively. This is particularly the case with regard to reasonable requirements which are not burdensome, such as the proposed Show of Interest procedures and the qualification process deposit.

Further, ANP is incorrect in arguing that the ISO has not explained the need for the qualification deposit. In the February 15 Filing, the ISO explained why this deposit is necessary

<sup>69</sup> ANP Pleading at 12.

in addition to the standard interconnection fee, both to cover the costs of analysis involved and to winnow out incomplete proposals.<sup>70</sup>

Finally, granting ANP's request to delay the effective date of the qualification deposit to a date prospective from a Commission order on this issue is counterproductive: one purpose of the deposit is to winnow out projects that are not serious or well-developed prior to the time that the ISO will commence its interconnection studies. Accordingly, the Commission should deny ANP's request.

**d. The ISO's Proposed Show of Interest Form and Qualification Deposit Procedures are Consistent with the FCM Settlement.**

Contrary to ANP's argument, the ISO's Show of Interest Forms and qualification deposit proposals are consistent with the FCM Settlement. In its protest, ANP cites Section 11.II.A of the FCM Settlement, which provides that potential capacity resources must submit qualification information to the ISO no later than the relevant bid qualification deadline, which for new capacity and imports will be approximately six weeks after the ISO's posting of de-list and export bids from existing capacity.<sup>71</sup> ANP asserts that this is the only permissible bid qualification deadline for new capacity resources. ANP further argues that Section 11.III.D.2 of the FCM Settlement requires that the qualification deadline for new resources be after the qualification deadline for existing capacity because under that section, de-list and export bids may be submitted to the ISO up until the qualification deadline for existing capacity.<sup>72</sup> ANP asserts that the ISO is seeking to disqualify new capacity resources from participation in FCAs if they

<sup>70</sup> February 15 Filing at 14.

<sup>71</sup> ANP Pleading at 7-10.

<sup>72</sup> *Id.* at 10.

fail to get complete information in final, unalterable form to the ISO four months before the qualification deadline for existing capacity.<sup>73</sup>

These arguments should be rejected. The ISO is not changing the Settlement provisions concerning qualification cited by ANP. The ISO is only proposing essential preliminary screening provisions that are easy to meet for any new project that is likely to qualify under the FCM Settlement qualification provisions. As discussed above and in detail in the February 15 Filing,<sup>74</sup> the Show of Interest Form is necessary in order for the ISO to have enough time to conduct all of the analyses required to assess the feasibility of proposed projects.

It is also clear that it is reasonable to interpret the FCM Settlement to allow the ISO to propose such measures that are essential if the FCM is to be workable. As stated in the February 15 Filing:<sup>75</sup>

Section 3.B of the Settlement provides that “The market rules shall be consistent with, and in furtherance of, all the terms contained in this Settlement Agreement \* \* \* .” Importantly, this provision clearly recognizes that ISO and stakeholder development of market rules implementing the Settlement will necessarily go far beyond the specific language of the Settlement itself. Indeed, as with most settlements, the FCM Settlement established a framework for the market, but the rules must clearly set out all of the rates, terms and conditions that are applicable. Accordingly, the ISO has undertaken a massive effort to ensure that the market will be effectively implemented through its rules. In many areas, most notably the qualification section of the rule, the ISO has developed detailed timelines, standards and processes for resource qualification. As will be detailed throughout this filing, the rules clearly meet the Section 205 standard and, in addition, meet the Settlement standard that they must be “consistent with, and in furtherance of, all the terms contained in this Settlement Agreement.”<sup>76</sup>

The ISO notes also that Part 3.B of the FCM Settlement goes on to state “[e]ach Settling Party retains the right to challenge the provisions of the market rules that address the terms of

<sup>73</sup> ANP Pleading at 8.

<sup>74</sup> February 15 Filing at 9-11 and 29-31.

<sup>75</sup> *Id.* at 5.

<sup>76</sup> FCM Settlement at Section 3.B.

this Settlement only on the basis that they contain provisions that are either inconsistent with or not required by this Settlement Agreement.”<sup>77</sup> Therefore, the absence of specific direction in the FCM Settlement to require a particular provision of the market rules is not, in and of itself, sufficient justification to reject the inclusion of those rules. It is the ISO’s position that the market rules, as filed, are required to implement the FCM Settlement.

Further, ANP is incorrect in suggesting that under the ISO’s proposal, new capacity will fail to qualify unless it gets “complete information” to the ISO in the Show of Interest Form four months before the qualification deadline for existing capacity. The information required in the Show of Interest Form is nowhere near the “complete” information required for qualification that is required in the New Capacity Qualification Package (described in proposed Section III.13.1.1.2.2 of the Rules) that must be submitted by the New Capacity Qualification Deadline. A line by line comparison of the information required in the New Capacity Qualification Package and in the Show of Interest Form indicates that the information required by the latter is very rudimentary and that the Show of Interest Form only requires the Project Sponsor to outline the most basic elements of its project. For example, no information is required in the Show of Interest Form concerning critical project milestones such as the status of equipment orders and financing.

ANP is also incorrect in characterizing the information required in the Show of Interest Form as “unalterable.”<sup>78</sup> Section III.13.1.1.2.1 of the proposed tariff provisions specifically provides that only “material changes” (as defined in the long standing interconnection provisions of Market Rule 1) to the basic information provided in the Show of Interest Form are prohibited.

<sup>77</sup> FCM Settlement at Section 3.B.

<sup>78</sup> ANP Pleading at 10.

**e. Even if Applicable, the ISO has met its Burden to Propose a Modification of the FCM Settlement Market Rules**

Above, the ISO has shown that the proposed Show of Interest and qualification deposit procedures are reasonable and consistent with the FCM Settlement. However, such procedures are also justified as a modification to the FCM Settlement Market Rules if the FCM Settlement provisions concerning such modifications would be deemed applicable. Section 4.A of the FCM Settlement provides that

Except . . . , the ISO shall retain its authority under Section 205 of the FPA to file *modifications of the Market Rules that address the terms of the Settlement Agreement*; where the ISO makes such a filing, the ISO must demonstrate to the FERC that failure to implement the proposed change in the Market Rule would have a negative effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. (emphasis added)

Initially, since the language of Section 4.A omitted by ANP is phrased in terms of “modifications of the Market Rules that address the terms of the Settlement Agreement,” the quoted portion of Section 4.A arguably does not apply to the existing situation because in the February 15 Filing the ISO is proposing implementing market rules in the first instance and is not proposing to change existing market rules previously accepted by the Commission.

However, even if the two standards set forth in the quoted portion of Section 4.A apply, the ISO is justified in proposing the Show of Interest and qualification deposit tariff provisions. Clearly, failure to implement these provisions would have a significant negative effect on both system reliability and the competitiveness and efficiency of the FCM. System reliability would be compromised if ANP’s proposals concerning the Show of Interest and qualification deposit provisions are adopted because the ISO would then be forced to analyze a large number of proposals in an insufficient time period, with the result that the ISO would not have enough time to identify and verify all the proposals that would enhance reliability in the most effective and

efficient manner. Similarly, competition would be decreased not increased by adopting ANP's proposals because the ISO would then have insufficient time to identify and qualify all potentially viable competing projects, including perhaps the least costly projects, and such projects could then not participate in the FCA.

**f. ANP's Ex Post Facto Argument is Inapplicable and Should Be Rejected.**

In both its protest and its supplemental protest, ANP argues that the ISO is seeking to have the Commission impose the Show of Interest Procedures on an *ex post facto* basis.<sup>79</sup> ANP asserts that the ISO proposes to disqualify new capacity resources from participating in the FCA for the period commencing June 1, 2010, based upon a failure to have complied with the ISO's proposed procedures by January 2, 2007. However, the ISO has not interpreted the February 15 Filing in this manner. As the ISO stated in the February 15 Filing Transmittal Letter, the ISO's request that Project Sponsors submit a Show of Interest Form prior to February 15, 2007 when the proposed rules were filed, did not have the force of law, and the ISO accepted Show of Interest Forms received between January 2, 2007 and February 15, 2007. After its February 15 Filing and prior to the February 20, 2007 date for submitting deposits, the ISO received additional Show of Interest Forms, which the ISO has determined it will be able to review for the first FCA. The ISO would like to clarify that, for purposes of qualifying for the first FCA, generating projects will be reviewed by the ISO under the FCM market rules if the Project Sponsor has submitted both a Show of Interest Form and deposit by February 20, 2007. Accordingly, ANP's argument concerning this issue should be rejected as inapplicable.

**3. The HQI Issues Are Properly Addressed by the Market Rules**

<sup>79</sup> ANP Pleading at 10-12. ANP Supplemental Pleading at 6.

HQUS protests the proposed requirement for month-ahead around-the-clock transmission reservations to import HQI Capacity.<sup>80</sup> It asserts that this provision violates the express language of the FCM Settlement<sup>81</sup> that provides that the rules “shall be changed to allow External Resources to participate in the Forward Capacity Market . . . on a basis comparable to internal generation Resources.”<sup>82</sup> It maintains that no other resource must reserve transmission to sell capacity – let alone in every hour of each month, and that this requirement is unnecessary. HQUS believes that the FCM and reconfiguration auctions themselves prevent double-counting,<sup>83</sup> and that a much simpler method proposed by HQUS in the stakeholder process can be used to ensure that credit for capacity over the HQ Phase I/II facilities is given to the proper party. HQUS believes that the IRHs are capable of ensuring the correct allocation of HQ Interconnection Capability Credits (“HQICCs”) between themselves and already have a procedure to do so.<sup>84</sup>

NSTAR Electric & Gas Corporation (“NSTAR”) asserts that the proposed netting provisions governing treatment of HQICCs impermissibly vitiate existing HQICC contractual rights held by certain load served by IRHs by expropriating HQICCs to benefit import capacity

<sup>80</sup> HQUS Pleading at 1.

<sup>81</sup> FCM Settlement at Section 11 part VI.

<sup>82</sup> FCM Settlement at II.VI.

<sup>83</sup> HQUS argues that there is no risk of double-counting because of the FCA:

The initial quantity of necessary HQICC reductions will be known two to three years in advance when ISO-NE runs the Forward Capacity Auction. This amount may be adjusted by subsequent reconfiguration auctions, but HQUS’ final opportunity to participate in any such auction is at least one year prior to the market. The auction results will clearly demonstrate how much transmission capacity will be utilized on Phase I/II. This in turn will make the necessary amount of HQICC reductions *blatantly obvious*, with no less than one year’s advance notice for HQUS’ imports. To our knowledge, no NEPOOL participant disagrees with this fact. As such, the around-the-clock reservation requirement is *not* essential to avoid double-counting, and in fact, is not needed for that purpose at all.

HQUS Pleading at 12-13.

<sup>84</sup> HQUS Pleading at 13.

contracts.<sup>85</sup> NSTAR maintains that the proposed rules effectively provide that capacity import contracts may totally displace HQICCs, with the FCA revenues going exclusively to third-party contract holders and with no compensation for the lost value of the tie benefit provided to the load that would otherwise enjoy the value of the HQICC.<sup>86</sup> NSTAR is concerned that as a result of the proposed rules, it is likely that third parties will seek to use the entire 1800 MW of tie benefits to import ICAP, thus reducing the HQICC benefit to zero and requiring IRHs to pay the CONE to replace the lost value of their HQICC.<sup>87</sup> It argues that allowing capacity imports to exceed the total capacity of the HQI excess would transfer the higher cost of capacity acquired from the FCA while conferring a windfall on capacity importers that have not borne the cost of creating the tie benefit.

NSTAR further asserts that the current netting provision in Market Rule 1 is also wrong and that the Commission should not perpetuate that alleged error by allowing the instant proposed netting mechanism.<sup>88</sup> Rather, NSTAR requests that the maximum amount of import capacity offered be limited to the total available capacity of the HQI minus the total HQICCs.

National Grid USA (“National Grid”) asserts that, absent some modification to the current recovery structure in New England, New England Power Company (“NEP”) (and National Grid's ultimate customers) will forfeit the value of its HQICCs if firm capacity imports exceeding the total 600 MW threshold are brought into New England.<sup>89</sup> According to National Grid, considering that HQICCs are valued at the same price as capacity in the FCM, the revenue loss to NEP, and hence to National Grid's ultimate customers, will be considerably greater than

<sup>85</sup> NSTAR Pleading at 4.

<sup>86</sup> NSTAR Pleading at 6.

<sup>87</sup> NSTAR Pleading at 9.

<sup>88</sup> NSTAR Pleading at 11.

<sup>89</sup> National Grid Pleading at 9-10.

any gain due to increased transmission reservations over the Phase I/II HVDC.<sup>90</sup> National Grid states the Service Providers under Schedule 20A of Part II of the ISO Tariff (“Schedule 20A”) are developing a solution to ensure that customers in New England are protected from the loss of HQICCs to which they are entitled.<sup>91</sup> Although National Grid believes that there is no need for the Commission to defer its evaluation of this portion of the February 15 Filing, it requests the Commission to ensure that any action on the February 15 Filing will not prejudice any future filings addressing the impacts of the FCM on HQICCs.<sup>92</sup>

In their comments, the PPL Parties<sup>93</sup> assert that there should not be any reduction in the level of HQICCs that are allocated to the IRH associated with non-firm service over the Phase I/II HVDC, or with firm service of 600 MW or less during non-winter months.<sup>94</sup> Moreover, they maintain, the IRH should not be obligated to provide firm service in excess of 600 MW, consistent with the discussion in the ICR Order.<sup>95</sup>

There are a number of issues that must be properly resolved to assure that the HQICCS associated with the HQ I/II HVDC facilities and any contracts over those facilities are treated properly in the FCA. The February 15 Filing is a consistent set of rules that will enable those that own the facility and those that import capacity over the facility to participate in the FCA without double counting the facility’s capacity benefit and enable the ISO to determine, as part of the clearing of the FCA, which party will be paid for the capacity and has responsibility for delivering that capacity.

<sup>90</sup> National Grid Pleading at 9-10.

<sup>91</sup> National Grid Pleading at 10.

<sup>92</sup> National Grid Pleading at 10.

<sup>93</sup> The PPL Parties include PPL EnergyPlus, LLC, PPL Maine, LLC, PPL Great Works, LLC, and PPL Wallingford Energy LLC.

<sup>94</sup> PPL Parties Pleading at 6.

<sup>95</sup> PPL Parties Pleading at 6-7.

Some of the owners of the facility (PPL, NSTAR) have sought to assure that HQICCs are not reduced by treating HQICCs as a tie benefit, (but in the event they are the owners are paid the capacity clearing price for any capacity sold over the facility that reduces the HQICCs). The owners argue that the HQICCs are a tie benefit identical to the tie benefits from New York and New Brunswick, and argue that sufficient transmission capacity should be reserved over the Phase I/II HVDC facility for HQICCs in the same way capacity is reserved over the New York and New Brunswick ties.<sup>96</sup> On the other hand, HQUS, which seeks to sell capacity over the facility, wants as few restrictions as possible on its ability to sell capacity into the FCM.

The ISO did not propose to treat the Phase I/II HVDC facilities as a tie benefit identical to the tie benefits from New York and New Brunswick because these facilities are not paid for by all customers as part of the Regional Tariff but are owned by a separate set of owners. The ISO's rules on the use of the Facilities in the FCA were designed to meet two objectives. First, that the benefits of the line properly flow to the Facilities' owners and second, that the tariff provisions governing use of the line in Schedule 20A are respected. To understand how this is accomplished, it is helpful to review the use of the Facility during the transition period.

Under the rules governing capacity transactions during the transition period, those wishing to import capacity over the Phase I/II HVDC facilities notify the ISO that they wish to do so and the amount they wish to import. Contracts must be for a minimum of two months within a Capacity Commitment Period. There are two types of capacity contracts, a fixed capacity contract and a dispatchable capacity contract. Fixed capacity contracts must submit energy transactions and reserve transmission for all on-peak hours of the month. Dispatchable

<sup>96</sup> The proper forum for the IRH to have raised this issue was in the recent docket on ICR methodology. The ISOs filing in that docket clearly stated that HQICCs were to be treated differently than tie benefits and provided for the displacement of HQICCs by capacity contracts.

capacity contracts must submit energy transactions and reserve transmission for all hours of the month. At the end of the month the ISO verifies that these requirements have been met.

Under Schedule 20A, transmission reservations are used by the ISO to allocate the capacity benefits of the line between the owners of the line (the IRHs) and those who import capacity over the line. Per the FCM Settlement Agreement<sup>97</sup> during the ICAP Transition Period, the ISO will accept up to 1800 MW of capacity over the Phase I/II HVDC facilities. Currently, there is a maximum of 1200 MWs of HQICCs.<sup>98</sup> This means that up to 600 MW of capacity contracts may be imported over the HQ HVDC facilities and the IRH will continue to receive 1200 MW of HQICCs. Schedule 20A and associated procedures enforce this by reducing the HQICCs when the transmission reservations for a given month exceed 600 MW. Consistent with the description above, the transmission reservations are for all hours in the month (for a dispatchable transaction) or all on peak hours of the month (for a fixed transaction).

HQUS argues that the requirement in the FCM rules to reserve transmission for all hours of the month as a condition of delivering capacity over the facilities is too onerous and contradicts the language in the FCM Settlement requiring that the market rules be changed to allow External Resources to participate in the FCM on a basis comparable to internal generation resources. HQUS notes that this requirement only applies to contracts that reduce HQICCs and not to contracts that would fall into the 600 MW category in the example above. In contrast, the owners of the facility have argued that they should be paid the value of the capacity for their

<sup>97</sup> FCM Settlement Agreement at Section 11.VIII.K.

<sup>98</sup> The PPL Parties state that in an example in its transmittal letter in the February 15 Filing, the ISO assumed that it will not count more than 1400 MW of capacity contracts and HQICCs over the Phase I/II HVDC facilities, whereas the line is currently approved at an 1800 MW value. PPL Parties Pleading at 6. The ISO here clarifies that the PPL Parties are correct in stating that the line is now approved at the 1800 MW value.

reduction in HQICCs if the amount of capacity contracts is large enough to reduce the HQICCS, which would occur if the contracted capacity was greater than 600 MW in the example above.

The proposed market rules contain a requirement that capacity contracts that displace HQICCs have around-the-clock transmission reservations to assure that those delivering the capacity have the use of the Phase I/II HVDC facilities. If a requirement for around-the-clock transmission reservations is not in place, then, under the current provisions of Schedule 20A, since the transmission has not been reserved to deliver the energy contracts to back the capacity contracts, there is no requirement or authority to reduce the HQICCs. In this scenario, the reliability benefits could be double counted as capacity contracts and HQICCs.

Thus, contrary to HQUS' argument, the proposed market rules do not unduly discriminate between external and internal resources. Unlike internal resources, the ISO does not have sole control over ties connecting to other control areas and, as explained above, the ISO must ensure that capacity is not double counted to ensure, in turn, that installed capacity deliveries from external sources may be relied upon. The ISO has proposed one effective method to achieve this result. If the ISO's proposal to require the reservation of transmission capacity to deliver capacity that displaces HQICCs is altered, as argued by HQUS, then there must be some other mechanism to ensure that after the FCM auctions HQICCs are reduced as necessary to avoid double counting. However, if the transmission use requirement is not in place, then it is debatable whether the HQICCs should be reduced since the transmission from which they are derived is still available.

**4. FCM is an Annual Market and it is Appropriate to Require Demand Resources Participating in the FCM to Provide Capacity for 12 Months.**

Some protestors contest the requirement in the market rules that Demand Resources provide capacity for the full 12 months of the Capacity Commitment Period either on their own

or as part of a composite offer that provides capacity for the full 12 months, as is required of other resources. These protestors maintain that this requirement will undermine their ability to participate in the FCM, in violation of the FCM Settlement.<sup>99</sup> Some of the protestors advocate that the market rules be modified to allow summer-only Demand Resources to participate in the FCM on a seasonal basis.<sup>100</sup>

The ISO believes that the proposed treatment of Demand Resources as set forth in the market rules is appropriate and takes into account the unique nature of Demand Resources as discussed in more detail below, as well as the Commission's policy of encouraging Demand Resources. Allowing summer-only Demand Resources to participate in the FCM without an annual availability requirement is consistent with the basic structure of the FCM. The FCM is an annual market for an annual product. It was designed this way because the reliability standard it is designed to meet is an annual reliability requirement that requires the same amount of capacity to be available all year round. Protestors argue for a limited exception for DR resources. However, they fail to note that Demand Resources are not the only resources that are seasonal in nature and, if the option were available certain natural gas-fired generators might prefer to be summer-only resources as well because of fuel supply limitations in the winter. Allowing Demand Resources such summer-only treatment would set a precedent that could undermine the

<sup>99</sup> See Protest of Comverge, Inc., Conservation Law Foundation, Connecticut Office of Consumer Counsel, the E Cubed Company, LLC., Massachusetts Division of Energy Resources, New Hampshire Public Utilities Commission, Northeast Energy Efficiency Partnerships, and National Association of Energy Services Companies ("DR Coalition") at 3, *ISO New England Inc.*, Docket No. ER07-546-000 (filed Mar. 8, 2007) ("DR Coalition Pleading"); and Motion to Intervene, Protest, and Comments of the New England Conference of Public Utilities Commissioners Regarding Revisions to Market Rule 1 Relating to the Forward Capacity Market at 39, *ISO New England Inc.*, Docket No. ER07-546-000 (filed Mar. 8, 2007) ("NECPUC Pleading"). The New Hampshire Public Utilities Commission and Cape Light Compact join in the DR Coalition Protest. See New Hampshire Public Utilities Commission Notice of Intervention and Joinder in Protest and Comments of the New England Conference of Public Utilities Commissions and Joinder in Protest of Demand Response Coalition, *ISO New England Inc.*, Docket No. ER07-546-000 (filed Mar. 8, 2007); and Cape Light Compact letter, Docket No. ER07-646 (filed March 7, 2007). Several state utility commissions have joined in NECPUC's Pleading. See NECPUC Pleading at 1, n.3.

<sup>100</sup> See, e.g., CSG Pleading and DR Coalition Pleading.

ability of FCM to meet the annual reliability criterion it is designed to achieve, as others who might prefer such treatment would argue for it and raise the problem from one of hundreds megawatts to a problem of thousands of megawatts.

**a. Protests Urging Inclusion of Summer-Only Resources Should be Rejected, As Allowing Summer-Only Demand Resources Without an Annual Availability Requirement Would Undermine the Basic Structure of the FCM to which the Parties Agreed in the FCM Settlement and Could Require a Fundamental Redesign of the Market Which is Not Contemplated by the FCM Settlement.**

Various protestors urge FERC to permit participation in the FCM by summer-only Demand Resources without requiring 12 month availability or composite bids. The DR Coalition<sup>101</sup> asks FERC to modify the proposed market rules to adopt the DR Coalition's specific proposal to allow participation by summer-only Demand Resources.<sup>102</sup> The proposal would not require 12 month availability or composite bids, although participation through composite bids would be an option. The DR Coalition would cap capacity offers by summer-only Demand Resources, up to a limit of 400 MW.<sup>103</sup> The DR Coalition maintains that its proposed changes are "simple and surgical," "would not unduly delay implementation of the FCA," and would, instead, "ensure the success of the FCA by fully integrating demand resources."<sup>104</sup>

However, the DR Coalition's proposed modifications are not innocuous. Instead, allowing seasonal or monthly products would require a fundamental redesign of the capacity market, contrary to the market design contemplated by the FCM Settlement. The FCM was

<sup>101</sup> The DR Coalition consists of: Comverge, Inc., the Conservation Law Foundation, Connecticut Office of Consumer Counsel, The E Cubed Company, LLC., Massachusetts Division of Energy Resources, New Hampshire Public Utilities Commission, Northeast Energy Efficiency Partnerships, and National Association of Energy Services Companies.

<sup>102</sup> DR Coalition Pleading at 7 and Attachment A.

<sup>103</sup> The cap would seek to avoid an unlimited amount of summer-only Demand Resources being offered, which may negatively impact reliability. DR Coalition Pleading at 7-8.

<sup>104</sup> DR Coalition Pleading at 5.

established to procure an annual capacity product, as the DR Coalition acknowledges.<sup>105</sup> In developing the market rules for Demand Resources' participation in the market, it was recognized that, even though New England is a summer-peaking region, the FCM must be based on an annual product because ICR is an annual requirement, which provides for sufficient off-season capacity to maintain system reliability while enabling other resources to go off-line for scheduled maintenance and to cover unscheduled outages as well. To the extent Demand Resources procured through the FCM are used to meet ICR, but permitted to participate on a summer season basis only, the ISO would not be meeting its reliability criterion in the non-summer months, thus frustrating the very purpose of the Settlement.

While the DR Coalition and NECPUC argue that the 12-month availability requirement for Demand Resources is not required by the FCM Settlement,<sup>106</sup> the fact is that the full-year availability requirement necessarily flows from the FCM Settlement, which is premised on procuring sufficient installed capacity to maintain system reliability. The DR Coalition and NECPUC maintain that the failure of the market rules to provide for seasonal participation by summer-only Demand Resources contravenes the FCM Settlement's requirement that a "distinct method" be developed to allow Demand Resources "to be fully integrated" as capacity in the FCM.<sup>107</sup> Contrary to this argument, the language of the FCM Settlement cannot be construed to allow a result that would undercut the FCM Settlement's fundamental intent by purchasing less than ICR during the winter months. To be "fully integrated" into the FCM, the "distinct method" developed for Demand Resources must adhere to the basic structure of the FCM as outlined in

<sup>105</sup> DR Coalition Pleading at 4.

<sup>106</sup> DR Coalition Pleading at 4, NECPUC Pleading at 39.

<sup>107</sup> See DR Coalition Pleading at 3 and 4 and NECPUC Pleading at 39. The FCM Settlement provides that a "distinct method shall be developed to allow energy efficiency and demand response resources (other than Real Time Demand Response) to be fully integrated as Qualified Capacity in the Forward Capacity Market." FCM Settlement at Section 11.II.E.2.a.

the FCM Settlement, not the other way around. The composite offer is a distinct method for the participation of Demand Resources in FCM.

Additionally, novel issues would need to be resolved to accommodate summer-only Demand Resources, including how much should resources that only perform in the summer (or winter) should be paid. Because FCM is an annual market, the ISO would need to determine how the capacity of resources that only perform in a single season would be procured in the other season (*e.g.*, if 400 MW are procured in the summer, then 400 MW must be procured in the winter). The ISO would also need to determine whether load or the resource should bear such costs. Such questions go to the heart of the market design and should not be opened at this time. Attempting to address such issues now would re-open fundamental market design issues that have already been resolved in the FCM Settlement.

Similarly, CSG's proposal to allow up to 600 MW of summer-only Demand Resources to qualify in the first three auctions is also inconsistent with the fundamental design of the market. Like the proposal advanced by the DR Coalition, CSG's proposal would require a complete re-design of the market, undermining the FCM Settlement agreed to by the parties. CSG is concerned that the composite bid process "creates significant uncertainty and transaction cost."<sup>108</sup> CSG believes that allowing summer-only Demand Resources to qualify in the first three auctions would provide the ISO with information that would help to determine whether the composite offer process will work, and provide time to make any needed adjustments to allow summer-only resources permanently, if needed.<sup>109</sup> Summer-only Demand Resources would be

<sup>108</sup> CSG Pleading at 5.

<sup>109</sup> *Id.* at 7.

capped at offering up to 600 MW in the first three auctions. However, CSG's proposal is merely a variation of the DR Coalition's theme, and suffers from the same fundamental problems.<sup>110</sup>

Like CSG, the ISO "remains optimistic that composite resource offers will emerge as an effective solution."<sup>111</sup> Unlike CSG, however, the ISO does not believe that it is necessary to allow summer-only resources to offer into the initial auctions to determine whether the composite offer process will be effective. On the contrary, permitting summer-only resource offers would eliminate the need for composite offers, which would undermine the ISO's ability to evaluate the effectiveness of the composite offer process. The ISO stands ready to assist Demand Resources now and in the coming days and months with any composite bid issues.

**b. Contrary to Protestors' Claims, Composite Bids Will Enable Demand Resources to Participate in the FCM.**

The ISO has acknowledged the concerns regarding the eligibility of summer seasonal resources, and the ISO and stakeholders spent significant effort in designing the market to accommodate seasonal, as well as annual, Demand Resources. The market rules provide for composite bids by summer seasonal resources teamed with other resources. Composite bids allow seasonal resources to combine with other resources to submit capacity bids for the full 12 months, as a single resource. Composite bids enable separate resources to combine to maximize their annual value in the market (*e.g.*, by combining the higher winter output of a combined cycle plant with summer capacity from a Demand Resource that reduces air conditioning load).

Additionally, seasonal resources may participate in seasonal or monthly reconfiguration auctions.

<sup>110</sup> NECPUC endorses CSG's proposal and further maintains that if FERC does not accept it, then the Commission should require the ISO, through the stakeholder process, to develop a proposal allowing for summer-only bids in the FCA, without requiring the use of composite bids. NECPUC Pleading at 40. NECPUC's proposal, like that of the DR Coalition and CSG, should be rejected.

<sup>111</sup> CSG Pleading at 6.

Some protestors maintain that requiring composite bids will impede the participation of Demand Resources in the FCM. The DR Coalition argues that the composite bid structure “adds more complexity and an additional burden on summer season demand resources that is not needed.”<sup>112</sup> They argue that requiring summer resources to pair with winter resources will result in consumers paying for unneeded capacity, and that the burden of this process will force needed resources out of the market and lead to higher prices for all consumers.<sup>113</sup> The DR Coalition is also concerned that Demand Resources will lack negotiating leverage in dealing with winter-only resources.<sup>114</sup>

However, the DR Coalition fails to acknowledge that composite bids represent opportunities for both sides. The ISO believes that resources with single-season capability will have the incentive actively to seek to pair up with other resources to earn capacity revenues that would otherwise be “left on the table.” Furthermore, summer-only Demand Resources may pair up with any winter Qualified Capacity, including other Demand Resources (*e.g.*, Distributed Generation, Energy Efficiency and Load Management associated with space heating, and other winter-only processes such as snow-making), as well as with the additional winter Qualified Capacity from thermal generators. Given the value presented by these opportunities, both sides should be able to negotiate the offers to their mutual satisfaction, and beneficial partnerships should result.

The DR Coalition also argues that the composite bid process raises anti-competitive issues;<sup>115</sup> however, this claim is without merit and the Commission should not be distracted by it.

<sup>112</sup> DR Coalition Pleading at 10. *See also* CSG Pleading at 5 (the “concern . . . is that this requirement to ‘pair up’ creates significant uncertainty and transaction costs”).

<sup>113</sup> DR Coalition Pleading at 10.

<sup>114</sup> *Id.* at 12.

<sup>115</sup> *Id.* at 5, 11-12.

The DR Coalition maintains that “it is not clear how one of these partnering arrangements would work, particularly without requiring collusion.”<sup>116</sup> Yet, the protestors fail to explain how the offering of composite bids is any different from many other types of joint endeavors that market participants, including competitors, often pursue, such as the joint development of generating plants. Under the DR Coalition’s reasoning, such joint ventures could inherently constitute collusion because competitors would be sharing information related to the venture. The action of parties joining together to provide composite bids does not constitute collusion. Instead, these bidders, subject to the same competitive pressures as other resources participating in the FCM, will share the requisite information to devise a single bid and will be competing against other resources. Thus, it will be in the interest of composite bidders to submit the best competitive bid that they can offer. The DR Coalition’s arguments are unfounded.

In further addressing the feasibility of the composite bidding process, the DR Coalition states that the deadlines for partnering with other resources leave little time for “courting and consummation of a deal.”<sup>117</sup> The DR Coalition incorrectly notes that new capacity (including New Demand Resources) must submit composite offers by June 15, 2007, while existing capacity must submit composite offers by April 30, 2007.<sup>118</sup> As explained in the Transmittal Letter<sup>119</sup> and expressly provided for in Section III.13.1.5 of the proposed market rules, “Separate resources seeking to participate together in a Forward Capacity Auction shall submit a

<sup>116</sup> DR Coalition Pleading at 11. What is not clear is how entities that the DR Coalition has characterized as having unequal bargaining power are simultaneously deemed by the DR Coalition to have the incentive to work together in collusion. The DR Coalition offers an assortment of antitrust-type arguments in opposition to composite bidding. It claims that the composite bid process can create unequal bargaining power for winter resources, barriers to entry for Demand Resources, and sharing of competitive information regarding bidding strategy. DR Coalition Pleading at 4–5.

<sup>117</sup> DR Coalition at 11.

<sup>118</sup> CSG also confused the deadline for submittal of composite offers. CSG Pleading at 6.

<sup>119</sup> February 15 Filing at 19.

Composite Offer Form by the New Capacity Qualification Deadline.” Thus, all resources have until June 15, 2007 to submit composite offers. Moreover, the ISO has indicated its willingness to work with interested parties now, and in the coming days and months, to facilitate composite offers through such means as providing information and conducting workshops. The ISO will also be holding its annual demand response forum in early May, and ways to ensure that composite offers are successful will be a key part of the agenda.

The ISO understands that the composite offers are a new concept and will closely monitor the concept’s effectiveness. If it is not working as intended, the ISO will act as quickly as possible to resolve these problems without compromising the essential requirement that the FCA procure an annual capacity product. However, until at least one auction cycle is complete an initial auction cycle, it is premature to state this approach will not work.

**c. The Proposed Rules are Consistent with the Commission’s Policy of Encouraging Demand Resources**

The DR Coalition states that FERC should consider the composite bidding requirement in the context of the Commission’s broader agenda of encouraging Demand Resources.<sup>120</sup> The DR Coalition suggests that the proposed market rules impede participation by Demand Resources in the FCM, in contravention of FERC’s Demand Resource policy.<sup>121</sup>

The ISO and the stakeholders have spent hundreds of hours in working groups and meetings of NEPOOL market participants, state utility and environmental regulatory staff, and other interested parties deliberating the best way to ensure Demand Resources’ participation in the FCM in a way that is consistent with the FCM Settlement and its fundamental purpose of procuring sufficient capacity to maintain reliability. The stakeholder process utilized by the ISO

<sup>120</sup> DR Coalition Pleading at 13-14.

<sup>121</sup> *Id* at 13.

and the FCM rules themselves achieves the stated recommendations of FERC Staff regarding the accommodation of Demand Resources in wholesale markets:

Demand response deserves serious attention. [FERC] Staff recommends that the Commission: (1) explore how to better accommodate demand response in wholesale markets; (2) explore how to coordinate with utilities, state commissions and other interested parties on demand response in wholesale and retail markets; and (3) consider specific proposals for compatible regulatory approaches, including how to eliminate regulatory barriers to improved participation in demand response, peak reduction and critical peak pricing programs. Staff also encourages states to continue to consider ways to actively encourage demand response at the retail level. In particular, staff recommends that the Commission and states work cooperatively in finding demand response solutions.<sup>122</sup>

The market rules, including the composite bid element, should substantially increase the participation of Demand Resources in the market. The provisions for integrating Demand Resources into the FCM are as advanced as any market in the country, have been supported by the majority of the New England stakeholders, and are unprecedented in many respects. If the recent participation in the Show of Interest for Demand Resources is an indication, the rules have been very successful in attracting interest in participation in the first auction of Demand Resources with over 2200 MW. Nevertheless, the ISO has not taken the Demand Resources' concerns lightly, and will promptly address any issues that may actually materialize with respect to Demand Resources' ability to participate in the FCM. The ISO commits to monitor and revisit this issue if necessary.

##### **5. Public Systems “One Size Fits All” Argument Should be Rejected**

Public Systems argue that notwithstanding the language of Section III.B.3 of the FCM Settlement that states that “*Qualification criteria may vary based on the size, technology, complexity, et cetera of the Resource*”, the “qualification criteria” in the proposed FCM tariff

<sup>122</sup> Assessment of Demand Response and Advanced Metering, Staff Report, Docket AD06-2-000, August 2006 at 133.

provisions do not vary based on these factors.<sup>123</sup> Instead, they argue, those provisions set forth a one-size-fits-all process, with a uniform set of data to be provided, and the imposition of an obligation to provide that data on the identical time schedule.<sup>124</sup> The Public Systems maintain that requiring all facilities, regardless of type, to meet the same set of criteria on the same schedule fails to comport with the realities of how generation projects are in fact built, and is not in accordance with the ISO's intention that the design of the qualification process minimize barriers to entry.<sup>125</sup>

For example, they assert, it is neither sensible nor consistent with the FCM Settlement to require those seeking to build peaking facilities to demonstrate "site control" at the "Show of Interest Form" stage, Proposed Rule Section III.13.1.1.2.1(b), *i.e.*, roughly three years before the commencement of the relevant Capacity Commitment Period.<sup>126</sup> They maintain that while a baseload nuclear plant, for example, requires consideration of a large number of details and long lead time items, a peaking project can go from initial concept to on-line status in less than two years.<sup>127</sup> While conceding that the ISO's need for the data to conduct analyses is relevant, they maintain that this need is not the only factor that should be considered. They contend that treating all resources based on a single set of criteria and a single set of submission deadlines potentially creates barriers to entry, limits the amount of supply resources that will bid into the auction, and increases the likelihood of failed auctions and higher capacity market prices.<sup>128</sup>

<sup>123</sup> Public Systems Pleading at 5-6 (emphasis in original).

<sup>124</sup> Public Systems Pleading at 6.

<sup>125</sup> *Id.*

<sup>126</sup> Public Systems' Pleading at 6.

<sup>127</sup> *Id.* at 6-7.

<sup>128</sup> *Id.* at 7.

The Public Systems' protest concerning this issue should be rejected. The FCM Settlement does not require their approach to be adopted. Rather the very FCM Settlement provision they quote, Section III.B.3 of the FCM Settlement, states that qualification criteria *may* vary based on various factors such as size, technology, etc., not that such criteria *must* be based on those factors. Thus, the ISO was specifically given flexibility to consider whether and when to give weight to such factors.

Further, the ISO believes it is best to treat resources consistently. All resources in the FCM are competing to provide the same product, annual installed capacity, and should, if possible, be required to compete on a level playing field with no particular resource or resources enjoying any special advantages. Implementation of such an approach also is far simpler and less contentious than striving to set up a multitude of processes for the various resources in the market.

In addition, if anything, the example posed by the Public Systems would lead to the contrary result. Since nuclear units are difficult to site and require a long lead time, it might be argued that they should be relieved of the requirement to supply certain information at a particular time. In any event, since the process for permitting and constructing a peaking project is usually much simpler than for a baseload unit, a peaking project should have much less difficulty meeting the information requirements that apply equally to baseload facilities. If a potential peaking plant wants to participate in an auction to establish supply commitments three years in advance, it should do so on the same basis of other installed capacity resources. If it does not wish to participate in the main auction because of the ISO's modest information requirements, it can participate in reconfiguration auctions if it meets the requirements for them.

The Show of Interest Form requirements set forth in the proposed market rules do not constitute a significant or unreasonable barrier to entry for market participants. As noted above, over 15,000 MW of generating capacity has submitted Show of Interest Forms and deposits. However, given the concerns voiced by Public Systems, the ISO will monitor this issue and revisit the proposed market rules if necessary to address any issues.

**6. FirstLight's Contention that Pumped Storage Should Be Treated as Demand Response Must Be Rejected.**

The FirstLight Parties allege that the eligibility criteria for Demand Resources unduly prejudice large-scale load management projects like pumped storage hydroelectric facilities that are not located behind the end-use meter.<sup>129</sup> According to FirstLight, such a restriction is not required by the FCM Settlement, and is unlawful under Section 205(a) of the FPA. Pumped storage provides the same peak load reduction value effect for resource adequacy purposes as that offered by behind-the-meter energy storage devices and there is no rationale for different treatment.<sup>130</sup> FirstLight Parties claim the ISO's policy is contrary to the Energy Policy Act of 2005, which states that unnecessary barriers to participation by demand resources in energy, capacity, and ancillary services markets shall be eliminated.<sup>131</sup> FirstLight requests FERC to direct the ISO and NEPOOL to develop revisions to the market rules to permit pumped storage resources that result in verifiable reductions in aggregate peak demand by shifting such demand to off-peak hours to qualify as Demand Resources for purposes of participation in the FCM, and to have such revised provisions in place before the second FCA.<sup>132</sup> By way of background, the

<sup>129</sup> FirstLight Pleading at 1-2. The FirstLight Parties are FirstLight Power Resources Management, LLC, FirstLight Hydro Generating Company and Mt. Tom Generating Company LLC.

<sup>130</sup> *Id.* at 5.

<sup>131</sup> *Id.* at 6.

<sup>132</sup> *Id.* at 7.

FCM rules rate demand resources by the amount of load they reduce during certain on-peak hours. This reduction is defined as their Demand Reduction Value.<sup>133</sup>

There are four compelling reasons to reject FirstLight's request: (1) treating pumped storage as a Demand Resource would double count its capacity value, (2) pumped storage provides no Demand Reduction Value, (3) pumped storage is not a Demand Resource, and (4) if it were determined that pumped storage were a Demand Resource, such resources would be prohibited by the FCM Settlement from participating in the FCM.

**a. Treating Pumped Storage as a Demand Resource would Double Count its Capacity Value.**

FirstLight's argument appears to be that by shifting pumping operations from on-peak hours to off-peak hours, pumped storage projects are operating in the same way as a Load Management Demand Resource. This argument is nonsensical. The value that a pumped storage project provides is its ability to produce on-peak generation and reserves. As such, pumped storage projects that clear the FCA will be paid for the capacity they deliver as a generation resource. To also treat the same pumped storage projects as a Demand Resource would double count the capacity they bring to the electric system. Pumped storage projects produce on-peak generation and reserves by using off-peak electricity generated by other capacity resources to provide energy for pumping purposes – such off-peak pumping has no purpose other than storing water for the production of on-peak generation and reserves. Accordingly, while it is appropriate to compensate pumped storage projects as a generation resource, it is not appropriate to also compensate them as a Demand Resource.

**b. Pumped Storage Provides No Demand Reduction Value.**

<sup>133</sup> See Market Rule 1 Section 13.1.4.2.

In producing on-peak generation, for which compensation as a capacity resource is available, pumped storage projects would not normally consume on-peak electricity in the first place. Since it is irrational for a pumped storage project to use costly on-peak electricity to produce less valuable off-peak electricity, and since such projects do not consume and produce on-peak electricity simultaneously, pumped storage projects seldom, if ever, consume on-peak electricity for pumping purposes in the first place. Since it cannot be shown that such units produce an additional and verifiable reduction in on-peak demand, a Demand Reduction Value cannot be quantified.

**c. Pumped Storage is not a Demand Resource.**

FirstLight's contentions should also be rejected because pumped storage hydro is simply not a Demand Resource – pumped storage hydro is an on-peak generating resource that uses off-peak electricity as fuel. According to the proposed Market Rule, Demand Resources are defined as:

“... installed measures (i.e., products, equipment, systems, services, practices and/or strategies) *that result in additional and verifiable reductions in end-use demand on the electricity network in the New England Control Area during Demand Resource On-Peak Hours, Demand Resource Seasonal Peak Hours, Demand Resource Critical Peak Hours, Real-Time Demand Response Event Hours, or Real-Time Emergency Generation Event Hours...*”<sup>134</sup>

As mentioned previously, the value provided by a pumped storage project is its ability to produce on-peak generation and reserves. However, it produces this value by *increasing* load (albeit during off-peak hours) on the electric system, not by reducing load during relevant

<sup>134</sup> Market Rule 1, Section III.1.3 (Definitions).

performance hours. It is difficult to conceive how a resource that increases overall load and produces no additional and verifiable *reduction* in demand (whether in front or behind an end-use customer meter) during relevant performance hours can be thought of as a Demand Resource.

**d. If Defined as a Demand Resource, the FCM Settlement would Prohibit Existing Pumped Storage from Participating in the FCM.**

According to VIII.J.2 of the FCM Settlement Agreement, only Real-Time Demand Response Resources pursuant to Market Rule 1, Appendix E and “new (as of the Effective Date) demand side management installations (both energy efficiency and demand response, other than Real-Time Demand Response)” are considered qualifying capacity resources. According to Section III.E.1.2. of Market Rule 1, Appendix E, “Generating Resources that are already qualified as generating assets are not eligible to participate in the Load Response Program.” Hence, existing pumped storage units qualified as generating assets cannot be a Real-Time Demand Response Resource. Also, the existing pumped storage units in New England existed well before the June 16, 2006, the Effective Date of the FCM Settlement Agreement – therefore, such existing pumped storage units cannot qualify as “new demand side management installations.” If not a Real-Time Demand Response Resource and not a new demand side management installation, then the FCM Settlement Agreement would prohibit such resources from participating in the FCM as a Demand Resource.

**7. Reporting Requirements**

Capacity Suppliers argue that the ISO should increase the transparency of its use of its authority to reject offers or bids for reliability reasons.<sup>135</sup> They suggest that the ISO should be

<sup>135</sup> Capacity Suppliers Pleading at 18. *See also* CT DPUC at 34.

required to report, with explanations of reliability limitations: offers of new capacity rejected because of interconnection limitations under Section III.13.1.1.2; demand bids that were not included because the resource is required for reliability pursuant to Section III.13.4.2.2(d); and if a capacity supply obligation bilateral is rejected for failing the standards under Section III.13.2.5.2.5, the ISO should report such rejections in an annual filing or separately to the Commission with an explanation of the reliability limitation.

In addition, Capacity Suppliers argue that if the ISO has identified a transmission upgrade that could alleviate the reliability issue, the affected market participant should be informed. Moreover, no de-list bid in an FCA or any demand bid in a reconfiguration auction should be rejected for reliability reasons without considering alternative supply sources that could address the reliability issues. Capacity Suppliers suggest in their Protest several revisions to the market rules to achieve these results.<sup>136</sup> According to Capacity Suppliers, these changes will allow market forces to achieve the required level of resource adequacy while limiting the unnecessary “command and control” decisions by the ISO.<sup>137</sup>

The proposed revisions requested by Capacity Suppliers are unnecessary because the rules already require the ISO to provide the information they request. Section III.13.8.1. requires the ISO to file a list of resources rejected in the qualification process. The reasons for the rejection will be included in the filing and in the rejection notice sent to the applicant. Section III.13.8.2 discusses the reporting requirements after the conclusion of the auction. It requires the ISO to identify any de-list bids that are rejected for reliability and the reasons for such rejection. Section III.13.8.3 requires the ISO to report on the qualification process for annual

<sup>136</sup> *Id.* at 20-21.

<sup>137</sup> *Id.* at 22.

reconfiguration auctions. If a unit that seeks to submit a demand bid is rejected for reliability, that fact will be included in the required report.

In determining whether a unit is needed for reliability, the ISO will include all resources and transmission improvements that are committed to provide capacity for the year in question, which it believes are all alternatives to the supply resources that should be included. Units that are competing in the auction, but have not yet cleared or committed to provide capacity will not be included since there is no way of knowing whether such units will clear the auction. The combination of the Regional System Plan and the reporting on the reasons for rejection should meet the suppliers request that they be notified if a transmission improvement will meet the reliability need. For the foregoing reasons, the ISO's process for rejecting offers or bids for reliability reasons is sufficiently transparent to allow market forces to achieve the required level of resource adequacy.

#### **8. Intermittent Power Resources Should not be Permitted to Back a Capacity Export to an External Control Area**

Brookfield Energy argues that the prohibition on capacity exports by Intermittent Power Resources is a new limitation on such resources not contemplated by the FCM Settlement.<sup>138</sup> They state further that the prohibition runs against FERC's preference to allow de-listing and exports to prevent seams issues.<sup>139</sup> In their view, the exclusion of Intermittent Power Resources capable of meeting the market rules' de-listing standards and export requirements applicable to all resources unfairly targets Intermittent Power Resources by placing them at a competitive disadvantage to other resources that are free to sell their capacity to the highest bidder.<sup>140</sup> They

<sup>138</sup> Brookfield Energy Pleading at 4.

<sup>139</sup> *Id.* at 5.

<sup>140</sup> *Id.* at 6.

claim that the proposed prohibition is discriminatory, without justification, not just and reasonable and FERC should require the ISO to revise Section III.13.6.2.2 to eliminate the restriction on Intermittent Power Resources from backing capacity exports into neighboring control areas.<sup>141</sup> The ISO disagrees.

By their nature, intermittent resources differ from conventional resources. Their output fluctuates considerably and can go from zero to full output in a very short period, by definition, outside the control of the owner. Additionally, the level of their output is not easily predictable on a day ahead basis. Recognizing this, the rules contain an exemption from the requirement to offer into the day ahead energy market imposed on all other capacity resources. This exemption is important for a true intermittent resource to prevent exposing the resource to energy market penalties.

If a resource is truly intermittent the lack of control over it makes it inappropriate to permit them to back capacity export transactions. By definition, the resources in this category are resources whose output is uncontrollable and unpredictable. Given this definition, it is difficult to imagine how such a resource can commit to support any particular level of output weeks or months ahead. The market rules in both New York and New England require that units backing capacity exports be committed at the level of the capacity transaction each month, and that energy contracts supporting that capacity export be offered to both the day-ahead and real-time energy markets for the entire month. However, since intermittent resources are properly exempted from the day ahead offer requirement, it is not sensible to permit them to back exports which require a day ahead offer.

<sup>141</sup> *Id.* at 6- 7.

**B. The Commission Should Refrain from Acting On Issues that Are Not Ripe for Review or Are More Properly Addressed in a Separate Proceeding or Stakeholder Process.**

**1. The Commission Should Not Reject The Provision Requiring a Stakeholder Process to Consider Including De-List Bids Rejected for Reliability as Out-of-Market Capacity**

NECPUC and CT DPUC object to the proposed market rule provision that would create a process for considering whether the Alternative Capacity Price Rule should be applied to FCAs affected by de-list bids rejected for reliability reasons, which they believe is contrary to a provision of the FCM Settlement.<sup>142</sup> They assert that the ISO must follow the process laid out in the FCM Settlement for modification of the FCM Settlement’s terms prior to placing this issue before the Commission, and urge the Commission to strike the provision of the proposed rules that requires the ISO to make a filing prior to such modification. The Vermont Department of Public Service and Vermont Public Service Board (“Vermont Parties”) and the Massachusetts Department of Telecommunications and Energy (“Mass DTE”) argue this same point in their separate pleadings.<sup>143</sup> The ISO urges the Commission to deny these protests because they are not ripe for decision.

By way of clarification, Section III.13.2.5.2.5(f) does not bind the ISO to accept the proposition that de-list bids rejected for reliability reasons must be counted for purposes of the Alternative Capacity Price Rule. This provision requires the ISO to engage in a stakeholder process to determine whether adoption of this proposal is consistent with the FCM market

<sup>142</sup> NECPUC Pleading at 7; CT DPUC Pleading at 7. Several individual state Commissions joined NECPUCS’s protest and comments. Although the CT DPUC filed its separate voluminous protest and comments, that filing largely tracks the NECPUC filing. The other New England state commissions, with the exception of Rhode Island which has not even intervened, filed short pleadings referencing the NECPUC filing. The Connecticut Attorney General (“CT AG”) filed a plain vanilla intervention which only mentioned that it filed a court appeal of the Commission orders approving the FCM Settlement. The Mass AG filed a basic intervention without providing comments. The Maine Public Utilities Commission notes specifically in its filing its appeal of the underlying order approving the FCM Settlement, and the Commission’s acceptance of the “underlying FCM construct.”

<sup>143</sup> Vermont Parties Pleading at 3; Mass DTE Pleading at 5.

design. The ISO has not yet determined the answer to this question, and it will not be ripe for a conclusion by the ISO prior to the stakeholder process.

Moreover, this provision of the rules was adopted as an amendment by the NEPOOL Participants Committee with a unanimous favorable vote. It was a part of the total package of proposed rules that achieved the support of almost 80% of the NEPOOL Participants Committee. As such, it should not be summarily set aside without the opportunity to fully develop the legal and factual issues implicated in this proposal.

During the stakeholder process, the ISO will have the opportunity to learn the views of the entire spectrum of stakeholders, and the rationale for each position. At the end of the process, the ISO, thus fully informed, will submit the filing required by Section III.13.2.5.2.5(f).

The ISO requests that the Commission permit the stakeholder process to proceed in accordance with Section III.13.2.5.2.5(f), and to reject these protests. Participation in this process will not strain the resources of the ISO, as this proposal does not raise the magnitude of complexity of, for example, review of the queue as the method for addressing overlapping interconnection impacts, discussed below, which has a long history of conflict among market participants and state regulators. Permitting the stakeholder process to proceed will permit development of a full set of facts on which a decision will be made, and will grant appropriate deference to an amendment that garnered the unanimous support of the stakeholders and to the entire package of FCM rules, which enjoyed support from a broad spectrum of interests.

## **2. Ruling on the Queue Issue Would Be Premature**

### **a. The ISO Is Not Able to Re-design the Queue in the Time Frame Urged by the States**

NECPUC and CT DPUC argue that the market cannot operate efficiently with the first-come, first-served interconnection queue as the method for assigning priority in situations where

it is not possible to interconnect multiple generators at the same location absent costly, long lead time improvements to the transmission system. They state that a timetable should be established to create a new process that gives interconnection priority to resources that offer the lowest price in the FCA. They argue that giving priority to resources based on their position in the interconnection queue may cause the clearing price to be higher in the FCA than it otherwise would be and that the interconnection queue facilitates the exercise of market power by incumbent generators. They request that the Commission require the filing of a new rule that revises the generation interconnection queue process to integrate the FCM and the generation interconnection queue by the ISO no later than November 15, 2007, so that it will be in place by the second FCA.<sup>144</sup>

NECPUC and CT DPUC note that a super-majority of the NEPOOL Markets Committee approved an amendment requiring the ISO to develop a modified rule addressing overlapping impacts by the second FCA. They also request the appointment of a settlement judge to develop an alternative to reliance on the queue.<sup>145</sup> The Vermont Parties and the Mass DTE specifically but briefly argue this same point in their separate intervention/protests which join in the NECPUC filing.

From the protests, the ISO understands that of all of the issues related to FCM that remain to be resolved, redesign of the queue is the states' highest priority. As the ISO indicated in the February 15 Filing, the ISO agrees that this is an important issue. However, as detailed below, the ISO has concluded that even if the redesign of the queue were the ISO's top FCM-

<sup>144</sup> The states also argue that the history and purpose of the queue does not support the queue's role in resolving overlapping impacts. The ISO has never claimed that the queue should be the method of choice for addressing this issue. The question is not whether the queue was intended, and therefore can be used, for this purpose, but rather the timeframe within which a more workable alternative can be developed.

<sup>145</sup> In this regard, CT DPUC attached to its comments the presentation it made to the NEPOOL Markets Committee on January 24, 2007.

related priority after the implementation of the FCM itself, it would not be possible to meet the states' requested date.

NECPUC *et al.* argue that resolving the relationship between FCM and the interconnection queue can be accomplished by November 15, 2007 and that indeed Connecticut is well along the road towards a solution. As much as the ISO would like to agree, the ISO believes that these conclusions are unduly optimistic and do not reflect the complexity and contentious nature of the interconnection queue and the FCM. Each of these issues has a history of contentious and lengthy stakeholder processes; and the formulation of a substitute proposal that implicates both will necessarily compound the difficulty and extend the time for resolution.

The queue was developed as part of the Commission's open access policy in 888. Its application in "New England" was hotly contested and, among other major issues, the Bucksport decision established the Minimum Interconnection Standard for New England. The Commission has often noted that changing the pro forma Tariff has to have extremely strong support. To achieve the results the states seek will require full re-examination and consideration of interconnection standards, grandfathering, prioritization, deliverability, cost responsibility for system upgrades and numerous other issues. Issues related to the queue arose with respect to the generation interconnection process, which began with a Commission Advanced Notice of Proposed Rulemaking ("ANOPR") in 2001<sup>146</sup> and concluded with a Final Rule on Generator Interconnection Agreements and Procedures in July of 2003.<sup>147</sup> The ISO and NEPOOL filed in

<sup>146</sup> Advance Notice of Proposed Rulemaking ("ANOPR") on Standardizing Generator Interconnection Agreements and Procedures, Docket No. RM02-1-000 (October 25, 2001).

<sup>147</sup> Standardization of Generator Interconnection Agreements and Procedures, 104 FERC ¶ 61,103 (July 24, 2003).

response to the Commission's directive in January of 2004.<sup>148</sup> FERC did not rule on this until November of 2004.<sup>149</sup> Additionally, this proceeding required numerous other ISO compliance filings and responses to additional orders.

The Commission is also well aware of the circumstances surrounding the creation of a capacity market in New England. The Commission first ordered that a locational capacity market be created in its December 2002 order approving New England's Standard Market Design ("SMD")<sup>150</sup> and subsequently, in the Order issued in April 2003,<sup>151</sup> required the ISO to make a compliance filing creating a locational capacity market in New England in June 2004. The ISO made that filing<sup>152</sup> which started a regulatory process that was not completed until June, 2006 with the approval of the FCM Settlement.<sup>153</sup>

Reopening issues that require a complex, contentious regulatory and stakeholder process, such as the generation interconnection queue and the design of the capacity market, should be done with full awareness of their difficulty and the time it will take to resolve them. It will require significant effort by key members of the ISO staff to develop solutions to this problem and to lead the stakeholder effort to discuss these issues. This effort requires ISO personnel that understand how the generation interconnection queue currently works in New England, the FERC Pro-Forma Tariff version of the Interconnection Queue, the types of engineering studies

<sup>148</sup> New England Power Pool Participants Committee's Proposed Amendments to NEPOOL Tariff that comply with the Commission's Final Rule on the Standardization of Interconnection Agreements and Procedures, Docket No. ER04-433-000 (January 20, 2004).

<sup>149</sup> *New England Power Pool*, 109 FERC ¶ 61,155 (2004).

<sup>150</sup> *New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287 (2002), *order on reh'g*, 101 FERC ¶ 61,344 (2002).

<sup>151</sup> *Devon Power LLC, et al.*, 103 FERC ¶ 61,082 (2003).

<sup>152</sup> ISO New England Inc. Filing in Compliance with April 25 Order, Docket No. ER03-563-030 (March 1, 2004).

<sup>153</sup> *Devon Power LLC*, 115 FERC ¶ 61,340 (2006).

that must be done to successfully interconnect a generator, how the qualification process for Forward Capacity Market works and how the Forward Capacity Auction works.

However, the ISO personnel with these skills are engaged in a number of high priority projects and initiatives that cannot be delayed or postponed. For the Forward Capacity Market, Locational Forward Reserve Market and Connecticut Request for Proposal to succeed, generators must be able to interconnect. This requires that resources currently in the queue continue to have studies done and move along towards completion. This, in turn, requires a significant effort by the ISO's transmission planning staff. There are currently 81 generators in the interconnection queue representing over 10,000 MW of capacity. Seven feasibility studies, eighteen system impact studies and three facility studies are underway, and those efforts are only addressing a portion of the 10,000 MW in the queue.

These same system planning resources are also required for several key projects essential for either system reliability or to meet the recently approved FERC mandatory reliability standards. The New England East-West Solution Project ("NEEWS") which will significantly improve the ability to move power from east to west in New England, is well underway. In 2007 detailed transmission planning studies, project evaluations and certain reports, evaluations, and studies concerning the Springfield, Massachusetts portion of NEEWS and a review of the impact of possible requirements to put facilities underground in Connecticut must be done. The NEEWS project is only one piece of a region-wide effort to coordinate the ten year transmission plans of all of the region's transmission owners. This coordination effort by the ISO is being done pursuant to a NERC requirement.

The Southeast Massachusetts Area ("SEMA") has been the cause of significant uplift in the energy market because of the need for transmission system improvements. The ISO must

complete a short term upgrade report and analysis, identify possible market efficiency upgrades, and begin a long term upgrade analysis for SEMA in 2007. There is also a need to review, and as required, define improvements to the transmission system in the state of Maine. The Maine Power Reliability Program (“MPRP”) is underway to solve this problem to assure that Maine is able to reliably serve its customers and meet necessary system reliability criteria. The ISO must also lead the compliance effort related to FERC Order No. 890 which will require significant ISO and stakeholder resources to get to a NEPOOL Participants Committee vote in September for a FERC compliance filing in September. Order No. 890 touches all parts of the OATT, with the exception of the generator interconnection process.

The resource qualification work for the FCM auction is substantial and must be completed by the early fall of 2007. It also requires a significant number of transmission planning studies for the 105 show of interest applicants that include 80 "new" generators, (only half of which are in the generation interconnection queue), 15 imports, and 10 upgrades of existing generating resources. These analyses include thermal screening, short circuit screening and overlapping impact tests. Finally, there are a number of NERC standards with which the ISO must comply and the system planning resources must assist in that effort.

As this discussion makes clear, much thought should be given to how and when to tackle the important, but complex issue of improving the relationship between the interconnection queue and the FCM. The ISO has proposed to take time this spring and summer to fully discuss priorities and resource availability with the stakeholders to develop a realistic schedule that balances all of the important projects the ISO and the region’s stakeholders must accomplish. We request that the Commission deny NECPUC’s request for a settlement process and setting a

date to resolve this issue. Both of these requests are premature and could result in a misallocation of resources and delay of one or more of the important projects detailed above.

**b. The FCM Settlement Does Not Require a Resolution of the Queue Issue by November 15, 2007**

Several states argue that the FCM Settlement requires the ISO to prioritize addressing changes to the existing FERC-approved interconnection queue process to resolve overlapping interconnection impacts based on price rather than queue position.<sup>154</sup> The FCM Settlement states:

ISO[-NE] and the [NEPOOL] Reliability Committee shall work out specifics with respect to . . . selection criteria (including auction details) for multiple projects when only a subset of such projects can be selected in the FCA due to overlapping interconnection impacts.<sup>155</sup>

NECPUC further argues “while the FCM Settlement does not specify a date by which this action must be accomplished, it is settled law that performance must be within a reasonable time.”<sup>156</sup> In their view, a due date of November 15, 2007 is reasonable.

The legal authority cited by the states does not support the conclusion they urge. While it is true that courts have held that when a contract is silent as to the time for performance, the law will imply a reasonable time for performance, what is reasonable must necessarily depend on the facts. Further, it is well-settled that “[w]hen the contract is silent, principles of good faith . . . fill the gap.”<sup>157</sup> The meaning of “good faith” varies by context. Good faith performance or

<sup>154</sup> See e.g., NECPUC Pleading at 14-21; CT DPUC Pleading at 29-32; Mass DTE Pleading at 7-8; Vermont Parties’ Pleading at 5-6; NUSCO Pleading at 4.

<sup>155</sup> FCM Settlement, Section 11.II.B.3.c.

<sup>156</sup> NECPUC Pleading at 14.

<sup>157</sup> See, e.g., *Kaplan v. First Options (In re Kaplan)*, 143 F.3d 807 at 818 (3<sup>rd</sup> Cir. 1998) (citing *Kham & Nate's Shoes No. 2, Inc. v. First Bank*, 908 F.2d 1351, 1357 (7th Cir. 1990) (When the contract is silent, principles of good faith fill the gap. They do not block use of terms that actually appear in the contract.)).

enforcement of a contract “emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party.”<sup>158</sup>

The ISO submits that the time frame and process outlined in the February 15 Filing is reasonable given the facts and circumstances of this case, and demonstrates good faith performance on the ISO’s part. While the ISO agrees that addressing the interconnection queue process is a high priority and must be done in a reasonable time, as discussed elsewhere in this Answer, there are finite stakeholder and ISO resources to devote to the resolution of wholesale electric market issues and the effort to accomplish this must not be underestimated. Additionally, as described in some detail above, the resources to resolve this issue are critical to other high priority projects, including the implementation of the FCM itself.

In addition to the resource constraints that make meeting the proposed timeline infeasible, the demand for capacity in the first auction and the potential supply suggests that delaying beyond the states’ proposed timeline is reasonable and demonstrates good faith because the approach in the proposed rules is unlikely to result in increasing the auction price, as feared by the states. Projections show that there will only be a need for less than 200 MW<sup>159</sup> in the first FCA. This amount does not account for any additional capacity added during the remainder of the ICAP Transition Period. In fact, if all of the capacity, including imports and demand response that are now being paid in the ICAP Transition Period remain in the auction in 2010, there would be no need for additional capacity in the 2010 Capacity Commitment Period. There is also evidence that competition will be strong enough to provide any megawatts that are needed at a competitive price. There has been over 17,000 MW in Show of Interest Forms submitted for

<sup>158</sup> Restatement (Second) of Contracts, § 205a (1981).

<sup>159</sup> See 2006 Regional System Plan (October 26, 2006), available at <[http://www.iso-ne.com/trans/rsp/2006/rsp06\\_final\\_public.pdf](http://www.iso-ne.com/trans/rsp/2006/rsp06_final_public.pdf)>

the first auction, including over 2200 MW of demand response resources. The combination of a small demand and a large amount of supply leads to the conclusion that the likelihood of a unit included in the auction based on queue position having the effect of raising the clearing price is very small.

While the ISO agrees that sole reliance on the queue is not an ideal solution, it has been faced with a myriad of competing issues and has in good faith sought to establish a fair process that will allow each issue to be adequately and timely addressed. The protests demonstrate that for the states the establishment of a date certain for the ISO to file a substitute mechanism is of paramount importance. However, the ISO cannot in good faith commit to a date without reviewing the resources available to address the problem, estimating the time it will take to resolve the problem, and prioritizing the issue in the context of all of the issues facing the organization. To assure that any date agreed to is realistic, the ISO requested in its February 15 Filing the opportunity to convene a stakeholder process to further investigate a number of issues, and based on that investigation and discussion with stakeholders, develop a list of priorities for all outstanding FCM related issues and other issues. However, in recognition of the pressing nature of this matter, the ISO is pushing to accomplish the stakeholder discussions as quickly as possible and thereby accelerate the filing of its proposed priorities, which will include a schedule for meeting those priorities. The ISO is currently planning to meet with NECPUC and NEPOOL in April to discuss priorities and resource constraints within which the ISO must operate. Additionally, the ISO is seeking a meeting with NECPUC, the NEPOOL Committee Chairs, and the ISO in late April or early May. These meetings will begin a full discussion of the issues facing New England and will facilitate the ISO's filing of a proposed schedule of activities.

**c. No Alternative Is Readily Apparent**

The states indicate that “substantial work has already been done” in developing an alternative to reliance on the queue, and imply that it would not be time-consuming to develop an alternative.<sup>160</sup> However, this characterization overstates the level of development of any proposal to replace the queue and understates the issues involved with changing the queue. First, the ISO is only aware of one proposal that has been significantly developed, and that is the alternative presented by the CT DPUC at the January 22, 2007 meeting of the NEPOOL Markets Committee. A copy of the proposal was attached to the CT DPUC protest. However, that proposal prompted a number of questions among members of the NEPOOL Markets Committee. For example, the market participants questioned how under the CT DPUC proposal a System Impact Study would be performed, who would pay for it, and perform it; how the question of projects of different sizes would be sorted; how a project that does not intend to compete in the FCM can reserve its position for the future; among other issues. The CT DPUC did not have full answers for any of these questions.

The CT DPUC proposal, while an interesting beginning, is still in the conceptual stages. It implies fundamental changes in the manner in which the queue works and interconnection costs are allocated. As stated earlier, there are currently 81 generators that are in the existing Commission-approved queue. Any proposed new method for handling the queue would have to address the rights, if any, to be preserved by these generators. Such changes will elicit significant concerns on the part of stakeholders that will be difficult and time-consuming to resolve.

NECPUC’s protest provides additional evidence of this complexity. NECPUC’s proposal attempts to address as many issues as possible, but then notes that alternative

<sup>160</sup> See CT DPUC Pleading at 30.

approaches have been offered, including the possibility of creating additional interconnection queues. Thus, resolution of this issue will not simply entail the development of the CT DPUC proposal, but rather a choice among competing approaches and the subsequent development of the chosen alternative. Each can be expected to have its supporters and detractors, and each one will need to be developed before an ascendant proposal is identified. This will take time and, absent the ability to have the proper resources focus on this issue and this issue only, identification of an acceptable alternative cannot be accomplished within the time frame urged by the states.

For the reasons noted above, the ISO commits to accommodate the states' request to develop a better alternative, and simply requests that the Commission reject the states' position that the ISO should file a new proposal by a date certain. Instead, the Commission should permit the ISO to establish priorities in a process in which the stakeholders can have input.

### **3. LIPA's Protest Should be Rejected Because the Issues are Being Addressed in a Separate Pending Proceeding**

LIPA, in its protest, makes many of the same arguments it offered in response to the ISO's filing in a separate proceeding of a new methodology to establish ICR for the FCM.<sup>161</sup> These arguments were thoroughly addressed in the Commission's "Order Accepting Tariff Changes And Requiring Compliance Filing," issued February 28, 2007, in that proceeding and, thus, require no further action from the Commission at this time.<sup>162</sup>

In brief, LIPA filed a limited protest to the February 15 Filing claiming that the market rules do not implement the terms of FCM Settlement, which require provisions specifying where

<sup>161</sup> See *ISO New England Inc and the New England Power Pool Participants Committee proposed revisions to Market 1 relating to the Methodology for Calculating Installed Capacity Requirements*, Docket No. ER07-365-000; *Motion to Intervene and Protest of Long Island Power Authority*, Docket No. ER07-365-000 (January 17, 2007).

<sup>162</sup> ICR Order.

zonal separation is determined to exist, a process for exporting capacity both from or through an import-constrained zone over tie lines to external regions.<sup>163</sup> According to LIPA, such specification was required to ensure both the reliability of the New England Control Area and the openness and robustness of the FCM.<sup>164</sup>

LIPA maintains that the proposed market rules in effect require it to sell its contracted firm export capacity into the FCA and fail to honor bilateral exports through a constrained region.<sup>165</sup> The ISO's proposal, according to LIPA, is also inconsistent with the portions of the proposed market rules in its February 15 Filing that specifically address exports.<sup>166</sup> To facilitate exports as it agreed in the FCM Settlement process, LIPA claims the ISO could have simply proposed rules to implement the export mechanism detailed in ISO witness Mr. Mark Karl's testimony filed in the Locational Installed Capacity Market ("LICAP") proceeding.<sup>167</sup>

LIPA also protests the proposed market rules' failure to address the alleged disparate treatment of the curtailment of capacity imports and exports. LIPA requests that the Commission order the ISO to provide for consistent treatment of imports and exports in the supplemental filing required of the ISO by the ICR Order to establish a process for exports of firm capacity from New England through a transmission import-constrained zone to adjoining control areas. If the ISO discriminatorily curtails firm capacity exports ahead of native load, there will be a double-standard for capacity imports and exports and the result will be to discourage capacity

<sup>163</sup> LIPA Pleading at 1.

<sup>164</sup> *Id.* at 7.

<sup>165</sup> *Id.*

<sup>166</sup> *Id.* at 8.

<sup>167</sup> *Id.* at 9.

trading between the New England Control Area and neighboring control areas, including that of the New York ISO.<sup>168</sup>

LIPA's protest should be rejected because the Commission has already addressed these arguments and set forth a process for addressing them. Namely, in response to LIPA's arguments in the ICR case, the Commission found as follows:

We agree with LIPA that the proposed rules in the instant filing do not provide a process for an Export through an import-constrained zone over tie lines to external regions, as required by the FCM Settlement Agreement. We disagree with ISO-NE that merely excluding such de-listed export capacity from the capacity that may be used to satisfy the ICR and Local Sourcing Requirement is sufficient to meet the FCM Settlement Agreement's requirement. While such exclusion would ensure that New England does not rely on exported capacity in meeting its ICR and Local Sourcing Requirement, as ISO-NE argues, that result does not provide a process to allow entities to export capacity through import-constrained zones.

In the ICR Order, the Commission set forth a process for resolving LIPA's issues and ordered the ISO to make a compliance filing within 180 days of the issuance of that order. To this end, the Commission stated:

We will not specify in this order how the FCM Settlement Agreement's requirement must be satisfied, but we will require that ISO-NE file to propose a process for such exports within 180 days of the date of this order.<sup>169</sup> We do not agree with what appears to be LIPA's recommendation to increase the Local Sourcing Requirement of the import-constrained area by the amount of the export at no cost to the exporter. To the extent that such capacity exports involve use of constrained transmission capacity, the exporter should pay a just and reasonable price for the transmission capacity.

Given that the Commission has already addressed this issue in a separate proceeding, the ISO believes that no further action should be taken by the Commission in the instant proceeding.

#### **4. Reliability Agreements**

<sup>168</sup> *Id.* at 11.

<sup>169</sup> The ICR Order renders moot LIPA's request for a technical conference.

NECPUC and CT DPUC “strongly support” the ISO’s approach to reliability agreements under the FCM. They believe that such agreements should be transparent and extraordinarily rare and that compensation thereunder should be based on only the unit’s going-forward costs. Further, they suggest a clarification of the rules to specify the costs that are properly recoverable.

Massachusetts Municipal Wholesale Electric Company (“MMWEC”) and Connecticut Municipal Electric Energy Cooperative (“CMEEC”) (collectively, “Public Systems”) also support the ISO’s determination to carefully limit the costs included in reliability agreements, and suggest that a number of issues be addressed, including:

- Once FCM is in place, the need for reliability agreements should be reduced drastically, as it should become even more challenging for generators to demonstrate financial eligibility for reliability agreements.
- Where the ISO finds that a de-list bid should be rejected for reliability reasons, the FCM market rules will provide ample opportunity for that need to be addressed well before a reliability agreement becomes necessary because market participants will have several years to determine how best to address reliability needs that are currently being met by resources that seek to de-list.<sup>170</sup>
- Allowing for the elimination, prior to the Capacity Commitment Period, of reliability-related needs identified at the qualification stage is in accord with FERC precedent.
- Any reliability agreement executed should be for only a single year’s duration.<sup>171</sup>
- FERC, in determining the just and reasonable rate paid should be mindful that the FCM will be undermined if generators needed for reliability have the option to receive the higher of a traditional cost-of-service rate or a market-based rate. A just and reasonable rate should be limited to net risk-adjusted going-forward costs.<sup>172</sup>

<sup>170</sup> Public Systems Pleading at 12.

<sup>171</sup> *Id.* at 13.

<sup>172</sup> *Id.* at 14.

PSEG Power LLC and PSEG Energy Resources and Trade LLC (jointly “PSEG”) argue that new reliability agreements should be allowed, and that FERC should clarify that the rejection of a de-list bid – especially a Permanent De-List Bid- due to reliability reasons does not foreclose the unit owner from seeking a reliability agreement. PSEG also complains that the proposed rules do not state how the just and reasonable rate for a unit whose de-list bid has been rejected for reliability purposes will be calculated and whether such rate will provide for recovery of full cost of service.

PSEG states that any modifications to current Reliability Must-Run (“RMR”) contract provisions are beyond the scope of this proceeding.<sup>173</sup> It explains further that the FCM Settlement only addresses the termination of existing RMR agreements when the FCM auctions commence and ICAP Transition Period ends, but does not preclude new reliability agreements.<sup>174</sup> While FERC orders did state that RMR agreements should be rendered unnecessary once a LICAP mechanism is in place, it did not preclude subsequent reliability agreements.<sup>175</sup> Precluding future reliability agreements is an improper and illegal confiscation of property, and the ISO’s suggestion that the FCM design is incompatible with the compensation mechanism for reliability agreements is unsupported.<sup>176</sup>

The ISO requests that these arguments be set to the side pending completion of a stakeholder process. In its February 15 Filing, the ISO noted:

The proposed rules do not resolve how such a just and reasonable rate will be determined, the form of the Reliability Agreement providing for such just and reasonable rates or the process of obtaining such a Reliability Agreement. To accomplish these

<sup>173</sup> PSEG Pleading at 3.

<sup>174</sup> *Id.* at 5.

<sup>175</sup> *Id.* at 6.

<sup>176</sup> *Id.* at 7.

ends, the ISO anticipates revising Sections I.3.9 and I.3.10 of the Tariff and the existing market rules (many of which are in Appendix A of Market Rule 1) dealing with Reliability Agreements and compensation thereunder. This major effort will also require significant stakeholder review, ISO resources and Commission approval.

The issues raised in these pleadings as to the form of reliability agreements, the rate to be paid thereunder, and the process are not ripe for a decision on the merits at this time.

Accordingly, the ISO urges the Commission to refrain at this time from rendering an advisory opinion on what those standards may be.

### **C. Clarifications**

#### **1. FCA Mechanics**

The CT DPUC and NECPUC have stated that FERC should require the ISO to clarify the rules on FCA mechanics and should direct the ISO to file under Section 205 any FCA bidder manuals (which should be subject to stakeholder scrutiny) with FERC.<sup>177</sup> The ISO requests that the Commission grant this request in part and clarify the mechanics of intra-round bidding.

The CT DPUC and NECPUC state that clarification is required regarding the rule that a capacity resource participating in the FCA must have included such offers in the form of a supply curve (up to five price-quantity pairs). NECPUC states that the ISO apparently does not intend that during every round of the FCA, every offer must be in the form of a supply curve with multiple price-quantity pairs. The ISO agrees, and requests that the Commission permit this clarification.

The CT DPUC and NECPUC have also stated that the rules associated with the FCA do not convey the actual way the descending clock auction will work.<sup>178</sup> In their view, the rules

<sup>177</sup> See e.g. CT DPUC Pleading at 45.

<sup>178</sup> NECPUC Pleading at 35-36. See also CT DPUC Pleading at 45-46.

sometimes confuse “offers” and “bids” and they offer a specific example of ambiguity created by such confusion.<sup>179</sup> In the specific example, the ISO believes that the terms are properly used.<sup>180</sup> However, the ISO is receptive to the states' broader point that more specificity with respect to auction mechanics is desirable, and intends to develop "user-friendly" manuals to address the auction mechanics so as to eliminate any confusion among the stakeholders.

As these manuals are developed, the ISO will carefully review whether any of the provisions constitute rates, terms or conditions of service, and make a determination as to whether the manuals, or any part of them, need to be filed with the Commission. However, prior to their development and completion, it would be premature to make a determination as to whether the manuals need to be filed.

## **2. CTRs**

Public Systems state that as part of the process of determining how the CTR-related benefits will be flowed through to CTR holders, the ISO should consider and address the interface between CTRs that are not allocated based on PPU Entitlement ownership or through other “special” allocation arrangements and self-supplied resources.<sup>181</sup> In accordance with the Settlement, the resources that can be used toward satisfying a load serving entity’s local sourcing requirement are those resources that are located in the same capacity zone as the associated load or pool planned units with a special allocation of CTRs. Any additional CTRs allocated to an LSE are based solely on its load serving obligation and are not dependent on entitlements in any

<sup>179</sup> *Id.* at 36.

<sup>180</sup> Throughout the transmittal letter and market rules, the ISO carefully uses the noun “bid” to refer to de-list bids and “offer” to refer to supply offers. However, in the instance cited by the CT DPUC and NECPUC, the ISO is using the verb “bid” to refer to an action taken with reference to an Existing Generating Capacity Resource.

<sup>181</sup> Public Systems Pleading at 10.

particular resource. As such, these additional CTRs can not be used to meet a local sourcing requirement.

### **3. 1385 Cable**

The CT DPUC asserts that in mapping external nodes through which imports may flow, the ISO identifies the Cross Sound Cable but, without explanation, omits the 1385 Cable. The CT DPUC requests the Commission to “require clarification from ISO-NE on this point.”

The ISO provides the following clarification. The ISO is working to allow the use of the 1385 line as a separate scheduling node in the energy market. The rules governing use of 1385 do not permit the use of the 1385 Cable for capacity contracts. Flows on this line are subject to frequent interruption based on operating conditions and their impact on the rest of the New York New England interface and thus cannot be relied upon to provide capacity as a separate path.

### **4. Ability to Retire**

As provided in the proposed market rules, a de-list bid that is rejected will be treated as existing capacity and remain in the auction until the price drops to 0.8 time CONE and it submits a de-list bid. Exelon argues that if a generator is unwilling to accept the INTMMU rejection of a bid and insertion of unit into the auction at a zero price, the generator should be allowed to opt out of the market entirely and retire the unit. According to Exelon, the ISO should not be allowed to force generators to participate in a market at a loss - if a unit is needed for reliability it should be paid under a reliability agreement.<sup>182</sup>

With respect to retirement, the ISO clarifies that under the FCM market rules, a unit may retire prior to the FCA for a given Capacity Commitment Period. If it chooses to do so, the unit will not be entered into the FCA and its capacity will be replaced. Once a unit has taken on a

<sup>182</sup> Exelon Pleading at 4.

capacity commitment in the auction, however, it should not be permitted to relieve itself of its obligation by retiring. The market design, with its minimal credit requirements and requirement of physical rather than financial capacity, is not designed to permit units to retire after taking on a capacity obligation into the FCM.

#### IV. CONCLUSION

For the foregoing reasons, the ISO respectfully requests that the Commission: (i) grant the ISO's *Motion for Leave to Answer*; and (ii) reject the protests and comments discussed herein in their entirety.

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Dated: March 23, 2007

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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.2010 (2006), upon each person designated on the official service list in this proceeding as compiled by the Secretary of the Federal Energy Regulatory Commission.

Dated at Washington, D.C., this 23rd day of March, 2007.

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/s/ Sherry A. Quirk  
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