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April 21, 2008

VIA ELECTRONIC FILING

The Honorable Kimberly D. Bose
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, DC 20426

Re: *Wholesale Competition in Regions with Organized Electric Markets*; FERC
Docket Nos. RM07-19-000, AD07-7-000; Comments of NEPOOL Participants
Committee on the NOPR on Wholesale Competition in Regions with Organized
Electric Markets.

Dear Secretary Bose:

The New England Power Pool (“NEPOOL”) Participants Committee hereby submits
electronically its comments for consideration by the Commission in the above-captioned dockets.

Respectfully submitted,

Michelle Gardner,
Counsel to the NEPOOL Participants
Committee

cc: Persons identified on the Service Lists in the captioned dockets

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

Wholesale Competition in Regions)
with Organized Electric Markets)

Docket Nos. RM07-19-000
AD07-7-000

**COMMENTS OF NEPOOL PARTICIPANTS COMMITTEE ON THE NOPR
ON WHOLESALE COMPETITION IN REGIONS
WITH ORGANIZED ELECTRIC MARKETS**

(April 21, 2008)

The New England Power Pool (“NEPOOL”) Participants Committee¹ offers these comments for consideration by the Commission in response to the Notice of Proposed Rulemaking titled “Wholesale Competition in Regions with Organized Electric Markets,” which was issued by the Commission in the above-captioned dockets on February 22, 2008 (the “NOPR”). The NOPR proposes amendments to the Commission’s regulations to reform the operation of wholesale electric markets on four specific topics. NEPOOL had previously filed comments in response to the Advance Notice of Proposed Rulemaking (the “ANOPR”)² in this proceeding and does not wish to repeat the same comments here, as applicable, other than to note in general that such comments contain extensive and useful background information regarding the topics raised in the ANOPR and NOPR as they apply to the New England region.³

¹ Capitalized terms used but not defined in this filing are intended to have the meanings given to such terms in the Second Restated New England Power Pool Agreement (the “Second Restated NEPOOL Agreement”), the Participants Agreement, or the ISO New England Inc. Transmission, Markets and Services Tariff (“ISO-NE Tariff”). Market Rule 1 is Section III of the ISO-NE Tariff.

² *Wholesale Competition in Regions with Organized Electric Markets*, Advance Notice of Proposed Rulemaking, 72 Fed. Reg. 36,276 (July 2, 2007), FERC Stats. & Regs. ¶ 32,617 (2007).

³ See NEPOOL Comments filed on September 14, 2007 in Docket Nos. RM07-19 and AD07-7 (“NEPOOL ANOPR Comments”).

I. INTRODUCTION AND BACKGROUND

The NOPR proposes amendments to Commission regulations under the Federal Power Act in four areas: (1) demand response and market pricing during a period of operating reserve shortage; (2) long-term power contracting; (3) market-monitoring policies; and (4) the responsiveness of RTOs and ISOs to stakeholders and customers, and ultimately to consumers who benefit from and pay for electricity services. In the NOPR, the Commission states that its proposals are designed to ensure just and reasonable rates and to remedy undue discrimination and preference and to improve the efficiency of wholesale competition in regions with organized markets.⁴ The NOPR is the next step in the Commission's efforts to meet these goals, following the three conferences held by the Commission on wholesale competition in 2007 and the record developed in this proceeding from the comments received in response to the ANOPR.

NEPOOL provided the forum for regional discussions of these issues and for identifying and articulating the positions of the market participants. NEPOOL is a voluntary association organized in 1971 pursuant to the New England Power Pool Agreement, and has grown to include more than 350 members. The Participants include all of the electric utilities rendering or receiving service under the Tariff, as well as independent power generators, marketers, load aggregators, brokers, consumer-owned utility systems, end users, developers, demand resource providers, and a merchant transmission provider. Pursuant to revised governance provisions accepted by the Commission,⁵ the Participants act through the NEPOOL Participants Committee. The Participants Committee is authorized by Section 6.1 of the Second Restated NEPOOL Agreement and Section

⁴ NOPR at P 4.

⁵ See *ISO New England Inc. et al.*, 109 FERC ¶ 61,147 (2004).

8.1.3(c) of the Participants Agreement to represent NEPOOL in proceedings before the Commission. NEPOOL is the principal stakeholder organization for the New England RTO.

Due to the interest in the region on the topics in the ANOPR and NOPR, NEPOOL organized an open stakeholder process for that dialogue, and formed special working groups specifically to review the issues in the ANOPR (the “ANOPR Working Group”) and the NOPR (the “Competition NOPR Working Group”). This process included representation from state regulatory commissions, ISO New England Inc. (“ISO-NE”), and all six Sectors. The Competition NOPR Working Group, which benefited from the extensive work already done by the ANOPR Working Group the previous year, held meetings for purposes of discussing the comments contained herein on March 20, and March 24, 2008. The Competition NOPR Working Group and NEPOOL Counsel reported on the NOPR and received additional feedback at the March Markets Committee meeting. The Participants Committee unanimously approved the substance of these comments at its April 4, 2008 meeting, with a number of abstentions from Participants who had more to say than NEPOOL on specific topics.

That broad NEPOOL support was achieved principally through common acknowledgement of and appreciation for the Commission’s efforts to enact improvements in the overall operation of the organized wholesale markets. NEPOOL comments have been distilled to those points on which there is consensus and do not reflect additional views voiced by some market participants and representatives of state regulatory agencies that go further on some points but without the same broad support. Further, the much appreciated participation by state regulator representatives was with the understanding that such participation was to inform both market participants of the perspectives of regulators and regulators of the perspectives of market participants. The ultimate positions of some market participants and state regulators will be reflected in statements, if any, that

they file with the FERC. Accordingly, the FERC is likely to receive from the region comments from entities within New England that express their separate views, notwithstanding a 100% vote in favor of NEPOOL's views.

II. DEMAND RESPONSE AND MARKET PRICING

i. Introduction

The Commission has requested comments on a number of proposals designed to eliminate barriers to the participation of demand response resources in organized electric wholesale markets, including the electric energy and ancillary services markets, and to ensure that demand response is treated comparably to other resources.⁶ NEPOOL supports the Commission's efforts to expand the participation of demand resources in wholesale energy markets. In many respects, New England is a leader in its efforts to increase the participation of demand resources in ISO-NE's wholesale energy markets. Stakeholders in New England have approved, and the region has now implemented, the Forward Capacity Market ("FCM"), which fully incorporates a wide range of demand resources (including demand response and energy efficiency resources) into its design and seeks to treat such resources on a more comparable basis with traditional capacity supply resources. Demand resources are eligible to set the Forward Capacity Auction ("FCA") clearing price, and will receive compensation and performance obligations more comparable to supply resources.

Based on the results of the first FCA, the FCM is eliciting a significant increase in new demand-side resources. According to the first FCA Results Filing, which was filed by ISO-NE with the Commission in March,⁷ "[a] total of approximately 1,813 MW of capacity from new resources secured Capacity Supply Obligations in the auction. Of that amount, about 1,188 MW

⁶ NOPR at P 26.

came from New Demand Resources. Additionally, 1,366 MW of Existing Demand Resources were selected in the auction.”⁸ These figures indicate that the FCM is working as intended to provide incentives and opportunities for demand resources to participate in that market.

As a further enhancement to this market, in compliance with FERC’s order approving the Market Rules for the FCM,⁹ the ISO-NE had initiated a stakeholder process through the NEPOOL Markets Committee to review the existing rules for participation of resources with varying seasonal capabilities, particularly summer-only or winter-only demand resources, to examine the desirability of any modifications to the current composite offer process.. As a result of that process, ISO-NE and NEPOOL concluded that the most appropriate course of action at this time would be to improve upon the existing timelines used in the composite offer submittal process, which process allows these seasonal resources to combine to submit a year-round offer in the FCM, and to provide an electronic bulletin board to allow those with excess summer or winter capacity to post availability. Such conclusions were contained in the “Report on Seasonal Resources” filed by ISO-NE with the Commission in February.¹⁰ As noted in that report, such changes are currently scheduled to be filed with the Commission to be effective for the third FCA.

The market rules in New England also allow demand resources to participate in the energy markets through two price-activated load response programs, the Day-Ahead Load Response Program and Real-Time Price Response Program. These programs provide incentives for interruptions in response to wholesale market prices. In particular, the Real-Time Price Response

⁷ See ISO-NE, Forward Capacity Auction Results Filing, filed in Docket No. ER08-633 on March 3, 2008 (“FCA Results Filing”).

⁸ FCA Results Filing at 5.

⁹ See *ISO New England Inc.*, 119 FERC ¶ 61,045 at P. 152 (2007) (“April 16 Order”).

Program provides for voluntary interruptions when the forecasted hourly real-time Locational Marginal Price (“LMP”) is greater than or equal to \$100/MWh. The Day-Ahead Load Response Program offers an additional incentive for voluntary interruptions during the Day-Ahead Energy Market. Offers as part of the Day-Ahead Load Response Program are evaluated after the Day-Ahead Energy Market has cleared. Offers to interrupt that are lower than the Day-Ahead LMP will clear in the Day-Ahead Energy Market and be paid the Day-Ahead LMP for such interruption.¹¹

These two programs are in addition to the three reliability-activated programs currently administered by ISO-NE: (1) Real-Time 30-Minute Demand Response Program, which requires a response within 30 minutes of instructions to interrupt; (2) Real-Time 2-Hour Demand Response Program, which requires a response within two hours; and (3) the Real-Time Profiled Response Program, which allows a similar interruption within two hours from aggregations of end-use customers. These three programs provide compensation to demand response resources that are able to interrupt during system reliability events, or, more specifically, able to interrupt in accordance with ISO-NE’s Operating Procedure No. 4, which establishes criteria and guidelines for actions during capacity deficiencies.¹²

¹⁰ See ISO-NE, Report on Seasonal Resources, filed in Docket Nos. ER07-546-012 and ER07-938-001 on February 29, 2008.

¹¹ Resources with cleared Day-Ahead Energy Market offers that show deviations in the Real-Time Energy Market will be settled with the Market Participant at the Real-Time LMP. The Commission recently accepted market rules changes to the Day-Ahead Load Response Program design to more accurately tie payments under that program to actual demand response. *ISO New England Inc.*, 123 FERC ¶ 61,021 at P 63 (2008). Based on additional consideration, ISO-NE recently filed yet another market rule change to the Day-Ahead Load Response Program, which does not have the support of NEPOOL. See ISO-NE, Heat-Rate Revision for Day-Ahead Load Response Program, filed in Docket No. ER08-830-000 on April 15, 2008 (“ISO-NE DALRP April Filing”).

¹² See ISO New England Inc. Operating Procedure No. 4 titled “Actions During a Capacity Deficiency” available at: http://www.iso-ne.com/rules_proceeds/isone/op4/op4_rto_final.pdf.

All of New England's existing load response programs, including the two price-activated programs, are currently set to expire on May 31, 2010, with the objectives of the three reliability-activated programs being superseded by the FCM.¹³ The market rules do provide, however, for an additional stakeholder process to consider whether programs for energy-based resources should continue beyond the commencement of the FCM. ISO-NE has stated its intention to begin this process in October of 2008 and has committed to file a report with the Commission by February 16, 2009 detailing its decision to file with the Commission either to terminate or to continue the Load Response Programs.¹⁴ To the extent that a decision is made to continue such programs, ISO-NE has stated that the February 2009 filing will include a schedule for developing market rules, which would be filed with the Commission in time to allow the pertinent programs to continue uninterrupted beyond May 31, 2010.

Further, the current New England market rules allow for certain demand resources to participate in the Forward Reserve Market and the real-time reserve market, with ISO-NE stating its intent to evaluate further opportunities to integrate such resources into the markets. The market design for the region's ancillary services markets provides opportunities for demand response resource participation in those markets, although there are certain size restrictions at present. In addition, a pilot program administered by ISO-NE has been underway since October 2, 2006, with a second phase to begin in November 2008, to evaluate how to incorporate smaller demand response resources (i.e., those less than 5 MW in size) into the region's new ancillary services markets. The

¹³ See Section III.E.1.3 of Market Rule 1 noting that all Demand Response Programs are set to expire on May 31, 2010 and that consideration of such programs "for energy-based resources beyond May 31, 2010 is subject to further study and consultation with NEPOOL stakeholder and state utility regulatory agencies."

¹⁴ See ISO-NE DALRP April Filing at 6-7.

purpose of that program is to fully integrate demand response into the region's operating reserve markets by 2010.

There are many complexities involved and work left to be done in New England to ensure full integration and comparability of such resources in these markets. NEPOOL is committed to working with ISO-NE to enhance the opportunities for demand response participation in all of the region's wholesale electric markets on a comparable basis to supply resources. The ongoing stakeholder efforts to evaluate the Load Response Programs and the participation of resources with varying seasonal capabilities in the Forward Capacity Market are two examples of that commitment. NEPOOL welcomes the Commission's decision to hold a technical conference regarding further reforms to increase demand response participation in wholesale markets and NEPOOL Participants look forward to participating in that effort.¹⁵ With that perspective, NEPOOL summarizes in this section its comments on the specific proposals offered by the Commission.

ii. Ancillary Services Provided by Demand Response Resources

The Commission proposes for comment a requirement that RTOs/ISOs accept bids from demand response resources in their ancillary services markets (spinning reserves, supplemental reserves, energy imbalance, and regulation and frequency response), comparable to other resources, provided that such resources are technically capable and submit a bid under the generally-applicable bidding rules at or below the market-clearing price.¹⁶ NEPOOL agrees with the Commission's statement that some forms of demand response are well-suited to providing ancillary services.

¹⁵ NOPR at P 95.

¹⁶ NOPR at P 56.

NEPOOL notes that ISO-NE has traditionally relied primarily on generating resources to satisfy operating reserve requirements. At the present time, the Forward Reserve Market and real-time reserve pricing already allow for certain demand resources, i.e. Dispatchable Asset Related Demands or “DARDs,” that are 5 MW or larger to participate in these markets by providing supplemental reserves. Only Dispatchable Asset Related Demands (“DARDs”), under market rules that were designed as part of the Ancillary Services Market (“ASM”) project,¹⁷ are allowed to participate directly in the reserves markets in a manner comparable to traditional suppliers. DARDs, which must be at least 5 MW in size and meet certain technical requirements, such as proper telemetering and ability to follow ISO-NE dispatch instructions, are allowed to make demand bids in the energy and reserve markets and are eligible to set LMPs. DARDs are not eligible to participate in any of the existing demand response programs. The DARDs that currently participate in this market are primarily pumped storage units, which are not included in the ISO-NE Tariff definition of Demand Resources, even though this may not always be the case in the future.

Given that the typical demand response resource in the New England Control Area is less than 5 MW, ISO-NE is currently administering a pilot project called the Demand-Response Reserves Pilot Program (the “DRR Pilot”) (also referred to as the Small Resource Reserves Pilot Program), which was accepted by the Commission,¹⁸ to determine the ability of additional demand resources (less than 5 MW) to participate in the New England operating reserve market. One of the objectives of the DRR Pilot is to determine the size, telemetry, metering, and bidding requirements of such demand-response resources to provide reserves. The DRR Pilot was established to

¹⁷ See *New England Power Pool and ISO New England Inc.*, 115 FERC ¶ 61,175 at P 7 (2006) (“May 12 Order”).

determine the abilities of demand resources to respond to reserve-activation events, as well as to evaluate the technologies necessary to enable such response. The DRR Pilot tests whether certain resources can reliably provide 30-minute and 10-minute Operating Reserve services, as compared to off-line and on-line generating resources. According to ISO-NE, several different demand resources have participated in the DRR Pilot, including weather-sensitive loads, non-weather-sensitive loads, emergency generation, and load-reduction resources.¹⁹

ISO-NE recently published and discussed with the NEPOOL Markets Committee at its April 8-9, 2008 meeting its findings from the DRR Pilot and its proposal to fully integrate demand response into the operating reserve market by June of 2010.²⁰ As part of its initial findings, ISO-NE concluded that the DRR Pilot had value, but that more needed to be learned, including how to measure how much demand response can be provided on a daily basis. ISO-NE proposed a Phase II of the DRR Pilot, which would run from October 2008 through May 2010 and would have as its purposes to: (1) finalize the requirements for communication, dispatch, metering, and telemetry sufficient to provide operating reserves; (2) implement identified lower-cost communications and telemetry solutions; and (3) integrate communications infrastructure with operations and market systems. Market rules for this program are scheduled to be filed with the Commission in early July.

In addition, as discussed recently with NEPOOL, ISO-NE is also planning to initiate another pilot program in November of 2008 for approximately 18 months that would evaluate the ability of

¹⁸ *Letter Order Accepting ISO New England Inc.'s Filing of 1st Revised Sheet 7014 et al. to FERC Electric Tariff, and Amendments to Appendix E of Market Rule 1 to Establish a Demand-Response Reserve Pilot Program*, FERC Docket No. ER05-1450-000 (Nov. 28, 2005).

¹⁹ ISO New England Inc., 2006 Annual Markets Report at P 118 (June 11, 2007). Available at http://www.iso-ne.com/markets/mkt_anlys_rpts/annl_mkt_rpts/index.html.

²⁰ A copy of the ISO-NE's presentation describing the DRR Pilot can be found on the ISO-NE website at: <http://www.iso->

non-traditional generating resources, such as demand response or new technologies, to provide regulation and frequency response.²¹ The “Non-Generation Based Regulation Pilot Program” was discussed with the NEPOOL Markets Committee at its March 11-12, 2008 meeting and market rules for this program are expected to be filed with the Commission in late August or early September.

NEPOOL agrees in general with the Commission’s concern that co-optimized markets, such as the joint energy-ancillary services market in New England, may provide disincentives for participation by demand response resources or other types of technologies. Certain resources, not just limited to demand response resources, may be unable, for technical or economic reasons, to offer into the energy markets without any restrictions or limitations. The Commission proposes the implementation of bidding limits for demand response resources in these markets to minimize the risk that these resources would be called upon too frequently or for too long a period.²² NEPOOL does not support, at this time, the imposition of these limits without providing the region an opportunity to more fully evaluate this issue, including whether bidding limits are the most appropriate solution and whether such limits or other reforms should be restricted to just demand response or whether they should include other kinds of resources as well. The requirement to offer into the Real-Time Energy Market is integral to participation in the Forward Reserve Market and any deviation from that requirement for certain resources, as would be the case with the

[ne.com/committees/comm_wkgrps/mrktls/comm/mrktls/mtrls/2008/apr892008/a7_iso_presentation_04_08_08_r1.ppt](http://www.iso-ne.com/committees/comm_wkgrps/mrktls/comm/mrktls/mtrls/2008/apr892008/a7_iso_presentation_04_08_08_r1.ppt).

²¹ A copy of the ISO-NE presentation describing this pilot program can be found on the ISO-NE website at: http://www.iso-ne.com/committees/comm_wkgrps/mrktls/comm/mrktls/mtrls/2008/mar11122008/a8_iso_presentation_03_11_08.ppt.

²² NOPR at P 62.

Commission's proposed bidding limits, needs to ensure comparability with those resources that cannot deviate from that requirement. Any change also needs to ensure that the reliability of the system is maintained.

NEPOOL supports the Commission's efforts to encourage fuller integration of demand resources in its ancillary services markets, but urges the Commission to allow the region to work through these issues in order to take account of the specific facts and circumstance of, and the rules and tools in use by, the region. While NEPOOL and ISO-NE have done much to integrate demand response into the region's ancillary services markets, there still remains more work to ensure full participation in all of these markets. To that end, NEPOOL is committed to working with ISO-NE, whether through a new stakeholder working group or other such mechanism, to more fully evaluate all of these issues (including integration of other appropriate resources or new technologies in ISO-NE's ancillary markets). NEPOOL is also willing to discuss and propose to the Commission the establishment of any milestone dates for this review, including any reporting deadlines. Accordingly, NEPOOL welcomes further guidance and encouragement but urges that the Commission allow the region to determine details on how specifically to integrate demand resources, as well as other technologies, into all of its ancillary services markets.

iii. Deviation Charges

The Commission proposed for comment a requirement to eliminate, during system emergencies, deviation charges to a buyer in the energy market for taking less electric energy in the real-time market than purchased in the day-ahead market.²³ NEPOOL has considered this issue at some length as part of its efforts to respond to the Commission in this proceeding, both in the ANOPR Working Group and in the Competition NOPR Working Group. In general, NEPOOL

supports the Commission's efforts to enact reforms that would encourage greater demand response participation in the Real-Time Energy Market. NEPOOL is not certain at this time, however, whether removing deviation charges for all load reductions in the Real-Time Energy Market during system emergencies would actually effectuate this outcome.

This uncertainty is based on the fact that there are many complex and complicating factors involved in ISO-NE's assessment of these deviation charges. ISO-NE has reported to NEPOOL that there are several sub-categories of charges (referred to as "Net Commitment Period Compensation" or "NCPC" charges) that are allocated based on deviations, both positive and negative, between the Day-Ahead and Real-Time Energy Markets. The largest of these charges is referred to as Real-Time Economic NCPC (or First Contingency Protection).²⁴ ISO-NE has calculated that the total amount of Real-Time Economic NCPC costs from January 2006 through February 2008 equaled approximately \$59 million and, of that amount, about \$8.8 million is associated with days that could be considered system emergencies, depending on how one defines a system emergency.²⁵ Most NCPC charges are excluded, however, from this allocation based on deviations, as total Real-Time Economic Costs equal approximately 11% of total NCPC costs according to the ISO-NE.

NEPOOL believes it is important to more fully evaluate the incentives and secondary effects of any removal of deviation charges, the issues around virtual bidding (and whether it is necessary to include virtual bidding in any discussion regarding the removal of these deviation charges), and

²³ NOPR at P 72.

²⁴ See Section III.F.3.2.15 of the ISO-NE Tariff.

²⁵ ISO-NE's calculations used days that could have been considered to have experienced a reserve and/or capacity shortage, i.e., any days in which the Reserve Zone/Reserve Product RCPF ("Reserve Constraint Penalty Factor") was used in any hour.

the potential effects (minimal or otherwise) of any reallocation of these charges. Further, any evaluation regarding the removal of deviation charges needs to consider the original justifications for imposing these charges in the first place, namely to create incentives for efficient scheduling and participation in the Day-Ahead Energy Market.²⁶ Such evaluation also needs to consider that total deviation charges do not go away, but would simply be reallocated.

NEPOOL also recognizes, as reported to it by ISO-NE, that there may be mechanical issues as well around how these deviation charges are calculated and assessed, including ISO-NE's ability to separate out the types of deviation charges proposed by the Commission for possibly different treatment. NEPOOL is committed, however, to continue to evaluate this issue through the stakeholder process, so that any change is effected voluntarily and with full benefit of discussion regarding the specifics and implications. NEPOOL urges the Commission not to impose its proposal without first allowing the region adequate opportunities to conduct this evaluation.

iv. Aggregation of Retail Customers

The Commission proposes a requirement to permit an aggregator of retail customers ("ARC") to bid demand response on behalf of retail customers directly into the ISO/RTO markets.²⁷ The current arrangements in New England already allow for the submittal of such bids through the region's Load Response Programs, which provide for increased participation by demand resources into the New England wholesale markets. The Forward Capacity Market continues this practice by allowing demand resources to aggregate their offers of capacity, with similar size and Load Zone

²⁶ Deviation charges in the Real-Time Energy Market Deviation charges in the Real-Time Energy Market ("Real-Time Energy Market Deviation Energy Charges/Credits") were included with the original Market Rule 1 filing establishing "Standard Market Design" in New England. See Section III.3.2.1(c) and (e) of Market Rule 1; *New England Power Pool and ISO New England Inc.*, 100 FERC ¶ 61,287, *reh'g denied in part and granted in part*, 101 FERC ¶ 61,344 (2002).

²⁷ NOPR at P 86.

restrictions as the Load Response Programs, for participation in the FCA.²⁸ In the NOPR, the Commission states that experience with the existing aggregation program in New England has shown that this program increased demand responsiveness in this region.²⁹ NEPOOL has received feedback that requiring all aggregated demand resources to be in the same Load Zone may discourage participation by certain energy efficiency resources, although there are technical reasons for these current restrictions. NEPOOL does, however, believe that any changes to the existing load aggregation program should be handled through the stakeholder process and not through a generic rule by the Commission requiring changes.

In addition, NEPOOL agrees with the Commission that cooperation and coordination among RTOs and ISOs in developing standardized terms for demand response programs would be beneficial,³⁰ and notes that there are already efforts in this regard underway through the North American Energy Standards Board (“NAESB”).³¹ NEPOOL does not support, and recognizes that the Commission is not proposing to implement, any standardization efforts through a generic Commission proceeding.

v. *Market Rules Governing Price Formation During Periods of Operating Reserve Shortage*

The Commission proposes four reforms to modify existing market rules that limit the market-clearing price during a system emergency, i.e., when there is a shortage of operating reserves, in order to more accurately reflect the true value of energy, increase reliability, and

²⁸ See Section III.13.1.4.1 of the ISO-NE Tariff.

²⁹ NOPR at P 87.

³⁰ NOPR at P 93.

³¹ NEPOOL notes the efforts of NAESB, but disclaims any knowledge regarding the adequacy or sufficiency of the NAESB process. NEPOOL is not, and has not been, actively involved in the NAESB process.

encourage demand response, new generation, and innovation.³² As noted by the Commission, New England has already implemented one of the four reforms proposed, which is the establishment of a demand curve for operating reserves.³³ The Commission states that such approach, which would allow price levels to increase with the severity of the shortage, would incent sufficient supply and demand response.³⁴

The real-time reserve pricing market in New England uses a “demand curve” mechanism through the “Reserve Constraint Penalty Factors” or “RCPFs,” which administratively increases reserves prices and energy prices in a reserve scarcity situation. RCPFs are defined as rates, in \$/MWh, that reflect the value of operating reserve shortages.³⁵ RCPFs are used in the clearing and pricing of energy and reserves in real-time. RCPFs will set the Real-Time Reserve Clearing prices when there are insufficient reserves available to meet the reserve requirement or when the system cannot maintain the requirement through redispatch. This mechanism ensures that in an emergency the effective price cap will rise, thereby promoting economic load reductions. As New England is already in compliance with one of the four reforms proposed by the Commission, it will not comment extensively on the other proposed reforms.

However, with respect to the first two proposed reforms, which would require RTOs/ISOs to either increase the energy supply offer caps and demand bid caps during system emergencies or increase bid caps above the current level only for demand bids during system emergencies, NEPOOL notes that if such proposals were imposed on the region by the Commission, they could have an unintended effect on the markets in New England. Moreover, some NEPOOL Participants

³² NOPR at PP 107, 117, 123-126.

³³ NOPR at P 125 and n 110.

³⁴ NOPR at P 125.

have noted that they premised their agreement to the Forward Capacity Market settlement on assumptions that energy offers and bids in excess of \$1,000/MWh would continue to be prohibited.

In addition, as part of the design of the Forward Capacity Market, demand resources must reduce demand (or supply resources must produce) during shortage hours in order to receive capacity payments.³⁶ This approach mitigates the potential for market power by forcing resources to either perform in the market or lose capacity revenues, and provides incentives similar to that of removing the bid cap for resource performance. The Forward Capacity Market also includes a Peak Energy Rent or “PER” deduction from capacity payments, which was designed to eliminate incentives for capacity resources to drive up the scarcity prices and to provide a hedge against high energy prices for consumers.³⁷ In response to the Commission’s comments that it may be appropriate or beneficial to shift price signals from the capacity markets to the energy markets through its reforms, NEPOOL believes that such actions may not be necessary or desirable for New England at this time, particularly in light of the agreements carefully negotiated and deliberated by the region to implement the Forward Capacity Market and intentionally retain revenues within a capacity market as opposed to an energy-only market for the benefit of those supplying and purchasing capacity. Further, the extensive efforts undertaken by the region to implement a capacity market that fully integrates demand resources lessens the need identified by the Commission to shift price signals to the energy markets in order to encourage greater demand response. NEPOOL notes, however, that it may decide at some later point to reevaluate this issue

³⁵ See Section III.2.7A of the ISO-NE Tariff.

³⁶ See FCM Settlement at Section 11.V.C; Section III.13.7 of the ISO-NE Tariff.

³⁷ See Section III.13.7.2.7.1.1 of the ISO-NE Tariff.

as its capacity market matures, particularly for those resources that are not listed capacity resources or otherwise part of the Forward Capacity Market.

In addition, separate from the Forward Capacity Market, NEPOOL has market rules in place applicable to cold weather emergencies to provide compensation to resources with extraordinary fuel costs that could not be recovered through the existing markets, which offsets the need to remove energy supply offer caps and bid caps during system emergencies as a result of cold weather.³⁸ In sum, NEPOOL would not support the imposition of either of these proposed reforms on New England by the Commission. If the Commission concludes, however, that such imposition is desirable, NEPOOL requests that the Commission allow sufficient time and opportunity to vet these issues with all stakeholders in the region.

III. FACILITATING LONG TERM POWER CONTRACTING

i. Introduction

³⁸ See Section III.H.3.7 of the ISO-NE Tariff.

NEPOOL supports, in general, the Commission's encouragement of long term contracting in organized markets. NEPOOL also supports the Commission's efforts to identify additional steps that can be taken to facilitate long term power contracting in organized markets, including in New England. Long term power contracting can benefit both consumers and suppliers of electricity and can promote the efficient functioning of organized markets. The availability of long term power contracts gives buyers and sellers an alternative to the volatility of the spot markets and can be an effective tool for mitigating the exercise of market power in the spot markets. NEPOOL agrees with the Commission that long-term power contracts promote stability in pricing, mitigates the risk of market abuse, and provide a platform for investment in new generation and transmission.³⁹

ii. Bulletin Board for Posting of Long-Term Offers to Sell or Buy

The Commission proposed for comment a requirement that RTOs/ISOs dedicate a portion of their websites for Market Participants to post offers to buy or sell power on a long-term basis.⁴⁰ NEPOOL supports this proposal and encourages the Commission to take it one step further to include services or products other than energy, such as ancillary or capacity products or services. NEPOOL urges the Commission to allow the regions to develop the details necessary to implement this proposal, including but not limited to issues around the accessibility of this information.

NEPOOL would support the creation of a joint ISO/stakeholder working group in New England to review these details to ensure that such website remains as inclusive as possible and protects confidential and business sensitive information. NEPOOL supports the Commission's proposal but notes that, in the course of discussion in the region, Market Participants identified some legal concerns associated with a bulletin or message board of this type, including ensuring

³⁹ NOPR at P 130.

⁴⁰ NOPR at P 155.

that any posting not be interpreted as a binding offer pursuant to the Uniform Commercial Code, not allowing the board to substitute for regulated markets, and ensuring that the same antitrust and market manipulation protocols that apply today to market behavior also apply to activities relating to this board.

iii. Disincentives to Long-Term Contracting

The Commission cites the proposals from the American Forest & Paper Association (“AF&PA”) and Portland Cement Association, et al. (the “Consumers”) to address problems with incentives for long-term contracting.⁴¹ The AF&PA proposal, termed a “Financial Performance Obligation” or “FPO,” would require every unit receiving a capacity payment to financially guarantee the delivery of energy to the real time market at or below a specified strike price in any hour, which obligation would be financial in nature only. The Consumers’ proposal puts forth an entire Forward Capacity and Energy Market Framework that addresses load forecasting and system modeling, a forward resource commitment auction process, a clearing process and payments to suppliers, and load costs.

NEPOOL has reviewed these proposals and believes that as an initial matter, both proposals are inconsistent with the agreed upon, approved and already implemented Forward Capacity Market in New England. The FCM includes a binding commitment to procure capacity approximately three years in advance of need, with the potential for a five-year commitment once that capacity is accepted in the auction. In the NOPR, the Commission cites the FCM as one of the recent reforms taken to shift reliance from short-term purchases to forward markets held sufficiently in advance of delivery that are more consistent with the time necessary to construct new generation.⁴² Indeed,

⁴¹ NOPR at PP 153, 161.

⁴² NOPR at P 113.

New England's FCM is designed to decrease reliance on the spot market and on short-term contracts, aid in stabilizing prices, and create an environment that is more conducive to the construction of new generation and transmission infrastructure. NEPOOL does, however, look forward to participating in the Commission's technical conference to evaluate these proposals.

IV. MARKET MONITORING POLICIES

i. Introduction

The Commission requests comment on a number of proposals relating to its market monitoring policies, including reforms relating to adequacy of resources, reporting, market evaluations, ethical standards, dissemination of information, and tariff revisions. In general, these proposals are designed to ensure that the market monitoring units ("MMUs") in the various RTO and ISO regions maintain their independence while performing the necessary functions to monitor competitive and efficient wholesale electric markets, and to provide all interested entities, including the Commission, state public utility regulatory agencies and Market Participants, adequate information about the performance of these markets. In general, NEPOOL supports the reforms identified by the Commission. NEPOOL fully supports any efforts that would result in greater transparency with respect to the information disseminated by its two market monitors, the internal market monitoring unit (the "INTMMU") and the independent market advisor (the "IMMU"), as well as the functions, including mitigation and other review functions, performed by its market monitors. Much of what the Commission has proposed in the NOPR is already addressed in the Participants Agreement between ISO and NEPOOL, which was approved by the Commission as part of the RTO arrangements in New England. NEPOOL has, however, included more specific comments on one of the proposals offered by the Commission.

ii. Mitigation and Operation

The Commission proposes to remove MMUs from tariff administration, including mitigation, on the basis that such removal would strengthen their independence in monitoring the markets.⁴³ NEPOOL does not believe that such actions are necessary, particularly for the New England region with its dual market monitoring structure. Compliance with the Commission's proposal would impose a significant burden on the region, particularly with respect to the administration of the Forward Capacity Market. The existing Market Rules in New England and the Participants Agreement provide for both the INTMMU and the IMMU to implement and apply the region's Market Monitoring and Mitigation Plan, with the INTMMU largely responsible for primary day-to-day mitigation. The IMMU, on the other hand, is largely responsible for monitoring New England's wholesale markets. The independence of the INTMMU and the IMMU is not, and has not been, compromised by those functions.

On October 31, 2003, ISO-NE and the New England Transmission Owners submitted the documents to create a RTO for New England. Part of that filing included the Market Monitoring and Mitigation Plan under Appendix A as well as a proposed Participants Agreement, which contained proposed arrangements to ISO-NE's market monitoring and mitigation functions through the INTMMU reporting functionally to the ISO Board and administratively to the Chief Executive Officer of ISO-NE and through contract with the IMMU selected by and reporting to the ISO Board of Directors (the "ISO-NE Board").⁴⁴ This proposal was accepted by the Commission as satisfying the requirements of Order No. 2000 and giving ISO-NE the ability, through both its market

⁴³ NOPR at P 210.

⁴⁴ See Participants Agreement § 9.4.2.

monitoring units, to evaluate Market Rules, market functions, and market procedures and to make the appropriate reports and recommendations to ISO-NE and the Commission.⁴⁵

The market monitoring structure accepted by the Commission is the same structure that is still in place today. That framework clearly outlines the functions to be performed by both the IMM and the INTMM with respect to tariff administration, including mitigation. Section 9.4.3 of the Participants Agreement outlines several functions that shall be provided by the IMM in this regard, including reviewing and assessing the effectiveness of the Market Monitoring and Mitigation Plan and remaining available for consultations with the INTMM, as needed, with respect to implementing and applying the Market Monitoring and Mitigation Plan. Under Section 9.4.4 of the Participants Agreement, the INTMM has the following functions relating to mitigation: (1) to develop and maintain the Market Monitoring and Mitigation Plan, (2) to review on a day-to-day, real-time basis market behavior and implement the Market Monitoring and Mitigation Plan, (3) to consult with the IMM, as needed, with respect to implementing and applying the Market Monitoring and Mitigation Plan, and (4) to be primarily responsible for interaction with external Control Areas, the Commission, other regulators, and Governance Participants with respect to the Market Monitoring and Mitigation Plan.

The independence of the INTMM and the IMM is not, and has not been compromised by these functions. The NOPR states that, because the operation and mitigation functions performed by MMs directly affect market outcomes and performance, an inherent conflict arises when an MM reports on market outcomes that the MM itself has influenced.⁴⁶ NEPOOL disagrees with the Commission's analysis. The MMs in New England must find that certain objective thresholds

⁴⁵ See *ISO New England Inc., et al.*, 106 FERC ¶ 61,280 at P 187 (2004) ("March 24 Order").

⁴⁶ NOPR at P 200.

have been met before mitigation measures are imposed.⁴⁷ These objective thresholds prevent the MMUs from imposing their discretion on markets in a manner that would create a conflict of interest. This is consistent with the Commission’s own statements in the NOPR that mitigation is supposed to be nondiscretionary in nature.⁴⁸ The Commission has acknowledged that when a MMU undertakes the “ministerial function of enforcing clear ISO tariff requirements which do not require the exercise of discretion to administer” there is less likelihood of a conflict.⁴⁹ There is no special need for independence and no potential for a conflict of interest because there is no significant opportunity for the MMUs in New England to exercise discretion.

Further, the dual market monitoring structure in New England addresses the Commission’s concerns regarding any perceived conflicts of interest created by having one entity mitigate a market that it must report on. As the Commission has noted, conflicts of interest occur in dual role scenarios when there is not a “strong separation between the oversight and operations functions.”⁵⁰ In New England, as noted above, the INTMMU is largely involved in primary day-to-day mitigation activities, which are nondiscretionary in nature. The IMMUs, on the other hand, is largely responsible for reviewing and reporting on the markets in New England under Section 9.4.3 of the Participants Agreement. Such responsibilities include, among others, performing independent evaluations and preparing annual and ad hoc reports on the overall competitiveness and efficiency of the New England Markets.⁵¹ The dual roles the INTMMU and IMMUs play in New

⁴⁷ See Section III.A.2.2.1 of the ISO-NE Tariff.

⁴⁸ NOPR at P 209.

⁴⁹ See *CAISO Corp.*, 109 FERC ¶ 61,089 at P 12 (2004).

⁵⁰ See *Rules Concerning Certification of the Electric Reliability Organization*, 114 FERC ¶ 61,104 at P 698 (2006).

⁵¹ See Participants Agreement § 9.4.3(2).

England provide the level of separation between mitigation and reporting sought by the Commission, even though NEPOOL acknowledges that both MMUs do perform both functions under the Participants Agreement.

In addition, the INTMMU is actively involved in reviewing and mitigating certain bids in the Forward Capacity Market, a role readily acceptable to all parties to the FCM Settlement and set forth in the Market Rules, without any challenge. The INTMMU is actively engaged in reviewing de-list bids submitted by existing capacity and may, where appropriate, mitigate such bids.⁵² The INTMMU also reviews offers below certain thresholds for new capacity.⁵³ These are critical roles fundamental to the success of the FCM. Without these reviews, opportunities for gaming and economic withholding could distort auction outcomes and thwart the success of the FCM. The independence of the INTMMU is not, and has not been, compromised by these functions. The fact that this role was never challenged at the Commission, and, in fact, was acceptable to all parties to the FCM Settlement, indicates the level at which Market Participants in the region believe that the INTMMU is best positioned to handle this role, while being able to maintain its independence and objectivity.

Further, in its orders accepting the Market Rules implementing the FCM Settlement, the Commission has even expanded the role that the internal MMU should have in reviewing and rejecting certain de-list bids in the FCA.⁵⁴ The Commission imposed new requirements on the INTMMU to submit its determination of the net risk-adjusted going forward and opportunity costs

⁵² See Section III.13.1.2.3.2.1.1 of the ISO-NE Tariff.

⁵³ See Sections III.13.1.3.5.6.2, III.13.1.1.2.8(f), and III.13.1.4.2.4(b) of the ISO-NE Tariff.

⁵⁴ See April 16 Order at PP 120-121; See *ISO New England Inc.*, 120 FERC ¶ 61,087 at P 52 (2007).

for existing generators whose de-list bids it had rejected.⁵⁵ This requirement placed more responsibility with the INTMMU than the originally submitted proposal to simply enter a zero bid in the FCA for any generator whose de-list bid had been rejected.

The role of the market monitors in these functions provides important real-time information and increases the abilities of the market monitors to identify early warnings of market manipulation or suspect behavior in real-time. The reports from the MMUs in New England reflects their ongoing investigation in the region's markets. The involvement of the INTMMU and the IMMUs in mitigation functions increases the abilities of those MMUs to identify early warnings of market manipulation or suspect behavior in real-time. Allowing these MMUs to perform this level of evaluation of the New England Markets provides a useful and necessary knowledge base to evaluate the New England Markets and to allow the MMUs to carry out their core market monitoring functions in a more efficient manner. This leads to greater overall market efficiency and competitiveness.

The Commission's proposed solution to remove MMUs from tariff administration, including mitigation, and to allow the ISOs and RTOs to serve that function is not necessary in New England given the dual nature of its market monitoring structure and would create a significant challenge to the region in terms of the role the INTMMU plays in the FCM. NEPOOL strongly urges the Commission not to adopt this proposal, or at the very least, to allow for regional accommodation so that New England, with its dual market monitoring structure, can continue having its MMUs perform mitigation functions.

⁵⁵ See 120 FERC ¶ 61,087 at P 53.

V. RESPONSIVENESS OF RTOs AND ISOs

The Commission proposes to establish new criteria intended to ensure that a RTO or ISO board is responsive to its stakeholders and customers.⁵⁶ NEPOOL supports the Commission's proposal to require a compliance filing by each RTO and ISO regarding these four criteria: (1) inclusiveness, (2) fairness in balancing diverse interests, (3) representation of minority positions, and (4) ongoing responsiveness. NEPOOL also supports the Commission's proposal to require ISOs/RTOs to post a mission statement or charter on their website that would set forth the purpose of the organization, guiding principles, and commitment to responsiveness. In addition, NEPOOL supports the Commission's efforts to ensure that RTO/ISO management programs give appropriate weight to stakeholder responsiveness.

NEPOOL agrees with the Commission that a one-size-fits-all approach, whether in the form of a board advisory committee, hybrid board or other proposal, would not work for every region, particularly in New England where there is a robust and active stakeholder process.⁵⁷ The New England stakeholder process and the successes it has achieved are due in part to the contractual arrangements between NEPOOL and ISO-NE found in the Participants Agreement approved by the Commission in March of 2004 as part of a comprehensive settlement for implementing RTO arrangements in New England.⁵⁸ One of the more notable features in that agreement is the ability of NEPOOL, through a nominating process, to provide input and vote on incoming ISO-NE board members.⁵⁹

⁵⁶ NOPR at P 245.

⁵⁷ *See* NOPR at P 277.

⁵⁸ *See* March 24 Order.

⁵⁹ Out of respect for the candidates being considered for the Board, ISO-NE has imposed strict confidentiality requirements on nominating committee members, including the state regulator who is

Under the terms of the Participants Agreement, the NEPOOL Participants Committee votes on the slate of candidates recommended by a Nominating Committee, which is composed of up to seven (7) members of the existing ISO-NE Board, up to six (6) NEPOOL Participants, and one (1) representative of the New England Conference of Public Utility Commissioners (“NECPUC”).⁶⁰ A super-majority vote of at least 70% of the aggregate Sector Voting Shares is required for Participants Committee endorsement of the slate, and all slates to date have received the support of the Participants Committee. The Participants Agreement provides, however, for the possibility of disagreement with the Nominating Committee. If the Participants Committee fails to endorse the recommended slate, the Nominating Committee is required to repeat the nominating process to propose a second slate to the Participants Committee, following investigation of the reasons for the first slate to fail to receive a Committee endorsement. If the Participants Committee fails to approve this second slate, then both slates are presented to the ISO-NE Board for its consideration. The ISO-NE Board ultimately votes on whether to approve a slate of candidates. In the event that the ISO-NE Board fails to approve any slate presented to it by the Nominating Committee, the nomination processes will be repeated once again in order to present a further slate to the ISO-NE for its final vote. In the event that the Participants Committee fails to endorse a slate of candidates for the ISO-NE Board, the ISO-NE Board will nominate and elect the directors and will advise the Participants Committee accordingly.

The Commission largely accepted the nominating and election processes of the ISO-NE Board, stating that these processes allow for “adequate input on the part of stakeholders” and allow

appointed by NECPUC to the nominating committee. The state regulators have sought additional flexibility to discuss candidates for nominees among themselves on a confidential basis ahead of the nominating committee making its recommendation. NEPOOL believes that that request is pending.

⁶⁰ See Participants Agreement § 13.1.5.

the ISO-NE Board to “act with sufficient independence of any market participant.”⁶¹ Since instituting these procedures in 2005, the Nominating Committee has functioned well, and in each of the past three years, has unanimously recommended a slate of directors, each of which was subsequently supported by NEPOOL and approved by the ISO-NE Board of Directors.

In addition, New England has a well-developed, highly functional stakeholder process for providing input to, and collaboration with ISO-NE. The effectiveness of the NEPOOL Participant Process lies in the consensus-building that has become a hallmark in this region and the number of tariff and market rule proposals that are presented jointly by NEPOOL and ISO before the Commission for its consideration. The voting structure outlined in the Participants Agreement provides a mechanism to ensure full representation and provides for mechanisms to address circumstances where consensus cannot be reached, or time will not permit such consensus to take place. The Commission approved this governance structure as “utilizing a meaningful stakeholder process to solicit, receive, consider and respond to advisory input from stakeholders.”⁶² The Commission also stated its belief that these stakeholder processes will facilitate the formation of consensus positions. This belief has largely held true. Nearly all the market rule and tariff changes ISO-NE has filed for acceptance by the Commission since it became the RTO for New England, including major proposals to implement new reserve and capacity markets, have received the recommendation of NEPOOL. NEPOOL is, as it always has been, willing to continue to work to improve its stakeholder process, including working with smaller participants and state regulators to enhance their participation.

⁶¹ March 24 Order at P 56.

⁶² March 24 Order at P 54.

With respect to the Commission's proposals on this topic, NEPOOL supports the proposal to require a compliance filing by each RTO and ISO regarding these four criteria: (1) inclusiveness, (2) fairness in balancing diverse interests, (3) representation of minority positions, and (4) ongoing responsiveness. While NEPOOL believes that the existing governance structure in New England meets and supports these criteria, NEPOOL generally supports the Commission's efforts to continue to increase the responsiveness of RTOs and ISOs through a compliance filing. NEPOOL also supports the Commission's proposal to require ISOs/RTOs to post a mission statement or charter on their website that would set forth the purpose of the organization, guiding principles, and commitment to responsiveness. Today, ISO-NE publishes annually a five-year business plan developed by the ISO-NE Board and ISO-NE senior management and shared with NEPOOL Participants and NECPUC representatives, which includes "responsiveness to stakeholders" as one of ISO-NE's three primary goals.

In addition, NEPOOL supports the Commission's efforts to ensure that RTO/ISO management programs give appropriate weight to stakeholder responsiveness. ISO-NE has reported to NEPOOL that it has several formal feedback mechanisms in place to receive input from customers and customer feedback is used as one of the metrics for determining ISO-NE management compensation. Many NEPOOL Participants already participate in annual customer surveys conducted by ISO-NE to assess overall customer satisfaction and satisfaction with ISO-NE's communications.

VI. CONCLUSION

NEPOOL appreciates and supports the Commission's efforts to improve the operation of organized wholesale electric markets. Many of the amendments proposed by the Commission make good sense for New England and are either in place or appropriately pursued, as discussed herein. NEPOOL does not, however, support the Commission's proposals to remove the MMUs from tariff administration, including mitigation, and urges the Commission to either reject its proposal entirely or to revise its proposal in such a manner to allow New England to continue its existing MMU practices.

Respectfully submitted,

NEPOOL Participants Committee

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Dated: April 21, 2008

CERTIFICATE OF SERVICE

I hereby certify that I caused a copy of the foregoing document to be served electronically upon each person designated on the official service list compiled by the Secretary of the Federal Energy Regulatory Commission.

Dated at Hartford, Connecticut this 21st day of April, 2008.

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