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September 11, 2007

**VIA ELECTRONIC FILING**

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

**Re: ISO New England Inc. and New England Power Pool,  
Docket No. ER07-365-003**

Dear Secretary Bose:

Attached for electronic filing in the above-referenced docket is the *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 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.

Counsel for ISO New England Inc.

Attachment

cc: Official Service List



## I. BACKGROUND

On December 22, 2006, the ISO and NEPOOL submitted proposed revisions to Market Rule 1 designed to memorialize the processes and methodologies used to determine ICR for the New England Control Area.<sup>6</sup> Revisions to portions of the process for developing the ICR were needed to accommodate the Commission-approved Settlement Agreement establishing a Forward Capacity Market (“FCM”) in New England.<sup>7</sup> On January 17, 2007, LIPA protested the December 22 Filing and maintained that it failed to comply with a provision of the FCM Settlement that addresses exports across constrained regions.<sup>8</sup>

On February 28, 2007, the Commission issued an order that accepted proposed changes to Market Rule 1 designed to memorialize the processes and methodologies used to determine the Installed Capacity Requirements (“ICR”) for the New England Control Area. The order also agreed with LIPA’s protest and directed the ISO to submit a compliance filing that provides for a process to allow exports across import-constrained Capacity Zones.<sup>9</sup>

The August 6, 2007 Compliance Filing proposed Market Rule changes addressing the treatment of capacity exports in the Forward Capacity Auction and also described outstanding No. 3 (“ISO Tariff”), the Second Restated New England Power Pool Agreement, and the Participants Agreement.

<sup>6</sup> Revisions to Market Rule 1 Relating to the Methodology for Calculating Installed Capacity Requirements, *ISO New England Inc. and New England Power Pool*, Docket No. ER07-365-000 (filed Dec. 22, 2006) (“December 22 Filing”).

<sup>7</sup> *Devon Power LLC*, 115 FERC ¶ 61,340, *order on reh’g and clarification*, 117 FERC ¶ 61,133 (2006).

<sup>8</sup> Explanatory Statement in Support of Settlement Agreement of the Settling Parties and Request for Expedited Consideration and Settlement Agreement Resolving All Issues, *Devon Power LLC*, Docket Nos. ER03-563-000, -030, -055 (filed Mar. 6, 2006) (“FCM Settlement”).

<sup>9</sup> February 28 Order at P41.

issues that were discussed but not resolved in the NEPOOL stakeholder process, including potential mechanisms to allow Market Participants exporting capacity-backed energy the option to reduce the risk of curtailment due to transmission constraints, and the allocation of reliability-related costs to such exports.

On August 27, 2007, LIPA submitted Comments indicating that it “supports the changes to Market Rule 1 . . . as significant steps toward a workable solution to facilitate capacity exports through an import-constrained zone over tie lines to external regions.”<sup>10</sup> However, LIPA also requested that the Commission direct the ISO to continue stakeholder discussions and establish a date certain for filing further changes. Such changes would allow Market Participants “an option to reduce the risk of curtailment due to transmission constraints for exports of capacity-backed energy by a market-firming service mechanism to allocate reliability-related resource commitment costs to such exports that elect the option.”<sup>11</sup> LIPA further requested consideration of a market mechanism to purchase energy from neighboring control areas rather than subjecting the exporter to the full curtailment costs.

## **II. ANSWER**

### **A. Allocation of Reliability-Related Commitment Costs to Capacity Exports to Reduce Curtailment Risk**

LIPA desires to have the ISO implement a process to commit additional resources in the import-constrained region to back capacity exports, and to charge the capacity exports for the commitment cost so that Market Participants may elect this option to reduce the risk of curtailment. LIPA correctly notes that the ISO agrees that this is a desirable addition to the

<sup>10</sup> Comments at 4.

<sup>11</sup> *Id.* at 6.

market rules.<sup>12</sup> In fact, the initial proposals discussed with stakeholders contained draft provisions addressing these issues. However, the draft provisions were removed from the proposals because agreement had not yet been reached regarding which costs should be assigned to capacity-backed exports, and because the ISO agreed, after further discussions with stakeholders, that the issue of commitment costs would be addressed in the upcoming process of conforming the energy market to the FCM design.

LIPA requests that the Commission direct the ISO to continue stakeholder discussions and establish a date certain for filing the proposed changes.<sup>13</sup> Although there is not a specific filing date associated with the market conformance effort, the ISO anticipates that the stakeholder process that will precede the filing will begin in the first quarter of 2008. This process will culminate in a filing with the Commission which the ISO anticipates submitting in the third quarter of 2008.

Between now and the third quarter of 2008, the ISO will also be expending substantial time and resources on several additional important priorities. Regional projects including FCM implementation, long-term firm transmission rights, redesign of the interconnection queue process, review of the treatment of Seasonal Demand Resources, and revision of the Reliability Agreement process are among the numerous tasks that the ISO must undertake in the near term. Given these substantial additional responsibilities, the timeframe proposed by the ISO to address the additional issues related to capacity-backed energy exports is quite reasonable.

Further, the ISO and most stakeholders determined it would be appropriate to deal with the commitment cost issues once, rather than in a piecemeal fashion. In addition, software and

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

<sup>13</sup> Comments at 7.

operating procedures will need to be modified following completion of the rule and policy effort, and it is not clear exactly how much work this will involve. Thus, the Commission should permit the ISO to address issues regarding the allocation of commitment costs related to capacity-backed exports in the ISO's third quarter filing in 2008, and also to address implementation issues at that time.<sup>14</sup> LIPA states that the ISO's proposed changes should be filed by a date certain "so that they may be implemented in advance of the rules applicable to capacity exports under the FCM that take effect in 2010."<sup>15</sup> This can be accomplished within the timeframe proposed by the ISO without precluding implementation before the FCM commences.

**B. Purchases From Neighboring Control Area to Reduce Curtailment Cost Exposure**

LIPA's Comments also propose that the Commission direct the ISO to "fully consider and propose market rules that use market mechanisms to purchase energy from a neighboring control area rather than subject the exporting party to the full costs of curtailment."<sup>16</sup> Early in the development of the ISO proposal, the ISO worked extensively with the New York Independent System Operator ("NYISO") to ensure that the ISO's and NYISO's processes are coordinated. These efforts identified that exports can be curtailed for local reliability, prior to an emergency condition. The market rules in New England allow Market Participants to submit Emergency Energy offers up to, but not exceeding \$1,000/MWh. The scheduled Emergency External Transactions are then paid the higher of their offer price or the applicable External

<sup>14</sup> The ISO has also noted its belief that the development of a mechanism to allow a Market Participant to reduce the risk of curtailment of a capacity export is an issue that is separate from the compliance obligation imposed by the Commission. Compliance Filing at 7.

<sup>15</sup> Comments at 7.

<sup>16</sup> *Id.*

Node Locational Marginal Price (“LMP”). This creates an incentive problem. The potential to obtain the \$1,000 price incents participants to wait for the emergency to be declared, rather than scheduling economic counterflow transactions at less than the \$1,000 potential emergency price. For example, energy may continue flowing to New York when the LMP at the New England External Node is \$700-\$800/MWh, despite there being a price of \$300 at the corresponding node in New York. If energy continues to flow from the high priced region to the low priced region, then the market has become flawed.

The ISO agrees to work with stakeholders to determine if a more market compatible process can be found, such as paying the export (sink) region the actual LMP, rather than encouraging delayed offers at an amount up to \$1,000. The timing for these discussions would also be during the market conformance process, and the ISO anticipates that the associated filing will be submitted to the Commission in the third quarter of 2008.

### III. CONCLUSION

For the foregoing reasons, the ISO respectfully requests that the Commission accept the comments in the ISO's Answer presented herein.

Respectfully submitted,

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Dated: September 11, 2007

## **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 (2007), 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 11th day of September, 2007.

/s/ Sherry A. Quirk  
Sherry A. Quirk

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