119 FERC ¶ 61,045
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

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

ORDER CONDITIONALLY ACCEPTING MARKET RULES
AND REQUIRING COMPLIANCE FILING

(Issued April 16, 2007)

1. In this order, the Commission conditionally accepts the revisions to the market rules proposed by ISO New England, Inc. (ISO-NE) to implement New England's Forward Capacity Market (FCM). The Commission also requires certain modifications to those rules.

I. BACKGROUND

A. New England's Forward Capacity Market

2. As discussed in prior orders in this proceeding,[1] as a means of ensuring reliability, for many years ISO-NE has imposed an installed capacity (ICAP) requirement on load-serving entities, requiring them to procure specified amounts of ICAP based on their peak loads plus a reserve margin.[2] Beginning in 1998, ISO-NE began operating a bid-based market for ICAP.[3] In 2000, as the region began to develop wholesale power markets and utilize market-based rates, the Commission began to identify flaws in the ICAP market, and it allowed ISO-NE to replace the ICAP auction mechanism with an administratively-determined ICAP deficiency charge. The Commission agreed with ISO-NE that the auction "can produce inflated prices unrelated to the actual harm caused by ICAP

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[1] *Devon Power LLC*, 111 FERC ¶ 63,063 (2005) (Initial Decision); *Devon Power LLC*, 115 FERC ¶ 61,340 (2006) (FCM Order), *order on reh'g*, 117 FERC ¶ 61,133 (2006) (FCM Rehearing Order).

[2] Before the establishment of ISO-NE, the New England Power Pool (NEPOOL) similarly imposed an ICAP requirement.

[3] *See New England Power Pool*, 83 FERC ¶ 61,045 at 61,263 (1998).

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deficiencies."[4] In 2002, the Commission addressed further deficiencies in New England's ICAP market, this time noting the lack of a locational element, and stating that it "believes that location is an important aspect of ensuring optimal investment in resources."[5] As part of this overall process, certain generators sought cost-of-service Reliability-Must-Run (RMR) contracts. In a series of orders,[6] the Commission rejected the majority of the RMR agreements, out of concern about the effect widespread use of such contracts could have on the competitive market. The Commission directed the ISO "to file no later than March 1, 2004 for implementation no later than June 1, 2004, a mechanism that implements location or deliverability requirements in the ICAP or resource adequacy market . . . so that capacity within [congested areas] may be appropriately compensated for reliability."[7] Accordingly, on March 1, 2004, the ISO submitted a filing seeking to implement a locational ICAP market in New England by June 1, 2004.[8]

3. After a hearing before an Administrative Law Judge and extensive further proceedings, the parties arrived at a settlement with regard to that filing (Settlement Agreement), which the Commission substantially approved in the FCM Order and FCM Rehearing Order.

B. <u>The Instant Filing</u>

4. On February 15, 2007, ISO-NE filed the required market rule revisions, pursuant to section 205 of the Federal Power Act (FPA), 16 U.S.C. § 824d (2000), as required by the Settlement Agreement.

5. The proposed rules establish that ISO-NE will conduct an annual auction to procure capacity. This annual auction (Forward Capacity Auction)[9] will be conducted

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[4] *ISO New England, Inc.*, 91 FERC ¶ 61,311 at 62,081 (2000).

[5] New England Power Pool and ISO New England, Inc., 100 FERC ¶ 61,287 at 62,278 (2002).

[6] *Devon Power LLC*, 102 FERC ¶ 61,314 (2003); *Devon Power LLC*, 103 FERC ¶ 61,082 (2003) ; *Devon Power Company*, 104 FERC ¶ 61,123 (2003); *PPL Wallingford Energy LLC*, 103 FERC ¶ 61,185 (2003); *PPL Wallingford Energy LLC*, 105 FERC ¶ 61,324 (2003).

[7] *Devon Power LLC*, 103 FERC P61,082 at P 37 (2003)

[8] *Id*.

[9] Capitalized terms used but not otherwise defined in this order have the meanings ascribed to them in ISO-NE's Transmission, Markets and Services Tariff (the tariff), the Second Restated New England Power Pool Agreement, and the Participants Agreement. *See* Transmittal, February 15 filing, at 1 fn. 4.

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three-plus years in advance of the period during which capacity will actually be supplied.[10] ISO-NE intends that the period between the Forward Capacity Auction and the supply commitment period will provide a planning period for new entry, so that potential new capacity suppliers (capacity resources) may participate in the Forward Capacity Auction and compete with existing resources. If a potential capacity resource clears the Forward Capacity Auction, it has more than three years to build the infrastructure needed to fulfill its capacity obligation.

6. Each Forward Capacity Auction applies to a commitment period that corresponds to ISO-NE's June-to-May Power Year. Any resource that clears the Forward Capacity Auction is obligated to supply capacity during the applicable supply commitment period, *i.e.*, the year beginning June first. "Clearing" the Forward Capacity Auction means that the capacity resource was selected in the auction, and then must assume a supply obligation for the supply commitment period to which the Forward Capacity Auction corresponds. Existing resources may only enter into commitments for periods of one year, but new resources may commit for periods up to five years.

7. Forward Capacity Auctions are designed as "descending clock" auctions. In a descending clock auction, the auction administrator announces a Starting Price. At the Starting Price, all capacity is presumed to be offering into the auction. Prices will "tick down" or descend from the Starting Price in a series of rounds, with resources being withdrawn from the auction (i.e., de-listing) in each round. The auction will conclude when the number of megawatts (MWs) offered equals the number of MWs that need to be bought.

8. The Settlement Agreement stipulated that in each Forward Capacity Auction, ISO-NE will procure 100 percent of the amount of capacity needed in the New England control area and within each capacity zone.[11] The amount of capacity is a MW quantity, known as the Installed Capacity Requirement. Prior to each Forward Capacity Auction, ISO-NE will calculate the Installed Capacity Requirement for the New England control area for each year through the commitment period.[12] The FCM includes a locational

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[10] The FCM also entails additional reconfiguration auctions to be conducted in the time between the Forward Capacity Auction and the supply commitment period. For example, the initial Forward Capacity Auction will be held in February 2008 and will procure capacity for the period of June 1, 2010 to May 31, 2011.

[11] Settlement Agreement at 11.I.A.

[12] The Commission recently issued an order approving tariff changes to revise ISO-NE's Market Rule 1 to formalize the processes and methodologies used to determine the Installed Capacity Requirement for the New England Control Area. *ISO New England Inc. and New England Power Pool*, 118 FERC ¶ 61,157 (2007) (Installed Capacity Requirement Order), *rehearing pending*.

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component that allows for prices to differ across capacity zones. Depending on the transmission system constraints, prices for capacity may differ in different capacity zones.

9. The proposed rules on FCM in the instant filing are divided into eight sections, all of which are within section III (Market Rule 1) of ISO-NE's tariff.[13] Section III.13.1 establishes the processes through which capacity resources qualify for participation in Forward Capacity Auctions. Section III.13.2 addresses the mechanics of the Forward Capacity Auction.[14]

10. This order addresses section III.13.1 and III.13.2 as well as the conforming changes to the market rules and definitions governing the Installed Capacity Requirements. The Commission will issue a subsequent order in Docket No. ER07-547-000 that addresses the remaining sections of III.13 as well as the Financial Assurance and Billing Policies and remaining changes to Market Rule 1 proposed in the February 15 filing.

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[13] Those sections are:

13.1. Resource Qualification
13.2. Annual Forward Capacity Auction
13.3. Critical Path Schedule Monitoring
13.4. Reconfiguration Auctions
13.5. Bilateral Contracting in the FCM
13.6. Rights and Obligations of Capacity Resources
13.7. Performance, Payments and Charges in the FCM
13.8. Reporting and Price Finality

[14] Section III.13.3 provides details related to the monitoring of the "Critical Path Schedule," which is required of new capacity resources seeking to participate in the FCM. Section III.13.4 describes how reconfiguration auctions will be conducted. Section III.13.5 describes the requirements associated with the acquisition of or shedding of obligations by means of bilateral contracts in the FCM. Section III.13.6 sets forth the rights and obligations of various resources (including generation, imports and demand response) in the FCM. Section III.13.7 details the rules for payment of resources and charges to load under the FCM, as well as adjustments to payments based on resource availability. Finally, Section III.13.8 addresses reporting requirements of the ISO to the Commission and challenges to certain ISO determinations, including price finality. As discussed *infra*, the Commission will be considering these remaining portions of the February 15 filing in its order in Docket No. ER07-547-000.

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11. ISO-NE states that the FCM rules were developed through an extensive stakeholder process. [15] The proposed rules on FCM (as well as the market rule and manual revisions necessary to extend the term of the existing Load Response Program) were supported by the Participants Committee with a vote of 78.74 percent in favor. ISO-NE states that the volume and timing of the instant filing were such that ISO-NE and NEPOOL were unable to file jointly. (NEPOOL states in its comments, however, that it fully supports the filing.)

12. ISO-NE has requested different effective dates for different portions of this package of rules. First, ISO-NE requests an effective date of February 16, 2007 for the definitions and those tariff sheets related to qualification (section 13.1 of the proposed rules on FCM). Second, the ISO-NE requests an effective date of March 1, 2007, for the conforming, non-substantive changes to the market rules and definitions governing the Installed Capacity Requirements. Third, ISO-NE requests an effective date of April 16, 2007, for the provisions of the proposed rules governing the Forward Capacity Auction (section 13.2 of the proposed rules on FCM).[16]

C. Interventions, comments and protests

13. ISO-NE's February 15 filing is divided into two dockets. The instant docket, Docket No. ER07-546-000, considers the following:

- Definitions, and those tariff sheets related to qualification, section III.13.1 (effective date requested by ISO-NE: February 16, 2007).
- Changes to the Installed Capacity Requirements (Installed Capacity Requirement) Market Rules (effective date requested by ISO-NE: March 1, 2007).

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[15] According to ISO-NE, formal discussions of the proposed rules on FCM began at the Markets Committee on September 13, 2006 and those discussions continued over the course of 23 meetings, with extensive involvement of the Reliability Committee and state utility regulatory agencies.

[16] With regard to the matters to be considered in Docket No. ER07-547-000, sections 13.3 – 13.8 of the proposed rules on FCM, ISO-NE requests that the balance of the proposed rules on FCM be made effective on June 15, 2007 (), and, with notice, for the changes to the Tariff's Financial Assurance and Billing Policies, ISO-NE requests an effective date of no earlier than June 1, 2007.

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- Market Rules governing the Forward Capacity Auction, section III.13.2 (effective date requested by ISO-NE: April 16, 2007). [17]

14. Notice of the filing in Docket No. ER07-546-000 was published in the Federal Register, with interventions, comments and protests due on March 8.[18]

15. Timely motions to intervene, protests or comments were filed in Docket No. ER07-546-000 by the parties listed in Appendix A. NICC and the BG Entities filed a motion to intervene out of time. ISO-NE, Capacity Suppliers, NRG, HQUS, IRH and CT DPUC filed motions for leave to answer the protests, and answers. FirstLight filed a motion to answer ISO-NE's answer, and an answer.

II. PROCEDURAL ISSUES

16. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.214 (2006)), the notices of intervention and the timely-filed unopposed motions to intervene serve to make the entities filing them parties to this proceeding. The motion to intervene out-of-time is granted, given the early stage of the proceedings, the party's interest and the absence of prejudice or delay. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2006), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the parties' answers to the protests, and FirstLight's answer to ISO-NE's answer, because they have provided information that assisted us in our decision-making process.

III. SUMMARY OF PROPOSED RULES

A. Section 13.1: Qualification

17. Section 13.1 addresses the rules and procedures associated with qualifying resources for participation in the FCM. Each resource that seeks to sell (offer) capacity into the FCM must qualify as one of several resource types, including: 1) a new generating capacity resource; 2) an existing generating capacity resource; 3) an import capacity resource, existing or new; or 4) a demand resource, existing or new.[19]

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[17] The Commission will consider the remaining matters contained in ISO-NE's February 15 filing in Docket No. ER07-547-000. *See* 72 Fed. Reg. 8368 (2007).

[18] 72 Fed. Reg. 8367 (2007).

[19] Load serving entities may designate resources as "Self-Supplied," which results in an offset to the load serving entity's share of its capacity obligation.

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18. All capacity resources are required to submit specified qualification information to ISO-NE that is designed to: determine the qualified megawatt capacity that the resource can offer into the Forward Capacity Auctions (as well as other FCM auctions, known as reconfiguration auctions) and certify that it can reasonably be expected to be available to supply capacity during the relevant commitment period. The character of information will depend on the type of resource – new, existing, imported, intermittent, a demand resource, or self-supplied capacity. Through the qualification process, ISO-NE will determine the maximum amount of capacity a resource may offer into the Forward Capacity Auction. This maximum amount of capacity will be the resource's summer Qualified Capacity. ISO-NE will also determine, through the qualification process, the amount of capacity that a resource may offer into reconfiguration auctions applicable to winter months (October through May). New generating capacity, new imports and new demand resources may only participate in a Forward Capacity Auction (i.e., offer capacity as capacity suppliers) if they have been qualified through the ISO-NE qualification process.

19. Existing capacity resources are assumed to participate, but may remove themselves from participation in the Forward Capacity Auction. This is accomplished through the submission of a de-list bid. Four types of de-list bids[20] must be submitted to ISO-NE in advance of the Forward Capacity Auction, during the qualification process; the fifth type (Dynamic De-List Bids) may change during the auction. If any of the pre-auction de-list bids are greater than a specified price threshold, that bid will be reviewed by ISO-NE's Market Monitor, which may require the capacity resource to submit additional information for review. ISO-NE is required to submit a filing to the Commission at least three months prior to each Forward Capacity Auction in which it will, among other things, will set forth its findings on the de-list bids that have been submitted, those that have been accepted and those that have not.

1. Generating Capacity Resources

20. A new generating capacity resource is considered new if it has never been "listed" as a capacity resource in New England.[21] An existing generating capacity resource that undertakes certain specified investments may qualify all or a portion of its capacity as new capacity. The proposed rules on FCM contain provisions that govern the process through which a resource that has previously been counted as a capacity resource

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[20] Permanent De-List Bids, Static De-List Bids, Export Bids, and Administrative Export De-List Bids.

[21] For the Forward Capacity Auction applicable to the commitment period beginning June 1, 2010, a resource that is not expected to begin commercial operation by February 1, 2009 will be treated as a new generating capacity resource.

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(including one that had been deactivated or retired) may participate in a Forward Capacity Auction as a new generating capacity resource.[22]

2. Demand Resources

21. Demand resource measures include energy efficiency, load management, and Distributed Generation (i.e., electricity generated close to the loads that it serves).[23] A demand resource that has previously been considered an existing demand resource may qualify as a new demand resource if it meets one of the specified conditions applicable to existing resources qualifying as new resources.[24] The Qualified Capacity of a new demand resource will equal the simple average of its estimated capacity value in the months of June, July and August.[25]

3. Show of Interest Form and Qualification Package

22. The process of qualifying for new capacity resources includes two steps. The first is the Show of Interest Form and accompanying deposit. The second is the submission of a Qualification Package. Specific timelines are associated with each. Both submissions are required regardless of the status of the project under the generator interconnection procedures. Existing capacity resources must also submit to the qualification process, though the requirements for existing capacity resources are less comprehensive than those for new capacity resources.

a. New Capacity Show of Interest Form

23. All new resources that wish to offer capacity into the Forward Capacity Auctions must submit a Show of Interest Form.[26]

24. For new generating capacity resources, the Show of Interest Form will include data to allow ISO-NE to conduct an initial interconnection analysis. Generally, Show of

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[22] Section III.13.1.1.1.2.

[23] Distributed Generation may also qualify as a new demand resource if it has operated only to address an electric power outage in certain circumstances, such as an electric power outage due to failure of the electrical supply.

[24] The Settlement Agreement specified a number of investment thresholds that would allow a resource that had been previously listed as capacity to undertake in order to be considered new capacity. Settlement Agreement at 11.II.B.2

[25] There are two additional categories of resources: import capacity resources and capacity resources designated as self-supply.

[26] Section III.13.1.1.2.1.

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Interest Forms may be submitted to ISO-NE during a two month window that closes at least one year prior to the Forward Capacity Auction.[27]

25. In determining the amount of capacity a new generating capacity resource can provide, ISO-NE will evaluate that capacity in relation to other proposed generating capacity resources. ISO-NE may determine that the presence of another proposed generating capacity resource prevents a new proposed generating capacity resource from providing its full amount of capacity. This is known as "overlapping impacts." The proposed rules on FCM contain a provision for dealing with overlapping impacts. Section III.13.1.1.2.3(f) proposes that in such instances, new generating capacity resources will be accepted for participation in the Forward Capacity Auction on the basis of their position in the interconnection queue, with priority given to resources that entered the queue earlier.[28] ISO-NE acknowledges that this approach may not represent the ideal solution and commits to working with its stakeholders to investigate alternative approaches. New capacity resources must also submit a Qualification Process Cost Reimbursement Deposit with the Show of Interest Form.[29]

26. ISO-NE chose an effective date of February 16, 2007 for the tariff sheets related to qualification. ISO-NE asserts that good cause exists to grant waiver of the 60-day notice requirement to permit an effective date of February 16, 2007 for the tariff sheets related to the qualification rules. ISO-NE asserts that the qualification process is a linchpin of the market design and that a waiver of the 60-day prior notice requirement will allow ISO-NE to evaluate the impacts of proposed projects on the transmission system. ISO-NE states that these studies must be completed in a timely manner, before the first Forward Capacity Auction.

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[27] Section 13.10.1 of the proposed rules on FCM lists the window of time during which ISO-NE will accept new capacity Show of Interest Forms applicable to the first eight Forward Capacity Auctions. ISO-NE established a deadline of December 31, 2006 for receipt of most Show of Interest Forms. Given that the instant filing was submitted to the Commission on February 15, ISO-NE acknowledges that the December 31 (or January 2, 2007, after the week-end) deadline did not have the force of regulation. ISO-NE states, however, that it received over 200 Show of Interest Forms, representing more than 10,000 MW, seeking to qualify for the first Forward Capacity Auction, by January 2. In the period between January 2 and February 15, additional Show of Interest Forms were filed and accepted by ISO-NE; other submissions were withdrawn in the same period. ISO-NE asserts that the additional submissions can be accommodated within the process presently underway.

[28] Resources with lower priority in the queue may be accepted partially.

[29] Section III.13.1.1.2.1(e).

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27. ISO-NE also believes that it is necessary that the requirement of a Qualification Process Cost Reimbursement Deposit be made effective on February 16, 2007, with deposits due on February 20, 2007. ISO-NE states that it intends to cease the review of any Show of Interest Form where the project sponsor has failed to submit a Qualification Process Cost Reimbursement Deposit by February 20, 2007.

b. New Capacity Resource Qualification Package

28. Following the Show of Interest Form submission, the proposed rules on FCM require that each new capacity resource submit a Qualification Package. For the first Forward Capacity Auction, most Show of Interest Forms were due January 2, 2007; the new capacity Qualification Package deadline is June 15, 2007.

29. Each new generating capacity resource must submit a new capacity Qualification Package no later than the specified deadline, including a Critical Path Schedule, information with respect to offers below certain prices, and the commitment period(s) in which the resource wishes to supply capacity. The Critical Path Schedule is a fundamental component of the new generating capacity Qualification Package and comprises information that enables ISO-NE to evaluate whether it is feasible for the project will achieve commercial operation by the beginning of the commitment period. The Critical Path Schedule for new generating capacity resources includes (but is not limited to) dates on which the following milestones are to occur: permits, closing of project financing, and achievement of commercial operation.[30] The Settlement Agreement specifically stipulated that new capacity resources that intended to submit capacity offers at prices below a specified threshold would submit those bids for review to ISO-NE's Market Monitor.[31] This threshold is 0.75 times the estimated Cost of New Entry.[32] The Settlement Agreement further required that any such offer be submitted prior to the qualification deadline.

30. Each new demand resource must also submit a new demand resource Qualification Package no later than the specified deadline.[33] Elements of the Qualification Package for new demand resources include: a project description, information on the sources of funding, a Measurement and Verification Plan and Critical Path Schedule.

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[30] *See* Section III.13.1.1.2.2.2.

[31] Settlement Agreement at Section 11.III.H.

[32] For the First Capacity Auction, Cost of New Entry = $7.50/kW- month. Cost of New Entry will be discussed later in the section addressing the mechanics of the Forward Capacity Auction.

[33] Section III.13.1.4.2.2.

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31. The project description must include several aspects, including the load zone where the project will be located and the type of demand resource, and as well as the types of measures that will be implemented (i.e., energy efficiency, load management distributed generation).[34]

4. De-listing Provisions for Existing Capacity Resources

32. The Settlement Agreement permits existing capacity resources to forego receiving capacity revenues for a commitment period by submitting bids to de-list from the capacity market. A de-listed resource has no obligation to bid into the Day-Ahead and Real-Time energy markets for the period for which it is de-listed, and does not have to honor ISO-NE's requests to reschedule maintenance.

33. All pre-auction de-list bids submitted during the qualification process and accepted by ISO-NE are binding and shall be entered into the Forward Capacity Auction as described in section III. 13.2.3.2(b). De-list bids that are above certain price thresholds specified in the Settlement Agreement will be subject to review by ISO-NE's Market Monitor.

34. The proposed rules on FCM provide for Market Monitor review of each Static De-List Bid, each Export Bid above 0.8 times Cost of New Entry and each Permanent De-List Bid above 1.25 times Cost of New Entry. This review is designed to determine whether these bids are consistent with the existing generating capacity resource's net risk-adjusted going forward costs.[35] Sufficient documentation and information must be included in the existing capacity qualification package to allow ISO-NE's Market Monitor to make such determinations. A Permanent De-List Bid priced between 0.8 times Cost of New Entry and 1.25 times Cost of New Entry will be presumed competitive unless the Market Monitor determines that the bid is an attempt to manipulate the Forward Capacity Auction.

35. Finally, existing generating capacity resources may submit de-list bids during the auction itself, by submitting a Dynamic De-List Bid. Dynamic De-List Bids are submitted during the auction at any price below 0.8 times Cost of New Entry. Such bids are not submitted to ISO-NE during the qualification process and therefore are not subject to review by the Market Monitor during the qualification process.

36. No later than 120 days before the Forward Capacity Auction, ISO-NE will send notification to existing capacity resources indicating whether the resources' de-list bids were accepted. Each accepted de-list bid will be binding and shall be entered into the

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[34] Existing resources are also required to submit qualification packages.

[35] Section III.13.1.2.3.2.1. These thresholds are expressly provided for in the Settlement Agreement. See Settlement Agreement at section 11.III.D.

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Forward Capacity Auction. The qualification determination will not include the results of the reliability review.

5. Composite Offers

37. All capacity resources offering capacity in the Forward Capacity Auction must offer and deliver a fixed amount of capacity throughout the year. However, certain demand resources exhibit variability in the total amount of capacity they are able to supply, due to the seasonal nature of the demand resource. A capacity resource exhibiting seasonal variability has the option of offering an amount of capacity into the Forward Capacity Auction that can be provided in all months across the whole year. Alternatively, such a demand resource may combine with another resource exhibiting complementary variability. For example an air conditioning reduction program (which has more kW of demand response to offer in the summer than winter) could pair with a combined cycle unit (which has more kW to offer in the winter than in summer). Such a combination is an offer composed of separate resources (composite offer).[36]

38. ISO-NE and stakeholders devised the concept of composite offers to allow seasonal demand resource to offer capacity into the Forward Capacity Auction. Separate resources may combine to participate in a Forward Capacity Auction as a single resource. The composite offer must be submitted and confirmed by each of the contributing parties and each must qualify individually.

6. Market Monitoring

39. The proposed rules state that ISO-NE's Market Monitor will have the authority to review in the qualification process each resource's summer Seasonal Claimed Capability if it is significantly lower than historical values.[37] This allows the Market Monitor to ensure that the resource's claims are not attempts to exercise physical withholding. The Market Monitor will also take "appropriate steps to ensure" that the de-list bids (other than Dynamic De-List Bids) submitted by new generating, import and demand resources are not replaced by that new capacity in a subsequent reconfiguration action. The Market Monitor may consult with sponsors or participants to clarify or address concerns over the submitted material.

7. Publication of Offer and Bid Information

40. The proposed rules state that each Permanent De-List Bid will be posted no later than three business days after the existing capacity qualification deadline.[38] This posting

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[36] Section III.13.1.5.

[37] Section III.13.1.7.

[38] Section III.13.1.8.

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will include the name of the resource, the quantity, the price, and load zone in which the resource is located. For Static De-List Bids, ISO-NE will post the quantity, price, and load zone no later than three business days after the same deadline. ISO-NE will post the name of submitter, quantity, and interface of export bids and administrative export bids, and of offers of new import capacity resources by the same deadline. ISO-NE will post the resource name, quantity, price, and load zone in which the resource is located of resources whose Static De-List Bid or Permanent De-List Bid above 0.8 times Cost of New Entry was approved. Personnel from state commissions will be provided confidential access to full information about posted Static De-list Bids and Permanent De-List Bids, upon request, pursuant to section 3.3 of the ISO-NE Information Policy.

8. Timeline

41. Beginning with the timeline for the commitment period commencing on June 1, 2016 (the seventh Forward Capacity Auction) and for each commitment period thereafter, the deadlines will be consistent for each commitment period, as follows: First, each commitment period will begin in June. Second, the new capacity Show of Interest submission window will be the November through December period that is approximately four years and six months before the beginning of the commitment period. Third, the existing capacity qualification deadline will be in April just over four years before the beginning of the commitment period. Fourth, the new capacity qualification deadline will be in June just under four years before the beginning of the commitment period. Finally, the Forward Capacity Auction for the commitment period will begin in February, approximately three years and four months before the beginning of the commitment period.

42. The time from the first day of the Forward Capacity Auction to the first day of the commitment period is 28 months for the first Forward Capacity Auction. That length of time extends to 40 months, pursuant to the Settlement Agreement, by the seventh Forward Capacity Auction. The market rules provide for a review of the issue and possible revisions to the schedule to increase the length of the planning period more quickly.

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B. Section 13.2: Mechanics of the Forward Capacity Auction[39]

43. ISO-NE states that the Settlement Agreement contemplated a 40-month planning period between each Forward Capacity Auction and the beginning of the associated commitment period. However, the proposed schedule for the first six Forward Capacity Auctions entails a shorter planning period for each of those Forward Capacity Auctions—increasing from 28 months to the 40 months referenced in the Settlement Agreement.[40]

44. The Settlement Agreement stipulates that Forward Capacity Auctions would be conducted as descending clock auctions.[41] Each Forward Capacity Auction will be made up of a series of rounds; these rounds will conclude only when all modeled capacity zones have arrived at clearing prices. A descending clock auction begins with a starting price; at that price all participating capacity is included and assumed to be providing capacity. During the Forward Capacity Auction, the price decreases and megawatts drop out of the auction until the desired quantity is purchased. The starting price will equal two times Cost of New Entry.[42]

45. The FCM's locational capacity market design allows for prices to differ across different zones within the New England control area. As prescribed by the Settlement Agreement, ISO-NE will determine capacity zones prior to the Forward Capacity Auction, which will be based on an identification of transmission limits that may bind. If

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[39] Section III.13.2 of the proposed rules on FCM describe the mechanics of the Forward Capacity Auctions. This section of the proposed rules is divided into nine subsections:

13.2.1	Timing of Auction
13.2.2	Amount of Capacity Purchased in each auction
13.2.3	Conduct of Forward Capacity Auction
13.2.4	Starting Price and Cost of New Entry determination
13.2.5	Treatment of Specific Offers
13.2.6	Capacity Rationing Rule
13.2.7	Determination of Clearing Price
13.2.8	Inadequate Supply and Insufficient Competition
13.2.9	2010/2011 Special Pricing Rule

[40] The Settlement Agreement requires that the Forward Capacity Auction, in most instances, will procure 100 percent of the Installed Capacity Requirement forecast for the commitment period. Settlement Agreement at 11.I.A. The proposed rules on FCM provide certain specified circumstances in which capacity purchases will be deferred until reconfiguration auctions.

[41] Settlement Agreement at 11.III.G.1 and 11.III.A.

[42] Settlement Agreement at 11.III.C.

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transmission limits (including predicted transmission upgrades that will be on-line by the commitment period) are expected to bind, separate capacity zones are designated and separate but simultaneous auctions are held for each zone.

1. Timing of Auction

46. Except with respect to the first six Forward Capacity Auctions, each Forward Capacity Auction will be conducted beginning on the first Monday in the February that is approximately three years and four months before the beginning of the commitment period.

2. Conduct of Forward Capacity Auction

47. Section III.13.2.3 of the proposed rules on FCM addresses how Forward Capacity Auctions are conducted. The proposed tariff is sub-divided into separate steps:

- Step 1: Announcement of Start-of-Round and End-of-Round Prices
- Step 2: Compilation of Offers and Bids
- Step 3: Determination of the Outcome of Each Round

a. Step 1: Announcement of Start-of-Round and End-of-Round Prices

48. Each Forward Capacity Auction will begin at a predetermined price – the Starting Price – which is two times Cost of New Entry.[43] There may be differing values of Cost of New Entry for these separate zones. The first round of the Forward Capacity Auction will begin at the Starting Price and conclude at the End-of-Round Price. After the first round, the Start-of-Round price for the next round will equal the End-of-Round Price from the previous round.

b. Step 2: Compilation of Offers and Bids

i. Offers from New Capacity Resources

49. The proposed rules require that new generating, import and demand resources that have been qualified to participate offer their full Qualified Capacity at the Starting Price.[44] New capacity resources are free to offer less or no capacity at prices below the Starting Price, subject to the other requirements of the proposed rules. The Settlement Agreement provides that the Market Monitor will review new capacity resources' offers

[43] Section III.13.2.3.1.

[44] Section III.13.2.3.2(a)(i).

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below a specific level (0.75 time Cost of New Entry).[45] New capacity resources must submit those offers to ISO-NE in their qualification packages, along with supporting information.

ii. Bids from Existing Capacity Resources Accepted in Qualification

50. As discussed earlier in this order, an existing capacity resource may submit de-list bids in order to remove itself from participation in the Forward Capacity Auction

iii. Existing Capacity Resources without Bids or whose Bids were not Accepted in Qualification

51. An existing capacity resource that did not seek to de-list prior to the auction will be automatically bid into each round of the Forward Capacity Auction at its summer Qualified Capacity. In order to remove itself from participation in the Forward Capacity Auction, such a resource must submit a Dynamic De-List Bid, which is submitted during the Forward Capacity Auction itself. A Dynamic De-List Bid does not require prior approval of ISO-NE's Market Monitor. In any round of a Forward Capacity Auction, when prices are 0.8 times Cost of New Entry or lower, any existing resource, other than those designated as self-supply, may submit a Dynamic De-List Bid.[46]

c. Step 3: Determination of the Outcome of Each Round

52. The proposed rules state that the auctioneer will use offers and bids submitted in a particular round to construct aggregate supply curves.[47] The auctioneer will construct a supply curve for the New England Control Area and for each modeled capacity zone included in the round. Generally, the information that is used to construct such curves will include the amount of capacity offered in capacity zones at prices within the round, the Installed Capacity Requirement, the Local Sourcing Requirement of any import-constrained zones, and the Maximum Capacity Limit of any export-constrained zones. On the basis of these aggregate supply curves, which reflect total system capacity, the auctioneer will determine the outcome of the round for each modeled capacity zone. Before the Forward Capacity Auction, capacity zones will be determined by ISO-NE based on an identification of transmission limits that may bind and if those limits are expected to bind.[48] However, the final set of distinct capacity zones will be based on actual Forward Capacity Auction results. If a modeled constraint does not bind in the

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[45] Settlement Agreement at 11.III.H.1.

[46] Section III.13.2.3.2(d).

[47] Section III.13.2.3.3.

[48] Section III.13.2.3.4.

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Forward Capacity Auction, the price in that zone will be the same as the price for an adjacent capacity zone. The final set of capacity zones that result from the Forward Capacity Auction will apply to all reconfiguration auctions applicable to that commitment period.

3. Starting Price and Cost of New Entry Determination

53. Each modeled capacity zone will have a Starting Price equal to two times the Cost of New Entry associated with that capacity zone. Under section III.13.2.4, Cost of New Entry for all capacity zones in the first Forward Capacity Auction will be $7.50/kW-month.[49] Cost of New Entry values for subsequent Forward Capacity Auctions will be calculated based on the clearing prices from previous successful auctions. After three successful Forward Capacity Auctions have been conducted for a given capacity zone, the proposed rules provide that the Cost of New Entry for that capacity zone in a Forward Capacity Auction will be the sum of 70 percent of that capacity zone's Cost of New Entry from the previous Forward Capacity Auction plus 30 percent of that capacity zone's clearing price from the previous Forward Capacity Auction.

4. Treatment of Specific Offers and Bids in Forward Capacity Auction

54. Offers from new generating, import and demand resources will "clear" the Forward Capacity Auction if the descending clock auction stops at a price at or above that specified in the offer.[50] Unless rejected for reliability reasons, a Permanent De-List Bid will clear[51] the Forward Capacity Auction if the clearing price is less than the price specified in the Permanent De-List Bid. The amount of capacity that is permanently de-listed capacity will be replaced either in the current Forward Capacity Auction or in subsequent annual reconfiguration auctions.[52] The clearing price in the Forward Capacity Auction will determine in which auction the de-listed capacity is replaced.

55. The proposed rules generally provide that, except where rejected for reliability reasons, a Static De-List Bid or an Export Bid will clear the Forward Capacity Auction if the clearing price is less than the price specified in the bid.[53] Similar to the provisions for Permanent De-List Bids, the Forward Capacity Auction clearing price will determine whether the de-listed capacity will be replaced in the Forward Capacity Auction or in

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[49] Settlement Agreement at 11.III.F.

[50] Section III.13.2.5.

[51] In contrast to offers to sell capacity, a Permanent De-List Bid clearing the market means that the existing capacity resource that submitted that bid no longer has an obligation to supply capacity.

[52] Section III.13.2.5.2.

[53] Section III.13.2.5.2.2.

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subsequent annual reconfiguration auctions. An Administrative Export Bid will clear in the Forward Capacity Auction regardless of clearing price and regardless of whether there is inadequate supply or insufficient competition in the capacity zone. The proposed rules state that a Dynamic De-List Bid will clear in the Forward Capacity Auction if the clearing price is less than the price specified in the bid.

56. Section III.13.2.5.2.5 addresses de-list bids that ISO-NE rejects for reliability reasons. ISO-NE will determine that an existing capacity resource is needed for reliability if the absence of that existing capacity resource would result in a violation of any criteria developed by the North American Electric Reliability Corporation or the Northeast Power Coordinating Council, or ISO-NE system rules.

57. Where ISO-NE has determined that some or all of the capacity associated with a de-list bid is needed for reliability reasons, then that capacity will not clear in the Forward Capacity Auction, and that resource will be notified following the Forward Capacity Auction.[54] Following the last reconfiguration auction, if ISO-NE determines that the reliability concern has not been addressed, then the resource will become a listed resource for the commitment period and will be compensated at a just and reasonable price, as determined by the Commission.[55] The proposed rules at present do not resolve the determination of a just and reasonable rate, the form of any reliability agreement or the process for obtaining a reliability agreement.

5. Determination of Clearing Prices

58. The proposed rules specify that the clearing price in an import-constrained zone cannot be lower than the clearing price in the Rest-of-Pool zone. Similarly, price in an export constrained zone cannot be higher than in the Rest-of-Pool zone.[56] The Settlement Agreement provided for a pricing mechanism applicable to the first three successful Forward Capacity Auctions (but no more than five actual Forward Capacity Auctions).[57] The price collar provision establishes a ceiling on the price for existing capacity resources at 1.4 times Cost of New Entry and a floor of 0.6 times Cost of New Entry until there have been three successful auctions. If the clearing price is above 1.4 times Cost of New Entry, existing capacity resources will be paid 1.4 times Cost of New Entry and new capacity resources will be paid the clearing price.[58] Clearing prices in the applicable Forward Capacity Auctions will not fall below 0.6 times Cost of New Entry. Where the clearing price reaches 0.6 times Cost of New Entry, ISO-NE will prorate offers so that no

[54] Section III.13.2.5.2.5.

[55] Section III.13.2.5.2.5(b).

[56] Section III.13.2.7.

[57] Settlement Agreement at 11.III.G

[58] Section III.13.2.7.3.

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more than the Installed Capacity Requirement is procured in the Forward Capacity Auction.

a. Alternative Price Rule

59. The Settlement Agreement provided for an Alternative Price Rule to be employed under certain circumstances. Under the Alternative Price Rule, the clearing price in a capacity zone would be set at $0.01 below the price at which the last remaining new capacity resource (located in that capacity zone) withdrew from the Forward Capacity Auction or Cost of New Entry, if all of several conditions were met. Generally, those conditions include but are not limited to situations in which the amount of new capacity required in the capacity zone is greater than zero, and the zone does not have inadequate supply.[59]

IV. DISCUSSION

60. The Commission conditionally accepts the proposed rules, while requiring modifications as discussed below. ISO-NE has already stated that it intends to make a filing with the Commission by or before September 1, 2007, setting forth the order of priority in which it will consider important issues relating to FCM.[60] Additionally, we will require ISO-NE to submit a compliance filing on or before September 1, 2007 making the modifications we order here.

A. Interaction of FCM and the Interconnection Queue

1. ISO-NE's position

61. ISO-NE states that several important policy and design issues related to the FCM arose during the stakeholder process, including the relationship between the FCM and the

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[59] A capacity zone is considered to have inadequate supply if, at the starting price, the amount of new capacity offered in that capacity zone is less than the amount of new capacity required in that capacity zone.

[60] *See* Transmittal, February 15 filing, at 22:

> Since [many of the remaining issues relating to FCM are] complex, discussion and resolution of the totality of the issues will require a significant expenditure of effort on the part of the ISO and its stakeholders. To assure that these efforts are efficient, it is necessary to prioritize these issues and devote resources to systematically consider and craft effective solutions to them. . . . The ISO will make a compliance filing setting forth a prioritization of issues on the earlier of September 1, 2007, or thirty days after a joint NECPUC/NEPOOL meeting where such prioritization is a major topic.

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interconnection queue process. The proposed rules on the FCM require that new resources seeking to qualify to provide capacity will be subject to an interconnection analysis that will assess the impact of the proposed project on the transmission system and assure that the proposed project will not result in transmission system violations, either on a stand-alone basis or in combination with other proposed projects. Under the present New England interconnection queue process, generation capacity is interconnected on a first-come, first-served basis.

62. ISO-NE agrees that "sole reliance on the queue is not an ideal solution" but argues that, before the details of queue process can be integrated with the FCM, several significant policy decisions must first be considered and resolved.[61] For example, ISO-NE argues that, while supplier participation in the capacity market is voluntary, a proposal that allocates interconnection rights through the FCM implies that FCM participation is mandatory for new resources. ISO-NE also claims that the question of intra-zonal deliverability, which the Commission has required ISO-NE to consider, is closely related to the relationship between the interconnection queue and FCM. Given this issue's overall complexity, ISO-NE has proposed to defer the development of a solution of this issue until after the filing of the FCM rules. ISO-NE acknowledges the importance of such issues and proposes to work with NECPUC and NEPOOL participants to prioritize them. As noted above, ISO-NE states that it will make a compliance filing prioritizing these issues by September 1, 2007 and asks that the Commission refrain from prejudging prioritization.

2. Protests and comments

63. NU, VDPS, the CT DPUC, NECPUC[62] and Mass DTE are concerned that the proposed rule would prevent resources with lower costs, but with lower queue positions, from participating in the Forward Capacity Auction. VDPS and the CT DPUC argue that the interconnection process can significantly influence the system-wide capacity auction. The CT DPUC and NECPUC assert that the interconnection queue could become a means for an existing supplier, with minimal investment, to lock out new competitors over many years by filing multiple interconnection applications. The CT DPUC and NECPUC assert that nothing in the Commission's interconnection orders authorized the use of queue position to disqualify prospective participants in competitive capacity markets. NECPUC and the CT DPUC further argue that there is no economic basis for selecting one project versus another based on being quickest to submit an Interconnection Request, as contained in ISO-NE's proposed rules on FCM.

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[61] Transmittal, February 15 filing, at 17.

[62] NECPUC's comments in this proceeding are joined by the Maine PUC and NHPUC.

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64. The CT DPUC and NECPUC argue that the Settlement Agreement recognized the need to resolve conflicts between the interconnection queue and the FCM by providing:

> If applicable for a specific Resource, while a full and complete System Impact Study is not a requirement to participate in the [Forward Capacity Auction], at a minimum, an initial interconnection analysis is required. The ISO and the Reliability Committee shall work out specifics with respect to the performance of such initial interconnection analysis and selection criteria (including auction details) for multiple projects when only a subset of such projects can be selected in the [Forward Capacity Auction] due to overlapping interconnection impacts.[63]

The CT DPUC argues that the Settlement Agreement contemplated the development of criteria that would further the objective of selecting new capacity resources on the basis of their competitive price and asserts that, had parties intended to maintain the status quo, the above provision would not have been necessary. NECPUC asserts that ISO-NE is in violation of this term of the Settlement Agreement if it fails to address, without delay, the conflicts between the interconnection queue and the Forward Capacity Auction. The CT DPUC asserts that the Commission, through its orders on interconnection procedures, has given ISO-NE latitude to develop interconnection procedures that address the region's needs, and that a range of specific selection criteria could be developed without violating the Commission's interconnection orders.

65. NECPUC and the CT DPUC contend that ISO-NE's proposal to prioritize a series of issues in six months' time assures that there will be no modification in place for the second Forward Capacity Auction and will likely create unjust and unreasonable results. In turn, this will perpetuate a queue-based disqualification procedure that would delay resolution and would "risk irrecoverable damage to the FCM's credibility."[64] Thus, they request that the Commission require all the stakeholders to address these questions in a fast-track settlement proceeding, and they propose the appointment of Commission Administrative Law Judge Lawrence Brenner for Settlement Judge. The CT DPUC also requests that ISO-NE be required to file a new rule addressing overlapping interconnection impacts by November 15, 2007, or in time to be implemented for the second Forward Capacity Auction.[65] The CT DPUC recommends replacing it with a cost-based selection mechanism.

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[63] Settlement Agreement at 11.II.B.3(c).

[64] CT DPUC protest at 16.

[65] The CT DPUC does not advocate delaying the first Forward Capacity Auction.

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66. The CT DPUC has also raised an issue with regard to intra-zonal deliverability standards. The Commission already has imposed a requirement that ISO-NE file a report by July 2, 2007, on how such standards should be addressed within the New England markets, along with a time frame for implementation.[66] The CT DPUC asserts that ISO-NE has emphasized the link between intra-zonal deliverability and qualification, and with the first Forward Capacity Auction looming further delay is not an option. CT DPUC asserts that new capacity resources need to know the long-term interconnection rules that ISO-NE will apply and how those rules affect qualification. NU similarly believes that ISO-NE should address the interconnection issues raised by the CT DPUC as quickly as possible.

67. In its answer, ISO-NE recognizes that redesign of the interconnection queue is the states' highest priority, but concludes that the November 15, 2007 date is unduly optimistic, given the complexity of this issue. ISO-NE also asserts that the formulation of a substitute proposal via the stakeholder process (given that the CT DPUC's proposal is still in the conceptual phase) will extend the time needed for resolution. ISO-NE states that, according to projections, less than 200 MW of new capacity resources will be needed in the first Forward Capacity Auction. Given that it received over 17,000 MW in Show of Interest Forms (including over 2200 MW of demand resources), ISO-NE concludes that, given the combination of a small demand and a large amount of supply, the likelihood is small that a unit included in the auction based on queue position having the effect of raising the clearing price. Finally, ISO-NE states that it has planned a series of meetings this spring with NECPUC and a variety of NEPOOL parties to accelerate the filing of its proposed priorities.

3. Commission Determination

68. The relationship between the interconnection queue and the qualification process is an important issue that merits serious and speedy consideration by all stakeholders. However, meeting the timetable proposed by the CT DPUC and others, in a fast-track settlement process, would impose an unreasonably short period of time in which to confront this complex issue. Moreover, the Commission is concerned that the tight timetable proposed, and the effort it would entail, could divert time and resources from the task of qualifying resources and conducting the initial Forward Capacity Auction. Thus the Commission will allow New England stakeholders to develop a prioritization list as part of its efforts to address the issues alluded to in the transmittal letter. The Commission finds that the rules governing capacity resource qualification, including the method of allocating interconnection space, should be transparent to all participants – existing and new – prior to the beginning of the qualification process. Given that the qualification process for the second Forward Capacity Auction will begin in

[66] Notice of Extension of Time, Docket No. ER04-433-000 (June 26, 2006).

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September 2007, the Commission finds that the tight timetable proposed is incompatible with this idea.

69. That said, the Commission considers the interconnection issue important and worthy of speedy resolution. ISO-NE's reaction to the protests indicates that this appears to be the most important issues to address. We agree. While we will not prioritize among the listed issues for the region, we believe that the interconnection queue issue is of sufficient importance to merit, at the very least, a position near to the top of any list of priority.

70. With regard to the Settlement Agreement, the Commission finds that the proposed rules on FCM do not violate the terms thereof. The Commission finds that there is nothing in the selected provision that precludes ISO-NE from relying upon, at the outset, a prioritization based on interconnection queue position. While the Commission agrees with all parties – the state agencies, Northeast Utilities and ISO-NE – that the filed provision is far from ideal, the Settlement Agreement requires simply that ISO-NE and the Reliability Committee "shall work out specifics with respect to the performance of such initial interconnection analysis and selection criteria."[67]

B. Issues Related to the Interaction of De-List bids and Reliability Must Run (RMR) Contracts

71. Existing RMR contracts approved by the Commission expire at the commencement of the first Forward Capacity Auction commitment period (June 2010). The Settlement Agreement provides that where a bid to remove a capacity resource from participation in the Forward Capacity Auction is rejected for reliability reasons, that resource will be "paid a just and reasonable price (as determined by FERC)."[68] The rules proposed in the instant filing, however, do not resolve the determination of a just and reasonable rate, the form of any reliability agreement, or the process for obtaining a reliability agreement. ISO-NE anticipates revising portions of the existing tariff and market rules to resolve these issues, which, it expects, will also require significant stakeholder review and Commission approval.

72. The CT DPUC, NECPUC, NHPUC, and Public Systems assert that, because the FCM is designed to minimize the need for RMR agreements in the future, the FCM should provide market signals to replace inefficient, more costly units that have been previously supported by RMR Agreements. If, however, such competition to displace existing RMR units does not materialize, CT DPUC, NECPUC, and NHPUC argue that ISO-NE and the Commission should investigate the causes and eliminate any unjustified impediments that may be disrupting efficient markets. Public Systems agree, asserting

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[67] Settlement Agreement at 11.II.B.3(c).

[68] Settlement Agreement at 11.III.K.

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that the current RMR agreements have "overwhelmed" New England's consumers and their role in FCM needs a redesign.[69] CT DPUC, NECPUC, and NHPUC recognize, however, that there may still be isolated instances when a unit is necessary for reliability but cannot be replaced in the Forward Capacity Auction or reconfiguration auctions. They support ISO-NE's conclusion that the Settlement Agreement requires replacement of resources whose de-list bids were rejected for reliability reasons with resources that do clear in the market at the earliest possible time.

73. As discussed below, parties have raised concerns as to the issue of how to treat needed capacity for the purposes of the Forward Capacity Auctions – i.e., what effect should the compensation paid to units needed for reliability have on the clearing price. ISO-NE initially recommended one method of pricing bids seeking to remove capacity from participation in the auction. However, participants raised concerns over that method during the stakeholder process. Some participants offered an alternative method of pricing these resources. ISO-NE notes that its initial review of that alternative is favorable, but that the proposal was advanced too late in the stakeholder process to receive full evaluation. Thus, ISO-NE commits to evaluate that alternative and make a filing with the Commission by June 30, 2007.

1. Just and Reasonable Compensation For Required Reliability Units

a. Positions of the parties

74. The CT DPUC, NECPUC, NHPUC and Public Systems state that ISO-NE properly found that the new reliability regime should not undermine the FCM by providing a generator needed for reliability an option to receive the *higher of* a traditional cost of service rate or a market rate. To avoid this problem, they suggest that the FCM should be structured so that (1) de-list bids are no greater than risk-adjusted going-forward costs; and (2) compensation for de-list bidders rejected for reliability should be no greater than their de-list bid. CT DPUC, NECPUC, and NHPUC maintain that FCM can only operate effectively if just and reasonable compensation for reliability units is based on going-forward costs.[70]

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[69] Public Systems support the proposed FCM structure that will provide several years to develop solutions (including the use of reconfiguration auctions) to instances where de-list bids are rejected for reliability purposes. With this amount of planning time, Public Systems argues that a market solution (rather than an RMR agreement) might address any potential reliability need, especially considering the Commission's stated position against the use of RMR agreements.

[70] The proposed FCM Rules define annual going-forward costs as "costs that might otherwise be avoided or not incurred if the resource were not subject to the obligations of a listed capacity resource during the commitment period (*i.e.*, maintaining

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75. The CT DPUC, NECPUC, and NHPUC note that (consistent with the proposed rules) the Settlement Agreement provides only that a capacity resource whose de-list bid is rejected for reliability reasons "shall be paid a just and reasonable price (as determined by FERC) . . . until it can be released to de-list."[71] CT DPUC, NECPUC, and NHPUC agree with ISO-NE that it may be desirable to have a defined basis for reliability units' compensation by the time of the first Forward Capacity Auction so that if a bid is rejected for reliability, the resource will fully understand the rate structure for compensation. The CT DPUC, NECPUC, and NHPUC argue that otherwise units needed for reliability would have perverse incentives to have their de-list bids rejected so that they could reap a higher compensation as a reliability unit.

76. Because the FCM Rules state that going-forward costs should not include costs that could be avoided in a single commitment period, CT DPUC, NECPUC, and NHPUC urge ISO-NE and the Commission to be vigilant in identifying capital improvements (*e.g.*, environmental upgrades) that generators may seek to cloak in the guise of "going-forward costs." This is because the benefit from those improvements will accrue to the unit's owners in operations beyond the one-year commitment period, either through continued operation of the unit, an increased sale price for the unit, or a higher salvage value. The CT DPUC, NECPUC, and NHPUC also argue that the Commission should clarify the Rules so that ISO-NE may only accept such capital improvements as "going-forward costs" in very limited circumstances – *e.g.*, (1) when the unit submits a Permanent De-list Bid and will shut down permanently without the improvement, (2) when the unit cannot operate reliably during the commitment period without the improvement, and (3) when the allowable cost of the improvement excludes all residual value at the end of the commitment period.

77. While acknowledging that ISO-NE will determine the rate in a future filing, NRG seeks clarification from the Commission that de-list bids do not constitute a just and reasonable rate for a generator whose bid is rejected for reliability reasons. NRG finds that these bids are not compensatory, as the level of reference costs for de-list bids does not include the fixed costs that are part of "doing business," including debt costs, depreciation expense, and return on equity. As such, NRG argues that the Commission should specifically state that it is accepting the use of going forward costs solely for the purpose of monitoring bid levels and that they do not reflect an appropriate measure of reliability compensation.

78. PSEG agrees with NRG's position, arguing that by design, de-list bids do not include the full cost of service needed to operate the resource. PSEG seeks clarification that that the owner of a unit whose de-list bid has been rejected because the resource is

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a constant condition of being ready to respond to commitment and dispatch orders)." *See* ISO Cover Letter at 76.

[71] Settlement Agreement at 11.III.K.

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needed for reliability purposes retains the option of seeking an RMR contract in lieu of accepting the de-list bid submitted in the auction as payment. In particular, PSEG believes that this should be available when a generator has submitted a Permanent De-List Bid to retire or mothball the unit. PSEG asserts that under the Settlement Agreement, it was "understood" that the option of obtaining an RMR contract with full cost-of-service rates would be preserved. PSEG states that the Settlement Agreement only addresses the termination of existing RMR contracts, and it did not preclude generators from seeking new RMR contracts. Otherwise, precluding any future opportunities to recover the full cost of operating a generating plant that is sustaining a loss and that the owner wishes to retire or mothball would amount to an improper and illegal confiscation of property.

79. In their answer, the New England PUCs (the CT DPUC, NECPUC and NHPUC) disagree with PSEG, noting that if reliability payments exceed a unit's de-list bid, it would subvert the FCM. These parties argue that such treatment would invite units to seek reliability agreement in those years when cost-of-service rate treatment will produce greater revenues, and to opt for market-based capacity payments whenever those revenues are likely to be greater. The New England PUCs argue that cost-of-service compensation has no legitimate place in the FCM, since de-list bids will reflect verified going-forward costs, and other markets will provide the requisite opportunity to recover fixed costs.

80. In their answer, the Capacity Suppliers state that the Commission should take no action on the comments of CT DPUC, NECPUC and Public Systems, as none of these parties actually request any specific relief in this proceeding. Further, the Capacity Suppliers note that the Commission also has rejected numerous attempts to limit RMR recovery to going forward costs. Finally, the Capacity Suppliers state that Market Rule 1 currently provides generators with the ability to seek recovery of their investment before the Commission and nothing in the Settlement Agreement or the proposed rules changes this provision.

81. Additionally, the New England PUCs argue in their answer that contrary to the positions offered by several parties, the Settlement Agreement did not permit a stakeholder process to decide just and reasonable compensation for units whose de-list bids are rejected for reliability reasons. Instead, the PUCs state that because the stakeholder process did not resolve this legal question, the Settling Parties agreed, and the Commission affirmed, that just and reasonable compensation for units needed for reliability must be determined by FERC. As a result, the PUCs argue that the Commission may not now authorize a stakeholder process to make a decision that the parties agreed would be made by the Commission on the basis of policy and precedent.

82. ISO-NE notes that section 11.III.K of the Settlement Agreement provides that where a de-list or export bid is rejected for reliability reasons, the resource will be paid a just and reasonable rate. However, ISO-NE states that the current proposed rules do not

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resolve how a just and reasonable rate will be determined, the form of the Reliability Agreement providing for a proposed just and reasonable rate, or the process for obtaining the Reliability Agreement. To resolve these issues, ISO-NE anticipates revising sections I.3.9 and I.3.10 of the Tariff along with the existing market rules dealing with Reliability Agreements and their compensation through a stakeholder process and subsequent filing with the Commission.[72] ISO-NE also commits to making a compliance filing establishing the prioritization of this and other issues to be resolved on the earlier of September 1, 2007 or thirty days after a NECPUC/NEPOOL meeting where such a prioritization is a major topic.[73]

b. <u>Commission Determination</u>

83. The Commission finds that, as ISO-NE states, the Settlement Agreement does not resolve the question of how a resource that is needed for reliability, and therefore not able to de-list, should be compensated. We further find reasonable ISO-NE's proposal for resolving this problem, through a stakeholder process that will develop a proposal for filing with the Commission.

84. The New England PUCs rely on the following section of the Settlement Agreement to support their argument that "just and reasonable" compensation for units needed for reliability must be "determined by FERC."

> A Capacity Resource having a Permanent De-list Bid, De-list Bid, or Export Bid that is rejected for reliability reasons shall be paid a just and reasonable price (as determined by FERC) from the beginning of the Commitment Period and, for Permanent De-list Bids, for each subsequent Commitment Period (unless the reliability concern is addressed before the start of the Commitment Period) until it can be released to de-list. In such cases, the ISO shall attempt to procure replacement capacity at each [Forward Capacity Auction] and annual reconfiguration auctions in order to release the capacity resource to de-list. Payments to such Resources shall continue only until the reliability concern is addressed (through procurement of replacement capacity or other means, such as a transmission enhancement).[74]

85. Nothing in this provision, however, precludes ISO-NE and stakeholders from proposing a methodology for determining a proposed just and reasonable rate for units needed for reliability. Further, we find that the Commission action requested here by various parties (including quantifying the duration of and the rate design for Reliability

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[72] Transmittal, February 15 filing at 18.

[73] *Id*. at 22.

[74] Settlement Agreement at 11.III.K.

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Agreements under FCM) would pre-judge ISO-NE's filing establishing the framework for Reliability Agreements under FCM. ISO-NE has committed to vetting this framework through the stakeholder process, and the Commission will review the revised market rules for Reliability Agreements in ISO-NE's resulting filing. While we will not order a date by which this filing should be made, we agree with ISO-NE that it would be desirable to have its Reliability Agreement process redesign in place before the first Forward Capacity Auction to provide a more transparent rate structure for compensation of units under any potential Reliability Agreements.

2. Revisions to Alternative Price Rule

86. In addition to raising issues regarding the method of determining compensation for units that seek to de-list but are required for reliability, parties have also raised issues as to the consequences that such compensation methods might have on the clearing price for all other units.

87. The Settlement Agreement created an Alternative Price Rule that modifies the way that the auction clearing price is determined in instances when out-of-market bids[75] exceed the required amount of new entry and certain other conditions are met. In essence, the Alternative Price Rule creates a higher clearing price than would otherwise be established.[76]

88. Proposed section III.13.2.5.2.5(f) states that beginning in April 2007, ISO-NE, in consultation with stakeholders and state utility regulatory agencies, will evaluate whether to modify the treatment of de-list bids rejected for reliability reasons. ISO-NE and these parties will evaluate whether to apply the Alternative Price Rule or a similar mechanism. The proposed rules also expressly state that by June 30, 2007, ISO-NE will file any potential rule changes related to the treatment of such bids or its recommendation not to institute any rule changes. ISO-NE adds that the proposed rule has been included in response to generators' concerns, raised late in the stakeholder process, that rejecting de-list bids for reliability reasons would reduce the auction clearing price and inappropriately dampen the signal for new entry.

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[75] "The ISO's [Market Monitor] will review any offer submitted by a new capacity resource below 0.75 times [Cost of New Entry]. If the [Market Monitor] determines that the offer is inconsistent with the long run average costs net of expected non-capacity revenues, then the amount of capacity associated with such offer that clears will be considered Out-of-Market Capacity for purposes of determining the applicability of the Alternative Capacity Price Rule." Transmittal, February 15 filing at 27.

[76] Settlement Agreement at 11.III.I.

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a. Protests and comments

89. The CT DPUC, Mass DTE, NECPUC and VDPS oppose the inclusion in the tariff of the provision for a stakeholder process that could result in changes in the Alternative Price Rule. They argue that the subsection is inconsistent with section III.I of the Settlement Agreement, which disqualifies existing capacity whose de-list bids have been rejected for reliability reasons from eligibility for a higher price under the Alternative Price Rule. Moreover, they contend, section 4A of the Settlement Agreement bars ISO-NE from making changes to the Alternative Price Rule unless ISO-NE demonstrates that the change is needed to prevent a negative effect on system reliability or security or the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. According to these parties, ISO-NE has not represented that a filing contemplated in the subsection can meet this standard.

90. By contrast, FirstLight states that it is pleased that ISO-NE has committed to consider solutions to the issue of the price-depressing effects of rejecting de-list bids for reliability reasons, but is concerned that ISO-NE has not committed to implementing a solution. FirstLight urges the Commission to condition its approval of the proposed subsection on the adoption of a method to address the price-collapsing effect in time for the first Forward Capacity Auction.

b. Commission Determination

91. We deny the requests of NECPUC and others to delete section III.13.2.5.2.5(f). We disagree that that section is inconsistent with the Settlement Agreement. Rather, it merely commits ISO-NE to a process that it could undertake, in any event, even without this provision. Even absent this provision, ISO-NE could initiate a stakeholder process to evaluate whether additional market rules need to be filed, pursuant to section 4A of the Settlement Agreement, to avoid an adverse effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. When and if ISO-NE elects to file such market rule changes, section 4A of the Settlement Agreement requires that ISO-NE demonstrate that the changes are needed to avoid these effects. We will not prejudge the outcome of these stakeholder deliberations, and we make no findings in this order about whether such additional rules are necessary. Thus, we deny FirstLight's request to condition our approval of this subsection on the adoption of a method to address the price effects of rejecting de-list bids for reliability reasons.

92. While the Settlement Agreement is intended to reduce or eliminate the need for RMR contracts, we agree with PSEG that the Settlement Agreement does not explicitly preclude the owner of a resource from seeking an RMR contract when the resource is needed for reliability and the resource cannot receive adequate compensation through the markets. Consistent with current RMR contract evaluations, when and if an entity seeks an RMR contract under FCM, we will consider the evidence presented in order to

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determine the need for the contract;[77] in light of ISO-NE's stakeholder process. However, it is reasonable to expect, though, that the circumstances under which generating units would seek RMR contracts would be more limited than in recent years in New England. Similarly, in response to NRG's comments, we will not address here the issue of what the just and reasonable compensation should be for a resource whose de-list bid is rejected for reliability reasons. Rather, when and if we are presented with a specific case in the future, we will consider the evidence presented and make our decision at that time.

3. Early Disclosure of Rejection of De-list Bids for Reliability Reasons

93. Proposed section III.13.2.5.2.5 of the FCM rules states that a generator whose de-list bid clears in an auction round but which ISO-NE determines cannot be allowed to de-list for reliability reasons, will not be informed that its de-list bid has been rejected for reliability reasons until the conclusion of the auction. ISO-NE states, in this regard, that it is not possible or appropriate to inform a generator that it might be needed for reliability prior to determining whether the resource would have cleared in the auction. ISO-NE states that the need for a resource might depend on which other resources clear in the auction. ISO-NE further states that if generators know they are needed for reliability, they will have an additional incentive to de-list to attempt to earn the higher of cost-based or market-based rates.

a. Protests

94. The CT DPUC, NECPUC, and NHPUC argue that if RMR agreements are to disappear, then ISO-NE and the states should promote the development of new resources in locations where new capacity is required. To support this position, these parties argue for complete transparency in all reliability determinations, as the earlier such information becomes available, the more likely it will be that competitive resources will respond. Finding that ISO-NE has taken some steps toward achieving the desired transparency, the CT DPUC, NECPUC, and NHPUC nonetheless assert that the Commission may need to require some modifications to the rules to stimulate the greatest competitive response.

95. For example, ISO-NE proposes to notify the de-list bidder only after the Forward Capacity Auction is concluded if its de-list bid did not clear because the unit is necessary for reliability. The CT DPUC, NECPUC, and NHPUC find that this approach is sensible in instances where new capacity has shown an interest in replacing existing units needed for reliability because ISO-NE cannot determine whether the new unit's offer will be accepted until the end of the Forward Capacity Auction. By contrast, the CT DPUC, NECPUC, and NHPUC assert that there may be other cases where ISO-NE can determine

[77] *Bridgeport Energy, LLC*, 112 FERC ¶ 61, 077 (2005) at P 39.

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from new capacity resources' Show of Interest Forms that there are no potential replacements for an existing unit that will be needed for reliability. In those cases, the CT DPUC, NECPUC, and NHPUC argue that the Commission should direct ISO-NE to modify the Rules so that it will notify the de-list bidder and prospective new capacity resources that the de-list bid will be rejected on reliability grounds. If ISO-NE publishes the reliability determination early, once it is certain that no other supplier will be available in the Forward Capacity Auction to fulfill that need, other potential resources can begin planning to participate in a reconfiguration auction to replace the rejected de-list bid.

96. Milford and NRG similarly object to ISO-NE's proposal, stating that it violates the fundamental right of market participants to the information they need to structure bids in the auction properly. Milford and NRG claim that failure to disclose that a unit whose de-list bid appears to have cleared the market will actually be required to run for reliability can result in the generator making economically harmful decisions in the auction. Milford and NRG notes that where a generator has several units at a single station, its de-list bids are interrelated because the units share various common costs; thus, if a de-list bid clears and the generator assumes that the unit will be retired, its de-list bids for the remaining units will be affected.

97. Milford and NRG also protest ISO-NE's contention that generators will have an incentive to de-list to attempt to earn the higher of cost or market if they know they are needed for reliability. Milford and NRG point out that a generator will not know if its unit is needed for reliability until the auction is run, and then, only in the round of the auction in which it appeared that the unit would be de-listed. Milford and NRG state that a de-listing generator runs a substantial risk of harming itself if it submits a de-list bid that is unrepresentative of its costs, and in addition, all bids above 0.8 times Cost of New Entry will be subject to Market Monitor review; thus, Milford and NRG state, the possibility for market manipulation is small.

b. <u>Commission Determination</u>

98. The Commission will not require ISO-NE to inform an existing generating capacity resource that its de-list bid has been rejected for reliability reasons until the conclusion of the auction. ISO-NE will be unable to determine whether a unit is required for reliability reasons until the conclusion of the auction. Only at that point will ISO-NE be able to assess the results of the auction and may determine that a resource that has submitted a de-list bid that cleared the auction is needed for reliability and cannot be allowed to de-list. Prior to that assessment, ISO-NE will not have sufficient information to make a determination that a resource seeking to de-list is needed for reliability. As such, we will not grant the relief requested by the protesters.

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C. Additional Issues Relating to De-List Bids

1. Rejection of De-List Bids by Market Monitor

a. Timing and Binding Nature of De-List Bids

i. Protests

99. ISO-NE proposes that all pre-auction de-list bids must be submitted to ISO-NE no later than the Existing Capacity Qualification Deadline, approximately nine months prior to the auction. All such de-list bids that are submitted and approved are binding. The bid is entered in the Forward Capacity Auction at the bid price and will clear if the auction price drops below the amount of the de-list bid. If the de-list bid is rejected by the Market Monitor, the resource that submitted it will then be entered into the Forward Capacity Auction as a price-taker and will take on a delivery obligation at the auction clearing price. An existing generating capacity resource will not be able to modify a de-list bid after it has submitted supporting documentation, to avoid undermining the integrity of the bidding and Market Monitor review process and the effective functioning of the market. ISO-NE further notes that the Settlement Agreement requires that de-list bids be posted, and if the postings are modified, market participants will receive less reliable information and the modified bids would not have met the posting requirement.

100. Exelon objects to the binding nature of de-list bids as not supported by the tariff, by sound competitive policy, or by fairness to generators. Exelon points out that under section I.3.9 of the existing rules, which are not amended by these new market rules, a unit is permitted to submit notice of retirement or deactivation at any time. Exelon argues that generators should be free to follow the current I.3.9 process unless and until it is changed. Exelon asserts that while a unit should be held to the de-list bid price if it does participate in the auction, there is no good reason why a generator should not be able to deactivate or retire a unit right up until the auction, because the auction function would be unaffected. Exelon claims that failure to allow retirement requests up until the auction could put a market participant at unreasonable risk. This is because if a unit submits a Permanent De-List Bid and the Market Monitor decided that the costs reflected in the bid did not reflect its determination of that unit's costs, the Market Monitor would reject the bid and insert the unit into the February 2008 auction at zero. Exelon states that if a generator is unwilling to accept this outcome, the generator should be free to opt out of the market entirely and retire the unit, assuming the unit is not needed for reliability. Exelon states that ISO-NE should not be able to force generators to participate in a market at a loss. Exelon further claims that if ISO-NE needs the unit for reliability, then the unit should be paid under an RMR contract.

101. Milford and NRG object to ISO-NE's proposal to make de-list bids binding when they are submitted, as opposed to when the de-list bids are accepted. Milford and NRG argue that ISO-NE's proposal is unreasonable and inconsistent with the Settlement

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Agreement. Milford and NRG assert that given the length of time between the Qualification Deadline and the auction, existing generating capacity resources should be allowed to lower their de-list bids closer to the date of the auction[78] to reflect changes in costs which are likely to change with time. Milford and NRG argue that allowing existing generating capacity resources to lower their de-list bids closer to the auction would produce a more efficient market outcome by allowing resources to stay in the market longer by lowering the price at which it would leave the market. Milford and NRG assert that ISO-NE's proposal should also be modified to permit existing generating capacity resources to adjust accepted de-list bids downward throughout the auction to enable those resources to offer more megawatts of capacity at lower prices.

102. NRG claims that a downward modification of an existing generating capacity resource's de-list bid at any time during the auction cannot present market power concerns and supplemental market monitor review of the adjusted bid should not be needed. NRG argues that the role of the Market Monitor is to police bids so that they do not exceed a certain threshold, not to prohibit the participation of an Existing Generation Capacity resource in the capacity market as a price taker.

103. Milford and NRG argue that the Settlement Agreement's requirement that de-list bids be posted within three business days of the Qualification Deadline is well before the bids are accepted or rejected, and is intended to provide a measure of guidance to the market, not finality. Milford and NRG state that new capacity resources with the advanced knowledge of the de-list bids of existing generating capacity resources will not know if a particular resource will be de-listed at the bid price because that bid may be rejected. Milford and NRG claim that there is nothing in the Settlement Agreement which requires that de-list bids should be binding months before the auction, and the premature posting of binding bids contributes nothing to the integrity of the auction process.

ii. Answers

104. In its answer, the CT DPUC claims there is no basis in the Settlement Agreement or in sound policy for permitting existing resources to change their de-list bids before or during the Forward Capacity Auction. The CT DPUC argues that if resources could de-list without restraint, an owner with market power in a capacity zone might be able to de-list some of its resources – i.e., physically withhold its capacity – in order to prop the price up artificially for the remainder of its fleet. The CT DPUC claims that the Settlement Agreement was designed to preclude precisely such action because uncontrolled de-listing can be used to exercise market power or to manipulate the price.

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[78] Specifically, Milford requests that existing generating capacity resources be allowed to reduce their de-list bids up to 30 days prior to the Forward Capacity Auction.

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105. The CT DPUC also argues in its answer that existing resources should not be permitted to change their de-list bids up to and during the auction process. The CT DPUC claims that such a provision would be inconsistent with the Settlement Agreement, which specifies that in order "to be considered in the [Forward Capacity Auction]," all de-list bids above 0.8 Cost of New Entry and all Permanent De-List Bids must be submitted to the ISO before the bid qualification deadline and will be posted one day after the bid qualification deadline. The CT DPUC argues that these provisions are important to allow de-list bids to be verified and to assure transparency. However, the goals of verification and transparency could not be satisfied – and would be rendered meaningless – if the Commission were to approve Market Rules permitting generators to modify their de-list bids, without review, at any time until the bid is "accepted" in the Forward Capacity Auction.

106. ISO-NE, in its answer, states that 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. ISO-NE argues that such information would be rendered meaningless if it could be subsequently modified or if bids could be withdrawn after acceptance. ISO-NE states that unless de-list bids were binding, new capacity could effectively be 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 of the market.

107. ISO-NE also states that NRG and Milford's argument that allowing an existing resource to alter its bid closer to the auction in order to reflect its costs more accurately is unsupported by the Settlement Agreement. ISO-NE further states that 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. ISO-NE also states that, as Exelon has asserted, a unit should be able to retire after the submission of a de-list bid but prior to taking on an obligation in the Forward Capacity Auction, subject to certain timing requirements. According to the clarification provided by ISO-NE, a unit may retire prior to the Forward Capacity Auction for a given commitment period, but may not retire after it has taken on a capacity commitment in the auction.

iii. <u>Commission Determination</u>

108. The Commission will reject the protesters' arguments regarding the timing and binding nature of de-list bids and accept ISO-NE's proposal. While the Commission recognizes Exelon's concerns, the Commission finds that its directive (in subsequent sections of this order), to ISO-NE to revise the proposed FCM rules and allow existing generating capacity resources to submit revised de-list bids that are consistent with the Market Monitor's determination of costs provides these resources with assurance that if it cannot recover its costs in the Forward Capacity Market, it will be allowed to exit the market. Further, as ISO-NE clarifies in its answer, "a unit may retire prior to the

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[Forward Capacity Auction] for a given Capacity Commitment Period. If it chooses to do so, the unit will not be entered into the [Forward Capacity Auction] and its capacity will be replaced," subject to the timing requirements that ISO-NE notes.[79] ISO-NE's proposed FCM Rules do not preclude or revise the current New England market rules for the retirement of resources that allow generating resources to submit notice of retirement at any time, given a notice period of sixty days and subject to a reliability review by ISO-NE.[80]

109. The Commission finds Milford and NRG's argument that an existing generating capacity resource be allowed to alter its de-list bid as the auction approaches unpersuasive. First, the public posting provisions detailed in the Settlement Agreement would be rendered meaningless if resources had the ability to change their de-list bids as the auction approached. The purpose of the Settlement Agreement was to provide market transparency as to the actual de-list bids submitted by existing generating capacity resources. Allowing resources to alter those bids essentially removes any reliability from the posting requirement and counters the market transparency goal intended by the Settlement Agreement. Further, as ISO-NE points out in its answer, non-binding de-list bids would subject new capacity to the risk of being undercut by subsequently reduced high de-list bids, making it easier for existing resources to reduce competition by lowering prices until competitors are driven out the market.

110. Additionally, the time period lag between the time de-list bids are initially submitted, i.e., the Qualification Deadline, and the date requested by the protesters to change de-list bid levels, i.e., 30 days prior to the Forward Capacity Auction, is just one sixth of the amount of time between the Forward Capacity Auction and the relevant capacity commitment period. The nature of a forward market involves estimation of costs far in advance of the delivery period. The slight benefit that may be achieved by allowing existing generating capacity resources to lower their de-list bids closer to the Forward Capacity Auction is outweighed by the diminution in reliability of the public posting of de-list bids and reduction in market transparency such an action would cause.

b. Market Monitor Review

i. Protests

111. Under proposed section III.13.1.2.3.2 of the FCM rules, ISO-NE's Market Monitor will review each Static De-List Bid and Export Bid above 0.8 times the Cost of New Entry, and each Permanent De-List Bid above 1.25 times the Cost of New Entry, submitted by existing generating capacity resources. The Market Monitor will review

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[79] ISO-NE answer at 10, 76.

[80] Section I.3.9 of the ISO-NE Transmission, Markets, and Services Tariff, FERC Electric Tariff Volume No. 3.

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such bids to determine whether the bid is consistent with the resource's net risk-adjusted going forward costs and opportunity costs. The proposed rules states that where the Market Monitor determines that the bid is inconsistent with the resource's costs, that de-list bid will be rejected and the resource will be entered into the Forward Capacity Auction as a price taker. In such case, the Market Monitor must provide an explanation of why the bid was rejected in an informational filing to be made with the Commission no less than 90 days before the first day of the Forward Capacity Auction. ISO-NE states that this will provide the de-list bidder with a forum to dispute ISO-NE's rejection of its bid and seek a remedy from the Commission.

112. Milford and NRG argue that ISO-NE's proposal would mitigate bids below existing resources' costs, so that the resource would be forced to offer capacity at a loss. Capacity Suppliers state that if the Market Monitor disputes any portion of the de-list bidder's bid, then the entire bid will be rejected, even if there is agreement between the Market Monitor and the de-list bidder regarding the majority of the cost components of the bid. During that time, the de-list bidder can seek relief from the Commission; however, due to the timing of the filing – no less than 90 days before the Capacity Auction – Capacity Suppliers point out that the existing generating capacity resource would be forced to participate in the Forward Capacity Auction as price takers. Capacity Suppliers state that it is almost certain that the Market Monitor and the de-list bidder will disagree on a material issue of fact if a bid is rejected, because the proposed rules require the Market Monitor to seek additional information from and engage in consultation with the de-list bidder prior to rejecting a bid. They argue that it is unlikely that the record of an informational filing and an intervening protest will be sufficient for the Commission to render a decision within the 90 days allotted. Therefore, Capacity Suppliers point out that there is a strong probability that a rejected bid will result in the existing generating capacity resource being forced into participating in the Forward Capacity Auction at a price level that may be insufficient to cover the resource's costs.

113. Milford and NRG suggest an alternative that would involve the Market Monitor disclosing its cost component-by-cost component review of an existing generating capacity resource's bid. Milford and NRG state that in the event a bid is then rejected, the affected resource could then submit an acceptable bid rather than be entered as a price taker. Milford and NRG note that this would avoid depressing the capacity clearing price. Milford and NRG argue that the Settlement Agreement does not prohibit this alternative proposal and will impose no additional burden on ISO-NE, because ISO-NE will still have to make a determination of what constitutes an acceptable bid. Capacity Suppliers propose to allow the participant to submit a de-list bid consistent with the Market Monitor's determination of justified bid components. The Capacity Suppliers claim that such a process would be permitted by the Settlement Agreement and is

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consistent with the New England day-ahead and real-time energy markets,[81] as well as PJM's version of a forward capacity market, the Reliability Pricing Model.[82]

114. Capacity Suppliers also assert that their alternative proposal would not encourage existing generating capacity resources to submit high de-list bids. Capacity Suppliers argue that existing generating capacity resources have many incentives to submit de-list bids consistent with their costs. First, Capacity Suppliers note that all data submissions are subject to audit and penalties. Second, Capacity Suppliers state that accepted de-list bids are binding as to both quantity and price, so the resource will be out of the market if the capacity clearing price falls below the accepted de-list bid.

ii. Answers

115. In its answer, the CT DPUC argues that whether ISO-NE enters a de-list bid adjusted to reflect the Market Monitor's findings or the generator enters the bid on the same basis, the result is the same: generators will still have an incentive to submit excessive de-list bids, recognizing that they have nothing to lose because the Market Monitor will adjust the bid – directly or indirectly – to include only verifiable going-forward costs. The CT DPUC asserts that such a mechanism would be unworkable and is inconsistent with the Settlement Agreement.

116. ISO-NE points out in its answer that the Settlement Agreement does not provide that if a bid is found to be inconsistent with the resource's going forward costs, the Internal Market Monitor shall determine and submit, on behalf of the generator, a bid that is consistent with the resource's going-forward costs. ISO-NE further states that 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 Internal Market Monitor will have a "benchmark." ISO-NE states that 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.

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[81] In these markets, the Market Monitor develops a cost-based proxy bid for all resources and, if certain market thresholds are triggered, the Market Monitor resets a resource's energy bids down to its proxy bids.

[82] Section 6.5(a)(i) of the PJM Open Access Tariff states that mitigation will be applied to generating capacity resources that submit "sell offers" of unforced capacity that is: 1) greater than the market seller offer cap applicable to such resource; and 2) would, absent mitigation, increase the clearing price in the auction. If these thresholds are met, the sell offer is adjusted downward to equal the market seller offer cap, as established by the PJM Market Monitor.

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iii. Commission Determination

117. The Commission agrees with the protesters and finds that ISO-NE's proposal could result in an existing generating resource being forced to offer capacity at a price less than its net risk-adjusted going forward and opportunity costs. In other words, the compensation received by the de-listed resource may not allow it to recover costs that might otherwise be avoided or not incurred if the resource were not subject to the obligations of a listed capacity resource during the commitment period. Such a result is unjust, unreasonable, and may act as a disincentive for de-listed resources to participate in Forward Capacity Auctions and the FCM more generally.

118. The Commission offers the following example as an illustration of how ISO-NE's proposed FCM rules can result in unjust, unreasonable, and confiscatory ratemaking. Suppose Cost of New Entry is determined to be $10.00/kW-month. Suppose an existing generating capacity resource submits a Static De-List Bid of $9.00/kw-month, or exactly 0.9 times Cost of New Entry. Since the Static De-List Bid is greater than the mitigation threshold of 0.8 times Cost of New Entry, the Market Monitor would undertake a review of that resource's de-listing bid. If, after due consultation with the resource, the Market Monitor determines that a more appropriate level for that the resource's Static De-List Bid would be $8.50/kW-month, or 0.85 times Cost of New Entry, the Market Monitor would then submit an informational filing to the Commission 90 days prior to the auction containing the reasoning and cost support of rejecting the $9.00/kW-month Static De-List Bid. If the Commission agrees with the Market Monitor that $8.50/kW-month Static De-List Bid is a more accurate reflection of the affected resource's costs, then under the proposed FCM rules, the Static De-List Bid's rejection would be upheld, and the resource would be entered into the Forward Capacity Auction as a price taker.

119. The proposed FCM rules do allow the affected existing generating capacity resource whose de-list bid has been rejected to submit a Dynamic De-List Bid during the Forward Capacity Auction that is not subject to review or mitigation by the Market Monitor, but the price level of that Dynamic De-List Bid cannot exceed 0.8 times Cost of New Entry. In the Commission's example, therefore, 0.8 times the Cost of New Entry is $8.00/kW-month; therefore, if the capacity clearing price drops below $8.00/kW-month, the resource in the example would be able to de-list and would not be forced to provide capacity at a price lower than its net risk-adjusted going forward costs. However, if the price that clears in the Forward Capacity Auction is greater than 0.8 times Cost of New Entry, but still below the Market Monitor's determination of the resource's costs, the resource would be forced to provide capacity at a price that both the Market Monitor and the generator agree is below the costs for that resource. In the Commission's example, if the capacity price cleared at $8.25/kW-month, the resource would not be allowed to exit the market and would be forced to offer capacity at a price $0.25/kW-month below the cost-appropriate level determined by the Market Monitor and affirmed by the Commission. The resource would not have the option of leaving the market, despite the

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fact that the clearing price was lower than its costs. This would be an unjust and unreasonable result.

120. The Commission finds Milford and NRG's requested relief to be just and reasonable. The Market Monitor, in reviewing de-list bids above certain price thresholds, will be required to determine an accurate and appropriate bid level for an existing generating capacity resource consistent with its net risk-adjusted going forward and opportunity costs. The Commission will require the Market Monitor to disclose the results of its review, including all cost components and appropriate input levels used in its mitigation formula. The Commission will also require ISO-NE to amend the proposed FCM rules to allow existing generating capacity resources whose Permanent De-List, Static De-List, Export, or Administrative Export bids are determined to be inconsistent with their net risk-adjusted going forward and opportunity costs, as determined by the Market Monitor, be allowed to submit revised de-list bids consistent with the price level determined by the Market Monitor. This requirement will provide the existing generating capacity resource with the option of submitting a revised de-list bid consistent with the Market Monitor's determination and would prevent any possibility of confiscatory ratemaking.

121. Specifically, in the September 1 compliance filing ordered above, the Commission will require ISO-NE to modify section III.13.1.2.3.2.1.1 of the proposed FCM rules to state that in the event a de-list bid is rejected by the Market Monitor, ISO-NE must provide the affected existing generating capacity resource its determination of the resource's net risk-adjusted going forward and opportunity costs. Further, the proposed FCM rules should be revised to provide that the resource has the option of submitting a revised de-list bid consistent with the Market Monitor's determination, subject to Commission review in the planned informational filing to be made 90 days before the Forward Capacity Auction.[83]

122. In the Commission's example above, Milford and NRG's proposal would have prevented the existing generating capacity resource from being forced to offer capacity at a price below its costs. The resource would have been informed by the Market Monitor that a more accurate and appropriate level for its Static De-List Bid, based on its net risk-adjusted going forward and opportunity costs, would have been $8.50/kW-month. The resource could then have had the option of re-submitting a Static De-List Bid of $8.50/kW-month. Once the capacity price dropped below $8.50/kW-month, settling

[83] The informational filing should include cost support for all cost components of the Market Monitor's determination, cost support for the existing generating capacity resource's original de-list bid, and an explanation of the difference between the Market Monitor's cost determination and that of the existing generating capacity resource.

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eventually at $8.25/kW-month, the resource would have been out of the capacity market and not forced to offer capacity at a price below its costs.

123. ISO-NE's concern that it is not the proper role for the Market Monitor to set default bids for existing generating capacity resources is unfounded. In order to review a de-list bid for mitigation purposes, the Market Monitor must determine what the net risk-adjusted going forward and opportunity costs for a resource, including appropriate levels for each cost component. Armed with that information, the Market Monitor would have ample information to determine an appropriate cost-based de-list bid for that resource; in fact, in order to make a determination on the resource's de-list bid, the Market Monitor must have an appropriate de-list bid level for comparison purposes. By imposing this disclosure requirement, the Commission is only requiring the Market Monitor to provide a cost component-by-cost component analysis of a proper cost-based de-list bid for the resource under review. This will not place an undue burden on ISO-NE or its Market Monitor.

124. The Commission also recognizes ISO-NE's concern that requiring the Market Monitor's determination of the proper cost components be disclosed to the affected resource may encourage price searching behavior on behalf of the existing generating capacity resources. As such, we will require ISO-NE to include, in the informational filing to be made 90 days prior to the Forward Capacity Auction, an analysis of evidence, if any, of price searching behavior on behalf of existing generating capacity resources.

125. Certain provisions of the rules provide for the Market Monitor to make determinations as to whether a generator is seeking to manipulate the Forward Capacity Auction or to engage in physical withholding.[84] The Commission's Market Monitoring Policy Statement provides that:

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[84] Section III.13.1.2.3.2.3 (Administrative Export De-list Bids) and section III.13.1.2.3.2.2 (Permanent De-List Bids) state that the Market Monitor can reject these bids if it determines that the bid is an attempt to manipulate the Forward Capacity Auction. Similar language is included in section III.13.1.3.5.6.1 (Offers from Import Capacity) which states that an offer from an existing Import Capacity Resource or a New Import Capacity Resource shall be rejected if the Market Monitor determines that the bid is an attempt to manipulate the Forward Capacity Auction. Finally, section III.13.1.2.2.5.2 states that the Market Monitor is required to review certain bids by existing generation resources, existing demand resources or existing import capacity resources to ensure that the bid is not an attempt to manipulate the Forward Capacity Auction. Section III.13.1.7, Internal Market Monitoring Review of Offers and Bids, states that the Market Monitor shall have the authority to review in the qualification process each resource's summer historical values to ensure that they are not attempts to exercise physical withholding.

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> If, in the course of monitoring participant behavior, the Market Monitor finds that an action by a market participant may require investigation and evaluation, or may be a potential violation of a market rule contained in an ISO/RTO filed tariff, or may be a violation of the Market Behavior Rules, the Market Monitor should notify the Commission staff. In this way the Commission will act in cases where market participants' behavior falls outside of the limited area of objectively identifiable, specific penalty rule violations the ISO/RTO may administer. [85]

126. The Market Monitor does not have the authority to make the determination as to whether or not there has been an attempt at manipulation or physical withholding. Therefore, ISO-NE is directed to revise sections III.13.1.2.3.2.3, III.13.1.2.3.2.2, and III.13.1.3.5.6.1, to state that if the Market Monitor determines that a bid or offer may be an attempt at manipulating the auction, the Market Monitor shall not only reject the bid or offer, but also will refer to the Commission the alleged attempt at manipulation, in accordance with the referral protocols set forth in Appendix A to the Policy Statement on Market Monitoring. Similarly, ISO-NE is directed to revise section III.13.1.2.2.5.2 to state that, if in its review of certain bids by existing generation resources, existing demand resources or existing import capacity resources the Market Monitor determines the bid may be an attempt to manipulate the Forward Capacity Auction, the Market Monitor shall refer the alleged attempt to the Commission. Finally, ISO-NE is directed to revise section III.13.1.7 to state that if the Market Monitor finds in its review of a resource's summer historical values that there may be an attempt to exercise physical withholding, the Market Monitor will refer the alleged physical withholding to the Commission. ISO-NE is directed to make this compliance filing by September 1, as ordered above.

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[85] *Market Monitors in Regional Transmission Organizations and Independent System Operators*, 111 FERC ¶ 61,267 (2005) (Market Monitoring Policy Statement) *(*footnotes omitted*)*. The Commission's Market Monitoring Policy Statement predated the current anti-manipulation rules, and so refers instead to the former Market Behavior Rules. Market Behavior Rule 2, dealing with manipulation, and Market Behavior Rule 6 have since been rescinded. *See Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 114 FERC ¶ 61,165 (2006). The other Market Behavior Rules have been codified at 18 C.F.R. § 35.37. In addition, the current anti-manipulation rule is now found in 18 CFR §§ 1c.2. *See Prohibition of Energy Market Manipulation*, Order No. 670, 71 Fed. Reg. 4244 (January 26, 2006), FERC Stats.& Regs. 31,101, *order denying reh'g*, 114 FERC ¶ 61,300 (2006).

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c. Market Monitor's Use of Reference Costs

i. Protests

127. According to ISO-NE's proposal, the New England Market Monitor will review all de-list bids above given thresholds. ISO-NE's proposed mitigation formula incorporates historical data for prices, outages, and the cost of replacement capacity. ISO-NE also proposes to use a historical Equivalent Forced Outage Rate (EFORd) for the unit as basis for the outage risk and the Forward Capacity Auction floor price as the cost of replacement.

128. NRG claims that that use of historical data for prices, outages, and the cost of replacement capacity is not likely to be representative of future performance and market expectations, and will lead to artificially depressing the level of acceptable de-list bids. NRG argues that use of "expectations of future market revenues"[86] is likely to yield a more accurate assessment of costs than historical data. NRG further asserts that the mitigation formula's use of EFORd as the basis for outage risk and the Forward Capacity Auction floor price as the cost of replacement will systematically understate a generator's costs. NRG states that under the Settlement Agreement and proposed FCM rules, a generator's risk of availability penalties is greater than it would be using historical EFORd. NRG notes that under the proposed FCM rules, a unit that is unavailable during Shortage Events in a commitment period can lose up to 10 percent of its annual capacity payment in a single Shortage Event, up to two and a half times its annual capacity payment in a single month, and up to its entire annual capacity payment over the commitment period. NRG claims that this risk factor is not captured in ISO-NE's proposed mitigation formula.

ii. Answers

129. The CT DPUC states that EFORd provides an unbiased gauge of a unit's performance experience and, thus, is a reasonable predictor of its future performance. The CT DPUC further states that the fact that the availability criteria under the FCM are not the same as under EFORd does not mean that EFORd may not reasonably be used to provide an impartial standard for calculating risk-adjusted going-forward costs. Further, according to the CT DPUC, NRG has offered no alternative other than each owner's self-interested perception of risk.

130. In its answer, ISO-NE states that the Settlement Agreement provisions associated with review of bids and offers by the Market Monitor were designed to measure accurately the risk-adjusted going forward costs and opportunity cost for each generator while minimizing the potential for market power, manipulation and withholding. ISO-NE asserts that there is no objective way to measure future market revenues in the

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[86] *See* NRG Protest at 15.

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context proposed by NRG and Milford, and thus historical data are the best indicia of prices in the near future.

131. Regarding use of EFORd, ISO-NE states that 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. ISO-NE states that unit outage risk actually measures the Day-Ahead Energy Market risk faced by a generator in the capacity market. ISO-NE states that 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. ISO-NE states that EFORd is the best measure of the likelihood a generator would be put into the above-described situation because it is the best available measure of outage risk, i.e., unavailability, in a given hour. ISO-NE states that this risk has no relationship to Shortage Events and capacity market payments as argued by NRG. ISO-NE states that NRG's contention that the reduction in capacity payments from failure to perform during Shortage Events is a component of going-forward costs is inaccurate. Rather, according to ISO-NE, capacity market payments are going-forward benefits. ISO-NE points out that the design of the FCM never requires a generator to pay money to remain in the market. ISO-NE states that 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.

132. ISO-NE argues that NRG and Milford's request to seek modification of the formula to take into account company-specific factors in the determination of reference costs should be denied. ISO-NE asserts that this request should be denied because NRG and Milford have not identified any risks that could be avoided by leaving the capacity market that are not already included in the formula.

iii. Commission Determination

133. The Commission disagrees with NRG's assertion that use of historical data for prices, outages, and the cost of replacement capacity will not be representative of future performance and market expectations. Prediction of pricing and outage data is not a perfect science; however, as the Commission has previously found,[87] use of historical data is likely to be the most accurate and reliable predictor of future market conditions. Further, NRG has offered no reasonable measurable alternative to use of historical data in the Market Monitor's mitigation formula.

134. The Commission will also deny NRG's requested relief regarding use of EFORd as the basis for outage risk in the Market Monitor's mitigation formula. EFORd is an industry-wide standard measure of outage risk used extensively in markets across the

[87] *See Electric Energy, Inc.*, 113 FERC ¶ 61,245 at P 21 (2005).

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country.[88] As ISO-NE points out in its answer, EFORd is the best measure of the likelihood a generator would have 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 available measure of outage risk, i.e., unavailability, in a given hour, and is therefore appropriate to measure this risk of outage. As ISO-NE states in its answer, this outage risk has no relationship to Shortage Events and capacity market payments as argued by NRG. Additionally, NRG has failed to propose any reasonable alternative to EFORd as a measure of outage risk.

135. The Commission will also deny NRG and Milford's request to modify the mitigation formula in order to account for unit-specific risk factors. NRG and Milford have failed to identify any such unit-specific avoidable risks for which the proposed mitigation formula does not already account.

2. De-Listing Due to Changes in Ambient Air Temperature

a. Protests

136. Section III.13.1.2.3.2.4. of the proposed rules states the conditions for Static De-List Bids due to ambient air conditions. The capability of some generators is temperature dependent, with their output decreasing as ambient air temperature increases. This means that some generators may not be able to generate their Qualified Capacity above 90 degrees, the temperature used to determine Summer Seasonal Claimed Capability, subjecting these generators to availability penalties. ISO-NE thus allows generators to de-list the capacity they expect to be unavailable at 2 times Cost of New Entry, subject to verification of the physical limit. ISO-NE states in its filing that it is uncomfortable with permitting generators to de-list due to ambient air temperatures below 2 times Cost of New Entry. ISO-NE is concerned that this could result in some bids not clearing the market. ISO-NE states that the proposed rule would prevent the exercise of market power because it would prevent generators from constructing a supply curve of the de-list bids and thus attempting to manipulate the price. It restates these arguments in its answer.

137. NRG and Milford disagree with section III.13.1.2.3.2.4. of the proposed rules which requires that de-list bids for ambient air conditions be at a uniform price of 2 times Cost of New Entry, and instead asks the Commission to modify the rules to allow these de-list bids at up to 2 times Cost of New Entry. NRG and Milford state that requiring

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[88] *See ISO New England Inc.*, 111 FERC ¶ 61,185 at P 32 (2005); *New England Power Pool*, 100 FERC ¶ 61,287 at P 12, 96-98 (2002), *order on rehearing*, 103 FERC ¶ 61,034 at P 77 & n.29 (2003); *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 114 & n.115-116 (2006); *New York Independent System Operator, Inc.*, 96 FERC ¶ 61,251 (2001).

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capacity to be bid at a uniform price prevents a generator from reflecting its actual costs in a de-list bid. NRG and Milford further state that the section III.13.1.2.3.2.4. rules are at odds with the basic rules requiring that de-list bids in general reflect actual costs.

138. The CT DPUC believes that ISO-NE's objective of accurately stating available capacity is legitimate, though it is concerned that allowing de-list bids based on ambient air conditions will likely increase the amount of new capacity that load must procure in the auction. The CT DPUC claims that generators may attempt to minimize the risk of availability penalties by de-listing any capacity above what they believe will be available on the hottest summer days. The CT DPUC claims that this strategy may be more attractive because the de-listed capacity would not be subject to peak energy rent reductions, so that generators can recoup part of the capacity payment foregone by the de-list bid. The CT DPUC emphasizes that the Settlement Agreement's restrictions on de-list bids were an essential element of the agreement because generators may have an incentive to de-list – including to account for ambient air temperature – when doing so will facilitate exercise of market power.

139. The CT DPUC recommends that the Commission approve this proposed rule subject to three specific conditions. First, the CT DPUC states that the Commission should require ISO-NE to conduct aggressive validation of de-list bids based on ambient air temperature to prevent exercise of market power. Second, the CT DPUC states that the Commission should reject the suppliers' proposal that they be permitted to de-list at less that 2 times Cost of New Entry due to ambient air temperature. Third, the CDPUC requests that the Commission require ISO-NE to modify the rule to limit its application to existing generating resources as of the first Forward Capacity Auction, and that new generation entering the Forward Capacity Auction should be designed to produce its qualified capacity at times of peak load and offers in the Forward Capacity Auction should reflect new generators' costs for providing that reliability service.

140. In their answer, Capacity Suppliers argue that the exclusion of new units requested by the CT DPUC should be rejected. Capacity Suppliers state that the CT DPUC ignores the fundamental physics of modern gas turbine design and the relationship of air density and temperature. Capacity Suppliers note that there is not a risk of gaming ambient air temperature adjustments by new units, since temperature-related derates are easily described in straightforward engineering analyses. Capacity Suppliers note that excluding new generators from ambient air de-listing would require new generators to install inlet chilling, even when the added capital and operating costs would not be efficient in a market setting. Capacity Suppliers further point out that allowing the CT DPUC's proposal would create a vintaging rule, which the Commission has rejected before and which would violate the the explicit endorsement in the Settlement Agreement that old units and new units are to be treated the same, *i.e.*, that all units that clear the auction are paid the same price regardless of vintage.

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b. Commission determination

141. We recognize that the capability of some generators is temperature dependent, with their output decreasing as ambient air temperature increases. We agree that generators should have the ability to partially de-list if they expect to be unable to produce full capacity due to ambient air temperature.

142. We also agree with generators that it is unreasonable to prohibit them from submitting de-list bids for temperature-dependent capacity at prices below 2 times Cost of New Entry. Therefore, by September 1, we will require ISO-NE to revise its market rules to permit generators with temperature-dependent capacity to de-list at prices below 2 times Cost of New Entry. If some generators can reverse the loss of temperature-dependent capacity by taking measures whose cost is less than 2 times Cost of New Entry, customers would benefit from allowing such generators to make that additional capacity available at prices below 2 times Cost of New Entry. Moreover, we do not understand ISO-NE's concern about market power in this instance. Allowing generators to submit de-list bids for temperature-dependent capacity at prices below 2 times Cost of New Entry will help to lower capacity prices and should not increase capacity prices, because such a rule would encourage additional supplies at prices below 2 times Cost of New Entry. Market power is exercised by withholding capacity from the market in order to increase prices. But ISO-NE's proposal would not lower prices and would not prevent withholding. To the contrary, ISO-NE's proposal could force some generators to withhold temperature-dependent capacity that they would be willing to keep in the market at prices below 2 times Cost of New Entry.

143. We disagree with the CT DPUC that de-list bids due to ambient air temperature should only apply for existing generation. Dependence of generation capability on ambient air temperature is a physical reality of both new and existing generators, and we find that it is appropriate that generators have the ability to bid the capacity that they believe can be available. We are not convinced that new generator design characteristics will eliminate capacity limitations due to ambient air temperatures, and we find that it is inappropriate to require generators to bid capacity that is not expected to be physically available into the Forward Capacity Auction.

D. Issues Relating to Demand Response

1. Treatment of seasonal resources and use of composite bids

144. Certain demand resources (seasonal resources) exhibit variability in the total amount of capacity they are able to supply, due to the seasonal nature of the resource. Because the Installed Capacity Requirement is an annual requirement seasonal resources are not eligible to supply the full amount of their capacity in the annual FCM auctions.[89]

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[89] Such resources could offer a fixed amount of capacity into the annual

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Composite offers allow seasonal resources to combine with resources that exhibit similar variability in a different season. For example an air conditioning reduction program (which has more MWs to offer in the summer than winter) could pair with a combined cycle unit (which has more MWs to offer in the winter than in summer), and the two would submit a composite offer. Nevertheless, ISO-NE notes that demand resource advocates have expressed concerns over the viability of the composite offer process and believe it may hinder the development of seasonal resources. ISO-NE asserts that it will closely monitor the effectiveness of the composite offer approach and, should their concerns materialize, and will work with demand response advocates to develop solutions without compromising the requirement that the Forward Capacity Auction procure an annual capacity product.

a. Protests

145. The DR Coalition, Conservation Services, EnerNOC, and NECPUC assert that the proposed rules do not provide appropriate treatment for resources that are only available to provide demand response during the summer. The DR Coalition and Conservation Services state that the proposed rules based on the annual capacity definition impede the ability of seasonal demand resources to participate in the FCM on equal terms with other resources. The DR Coalition has particular concerns about the use of "composite bids" in the proposed rules to address the treatment of seasonal resources. Composite bids provide the capability for a summer resource to partner with a resource providing capacity in the winter, and the two parties submit a joint bid. The DR Coalition argues, however, that the composite bid provision does not genuinely solve the problem faced by seasonal resources. It asserts that 1) the development of composite bids will impose such significant transaction costs on the parties that the composite bids will not be competitive with bids from other capacity resources and also because the composite bid process gives winter resources too much bargaining power vis-à-vis their summer partners, and 2) composite bids also raise anti-competitive concerns, because potential partners must share competitive information about bidding strategy, strike price and related issues in the process of preparing their bids. The DR Coalition requests that the Commission reject the requirement that seasonal resources provide capacity for a full 12 months, and propose that the mandate that seasonal resources must bid as composite bids be removed from the rules. In its place, the DR Coalition proposes changes to the rule that would allow the ISO to accept summer season demand resources up to a limit of 400 MW. In the alternative, the DR Coalition requests that the issues raised in its protest be set for

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FCM auction but it would have to be an amount it was capable of providing over 12 months. Additionally, seasonal resources may participate in seasonal or monthly reconfiguration auctions. The Commission notes that proposed rules addressing these auctions will be addressed in the subsequent Commission order in Docket No. ER07-547-000.

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expedited hearing so that these issues can be resolved promptly to not unduly delay the implementation of the first auction under the Forward Capacity Auction.

146. Conservation Services also argue that language in section 11.II.E.2.b of the Settlement Agreement 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" implies that the annual requirement did not apply to demand resources. Conservation Services, like the DR Coalition, requests the Commission to require ISO-NE to modify the market rules to allow up to 600 MWs of summer-only demand resources to qualify in the first three auctions.

147. NECPUC supports the Conservation Services protest and its suggestion to allow a reasonable amount of summer-only demand resources to participate immediately in the forward markets. If the Commission does not accept the Conservation Services proposal, NECPUC urges the Commission to require ISO-NE, through the stakeholder process, to develop a proposal that allows for summer-only bids to be entered into the Forward Capacity Auction without contracting for a composite bid. NECPUC requests that this proposal be developed and a filing be made with the Commission within six months of the Commission's decision on the instant ISO-NE filing.

b. <u>Answer</u>

148. ISO-NE states that FCM is an annual market requiring an annual product, and that it was so designed because it must meet an annual capacity requirement that requires the same amount of capacity to be available year-round. Further, ISO-NE states, if partial-year treatment were offered to seasonal demand resources, some gas-fired generators might also seek to be summer-only resources, because of fuel supply limitations during the winter. Therefore, ISO-NE asserts that allowing demand resources such summer-only treatment would set a precedent that might undermine the ability of FCM to meet the annual reliability criteria that it is designed to achieve. ISO-NE additionally states that, contrary to protesters' claims, composite bids will enable seasonal demand resources to participate in the Forward Capacity Market by presenting opportunities for both summer-only and winter-only resources to team up to earn capacity revenues that those resources would otherwise have to forego. ISO-NE also states that protesters are in error assuming that the partnering process will lead to anti-competitive behavior, noting that composite bids are no different from other types of joint endeavors that market participants who are otherwise competitors pursue, such as the joint development of generating plants. Finally, ISO-NE states that it recognizes that composite offers are a new concept, and that it will closely monitor that concept's effectiveness and be prepared to act as quickly as possible to resolve any problems that might arise.

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c. Commission Determination

149. The Commission considered the protests of the DR Coalition, Conservation Services and NECPUC, and their proposals to remove the 12-month eligibility requirement, and ISO-NE's answer to the protests. The proposed rules provide that, in order to participate in the FCM, a capacity resource must be available to provide capacity during all 12 months of the year. This annual commitment is provided for in the Settlement Agreement[90] and is part of ISO-NE's Installed Capacity Requirement determination.[91] The structure of the FCM, including the annual capacity auctions, is predicated on this annual commitment. The Commission approved this aspect of the Settlement Agreement in its FCM Order and FCM Rehearing Order. Moreover, a full year commitment period is consistent with the alternatives to ISO-NE's original capacity markets proposal that were offered by state agencies.[92]

150. Further, the Commission notes that the proposed rules accommodate participation by seasonal demand resources in reconfiguration auctions. Supplementing the Forward Capacity Auctions are reconfiguration auctions that provide a mechanism for ISO-NE, suppliers and traders to buy, sell, and exchange capacity obligations, and will maintain market liquidity. The FCM includes three types of reconfiguration auctions: annual auctions, monthly and seasonal auctions. Seasonal resources may participate in seasonal

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[90] *See* Filing Letter for Settlement Agreement at 22:

> The product is a megawatt of deliverable capacity with a future supply commitment in a Power year three years hence…. The duration of the supply commitment – the Commitment Period – coincides with the June to May Power Year and is one year for all existing capacity, but new capacity may choose a Commitment Period of up to five years.

[91] Section II.E.2.b of the 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 FCM. It further provides that such Qualified Capacity shall not be subject to the same availability penalties and/or poorly performing Resource treatment as other Resources, so the method shall also propose how to address poorly performing demand response and energy efficiency Resources. In addition, this section provides that the distinct method developed shall be appropriately considered in the ICR determination for the FCM.

[92] Both alternatives to ISO-NE's initial Locational Installed Capacity proposal presented by state parties at Oral Argument indicated that the commitment period of "no shorter than one year." See Four State Commissions' Proposed Alternative to LICAP and Statement in Support of the New England Resource Adequacy Market, filed September 13, 2005 in Docket No. ER03-563-030.

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or monthly reconfiguration auctions. However, unlike the annual forward capacity auction, we note that the reconfiguration auctions may not provide the same amount of lead time (three years) to develop a project that has cleared the auction. A related order that addresses the proposed rules on seasonal and monthly reconfiguration auctions, bilateral contracts and the remaining aspects of the FCM will be issued later.

151. Based on direction from the FCM settlement, ISO-NE has submitted a thorough and thoughtful approach for valuing demand resources (which include load curtailments, energy efficiency, and distributed generation) within the new forward capacity market in New England. By including five types of demand resources, ISO-NE has provided an opportunity for a wide variety of demand resources to bid into the auctions. Several of the positive features of the proposed inclusion of demand resources in the FCM include:

- Explicit incorporation of demand resources into the auctions. The FCM represents a market design that integrates demand resources directly into the auction, and not just as ICAP credits or special programs.

- Inclusion of additional demand resources broadens the type of reductions that could participate. The biggest beneficiaries of this inclusion are energy efficiency resources, but other forms of demand response that are not dispatchable or able to respond to directions to curtail will benefit from this change. The inclusion of energy efficiency in capacity markets is brand-new in the U.S., and ISO-NE is currently the only ISO/RTO that has broadened capacity markets to include energy efficiency.

- The ability to receive capacity payments if their bids are successful in the auction should provide a strong incentive for greater investments in demand responsiveness in the region. If successful, a new demand response resource will have a contract for up to 5 years that it must deliver 3 years hence. This multi-year payment stream will help developers finance their investments or companies obtain approval for upgrades or changes to their processes and facilities.

152. While the Commission will accept ISO-NE's use of composite bids, the Commission is nevertheless concerned about the potential loss of summer-only seasonal demand resources if the composite bid process does not work as envisioned by ISO-NE. With regard to seasonal measures, the proposed rules may not, in practice, take advantage of all of the benefits that energy efficiency and demand response resources can provide. We view this issue as a high priority, and ISO-NE appears to share this view. Accordingly, we direct ISO-NE to file a report by July 15, 2007 on the status of the composite bid process in light of the June 15 deadline for submitting composite bids. Further, we direct ISO-NE to adopt NECPUC's recommendation for a stakeholder process. This stakeholder process should consider any option that better optimizes

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seasonal bids (particularly summer only) in the FCM.[93] We also direct ISO-NE, by February 29, 2008, to submit a compliance filing that reports both on the composite bid process and on the status of this stakeholder process, including, if appropriate, a schedule for implementing options that better optimize seasonal bids for the second auction scheduled for December 2008.

2. Use of Pumped Storage as a Demand Resource

a. Protests

153. FirstLight asserts that ISO-NE's eligibility criteria for demand resource in the proposed rules are unnecessarily and inappropriately restrictive. According to First Light, the proposed rules unduly prejudice and disadvantage large-scale load management projects – such as pumped storage hydroelectric facilities – that are not located behind the end-user's meter. FirstLight states that pumped storage offers the same peak load reduction value effect for resource adequacy purposes as that offered by behind-the-customer-meter energy storage devices, and thus there is no rationale for distinguishing between such resources for purposes of demand resource eligibility in the FCM. FirstLight argues that restricting demand resources eligibility to behind-the-meter generation is not required by the terms of the Settlement Agreement. FirstLight also asserts that the proposed rules would be considered as undue discrimination against large-scale load management projects, and are therefore unlawful under section 205(a) and (b) of the FPA.

b. Answers

154. ISO-NE states that the Settlement Agreement does not require it to treat pumped storage as a demand resource. According to ISO-NE, 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. Thus, according to ISO-NE, treating pumped storage as a demand response would double count its value. Moreover, ISO-NE asserts that pumped storage provides no demand reduction value because a pumped storage plant is unlikely to be using costly on-peak electricity in the first place. Finally, ISO-NE states that pumped storage does not fit within the description of demand resources contained in the proposed market rule,[94]

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[93] The stakeholder process may also consider supply resources which are seasonal in nature, and not otherwise provided for in the Settlement.

[94] ISO-NE states that proposed market Rule 1, section III.3 (Definitions) defines demand resources as

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because under this definition, the value of a pumped storage project comes from its ability to produce on-peak generation and reserves, but it does so by increasing load during off-peak hours, not by reducing load during the relevant performance hours.

155. In its answer to ISO-NE's answer, First Light responds to ISO-NE's argument that a pumped storage unit is not a demand resource because it uses off-peak electricity as fuel, and is therefore an on-peak generating resource. FirstLight asserts that, similarly to pumped storage resources, behind-the-meter batteries also require a charge in off-peak hours and use off-peak electricity as fuel for storage to permit later displacement of on-peak loads. According to FirstLight, all load management devices that consume electric energy in charging a battery (whether in front of or behind the end-use meter) for later use in meeting peak demand result in an increase in overall load on the system as well as load in off-peak hours. Thus, FirstLight argues, the discharge of a battery in peak hours, and the use of pumped storage to generate electricity in peak hours, are both examples of supplying electric energy to a load for purposes of displacing demand in peak periods. FirstLight further asserts that ISO-NE does not dispute that increasing off-peak loads for the purpose of storing energy in a behind-the-meter battery to support later on-peak demand does provide demand reduction; thus, FirstLight states, the only question is whether the storage and discharge of a battery in front of a meter, such as a pumped storage facility, should be denied the same opportunity to participate in the FCM as the storage and discharge of a battery behind the meter. With regard to ISO-NE's "double counting" argument, FirstLight responds that it is seeking classification of pumped storage as a demand resource rather than as a generator, and does not ask that a pumped storage facility should be credited as both a demand resource and a generator for the same megawatts in the same commitment period. Finally, FirstLight claims that the Settlement Agreement does not exclude existing pumped storage from eligibility to serve as a demand resource, because section VIII.J.2 of the Settlement Agreement ignores the provision that "the role of demand response resources in the market will continue to evolve as Market Rule 1 Appendix and the Load Response Manual are revised," and "details concerning how [new demand resources] qualify as capacity Resources will be reflected in the Market Rules."[95]

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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.

[95] Settlement Agreement at VIII.J.2.a and VIII.J.2.b.

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c. Commission Determination

156. The Commission rejects FirstLight's protest. The proposed rules are not in conflict with the Settlement Agreement. A clear reading of the Settlement Agreement indicates that section 11.II.E.2 focused on the participation of demand resources and energy efficiency in capacity markets. Market Rule 1 currently defines demand resources to "mean any resource associated with the Load Response Program as defined in Appendix E to this Market Rule," and Appendix E states that "generating resources that are already qualified as generating assets are not eligible to participate in the Load Response Program."[96] The proposed changes to the definition of demand resources in Market Rule 1[97] are consistent with existing definitions. Since FirstLight's pumped storage facility has already qualified and operated as a generating asset, it does not meet the existing nor modified definition of a demand resource and cannot participate in the FCM as a demand resource. The Commission also agrees with ISO-NE that since pumped storage generates electricity during on-peak hours, it does not reduce end-use demand on the electricity network. Other load shifting technologies that are behind-the-meter and use off-peak electricity, such as battery storage and thermal storage, have the affect of reducing end-use, on-peak demand on ISO-NE system, which is consistent with the modified definition of demand resources. FirstLight is not proposing to change the ISO-NE tariff to allow generation resources to participate in the Load Response Program, it is only requesting that it be considered as a demand resource in the proposed FCM rules. Allowing FirstLight to continue to operate as a generation asset in energy and ancillary services markets, but at the same time receive demand resource capacity payments, would both violate the ISO-NE tariff and be discriminatory towards other generation assets.

3. Elimination of demand response customers from Real Time Demand Response program

a. Protests

157. EnerNOC raises concerns that, under the proposed FCM rules, demand resources will no longer be able to participate in the energy markets and the energy payments that are currently part of ISO-NE's 30-minute Real-Time Demand Response program will be eliminated. EnerNOC states that the proposed FCM rules will reduce customer benefits of demand response opportunities and undermine efforts to expand demand resource participation in New England.

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[96] III.E.1.2 of Appendix E of Market Rule 1.

[97] According to language proposed in the instant filing, the definition of demand resources "are installed measures (i.e., products, equipment, systems, services, practices and/or strategies) that result in additional and verifiable reductions in end-use demand." Transmittal, February 15 filing at 46.

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b. Commission determination

158. The Commission finds that EnerNOC's concerns are misplaced and premature. The FCM filing addresses the design and implementation of a forward capacity market and does not affect the rules regarding participation in ISO-NE's energy markets. In addition, the proposed extension and then elimination of the current Real Time Demand Response program are not addressed in this order. The merits of the extension of the Load Response Program will be addressed in a subsequent order.

E. Issues Relating to Hydro Quebec Capacity

a. Proposed Rules

159. The proposed market rules include provisions addressing import capacity resources that rely on the Phase I/II HVDC-TF interconnection with Hydro-Quebec (i.e., the HQ Interconnection). ISO-NE states that the Commission has found that the HQ Interconnection provided significant reliability benefits to the New England Control Area, and the Commission ordered that the entities that support the HQ Interconnection (i.e., the Interconnection Rights Holders, or IRHs) be given installed capacity credits (i.e., credits against the capacity obligations of the IRHs) in the form of Hydro Quebec Interconnection Capability Credits (or HQICCs). The Settlement Agreement provides that the IRHs will realize this reliability benefit through reductions in their capacity requirements.[98]

160. While the HQ Interconnection is rated at approximately 2000 MW, ISO-NE states that for reliability reasons, flows over the facility are generally limited to a smaller level – between 1200-1600 MW – because an outage over this facility could cause the single largest reliability problem in the combined New York, New England, and PJM systems. ISO-NE states that historically, it has limited capacity contracts on the facility to no more than 1800 MW, and that it is likely that this number will be reduced. ISO-NE states that it has assumed for purposes of the discussion of its proposed market rules that HQICCs will be set at 1200 MW and that the sum of HQICCs and capacity contracts will not exceed 1400 MW. To the extent that more than 200 MW of capacity contracts clear in the auction, HQICCs will be reduced ("netted") on a MW-for-MW basis, so that the combination of HQICCs and capacity contracts do not exceed 1400 MW. ISO-NE states that to ensure that the combination of HQICCs and capacity contracts do not exceed 1400 MW and to prevent double counting of capacity, it is proposing a market rule to require that capacity contracts[99] over the HQ Interconnection that will displace HQICCs must

[98] *See* Transmittal, February 15 filing at 54.

[99] Under proposed section III.13.1.3.5.1.1 of the tariff, there are two categories of import offers: "HQI Capacity" and "HQI Excess Capacity." The round-the-clock transmission reservation requirement applies only to HQI Capacity. The maximum MW amount of HQI Capacity Contracts shall be the

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have transmission reservations over the HQ Interconnection for the entirety of each month for which they have a capacity commitment.

b. Protests

161. National Grid provides comments to inform the Commission about the effect of ISO-NE's proposal on IRHs and to announce that a subset of IRHs are developing a filing with the Commission to address this detrimental effect. National Grid states that IRHs have an irrevocable obligation to pay all of the support costs of the HQ Interconnection, and in exchange, were granted exclusive physical rights to the transmission capacity of the HQ Interconnection. National Grid states further that previous Commission orders have made clear that IRHs have a right to the HQICCs, that the existence of the reliability benefit underlying the HQICCs is not dependent on transactions over the interconnection, but rather on the ability to access capacity in Canada, and that the value of the HQICCs cannot be taken from the IRHs and socialized among market participants that do not pay for the HQ Interconnection. National Grid argues that the current ISO-NE tariff contains a netting provision whereby the HQICCs received by the IRHs are reduced by the amount that capacity imports of ICAP exceed 600 MW over the HQ Interconnection on a MW-by-MW basis. National Grid states that such a reduction in HQICCs has happened only once to date, during July 2006, but that such reductions are more likely in the future as a result of the new Forward Capacity Market Rules. National Grid states that there is no need for the Commission to defer its evaluation of this portion of the ISO-NE filing, but that the Commission should provide that any action on the ISO-NE filing will not prejudice any future filings addressing the impacts of the Forward Capacity Market on HQICCs.

162. NSTAR complains that the netting methodology proposed for the HQ Interconnection is contrary to past Commission decisions on that line, as well as to the Installed Capacity Requirement Order which addressed the interrelationship of generic tie benefits and the Forward Capacity Auction. NSTAR states that as a general proposition, the amount of tie capacity available for capacity import contracts is the difference between the total capacity and the amount of capacity credits accorded to the entities that financed the interconnection. NSTAR states that in the Installed Capacity Requirement Order, the Commission held that where New England loads jointly share the costs of transfer capability, loads should jointly share the benefits of the tie benefits and the associated reduction in Installed Capacity Requirements; on that basis, the Commission accepted ISO-NE's proposal not to allow capacity imports that would reduce the tie benefits over transmission capacity jointly financed by New England loads. However, NSTAR argues, ISO-NE's Forward Capacity Market filing fails to allocate the full tie

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maximum monthly approved MW amount of HQICCs for the commitment period. When HQICCs are less than their maximum value, all or a portion of the HQI Capacity Contracts shall be reclassified as HQI Excess Capacity Contracts.

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benefit of the HQ Interconnection to the entities – the IRHs – who have borne its costs. That is because, according to NSTAR, under ISO-NE's netting provision, ISO-NE would accept capacity import contracts up to the total capacity of the HQ Interconnection and would then reduce HQICCs on a MW-for-MW basis to the extent that capacity import contracts exceed the difference between the HQ Interconnection's normally available capacity and HQICCs. Thus, NSTAR concludes, rather than import capacity contracts being the residual after HQICCs have been honored, HQICCs would be the residual. PPL also argues that this portion of the ISO-NE filing is inconsistent with the Installed Capacity Requirement Order. NSTAR acknowledges that a netting provision is currently in place in Market Rule 1,[100] but it argues that this provision is inconsistent with Commission precedent and wrong as a policy matter, and asks the Commission to eliminate this provision. In the instant docket, NSTAR recommends that the filing be modified so that the maximum amount of import capacity offered over the HQ Interconnection is limited to the total available capacity of the line, minus the value of extant HQICCs. Because firm capacity imports over the HQ Interconnection in excess of the difference between the maximum permissible capacity contracts and the maximum HQICCs would reduce the amount of HQICCs available for IRHs, PPL argues that no IRH should be obligated to provide firm transmission service over the HQ Interconnection in excess of this difference.

163. ISO-NE's answer replies to NSTAR and PPL. ISO-NE states that it did not propose to treat the HQ Interconnection facilities as a tie benefit identical to the tie benefits from New York and New Brunswick because the former facilities are not paid for by all customers as part of the Regional Tariff, but are owned by a separate set of owners. In its answer, HQUS argues that the real concern of NSTAR and National Grid is that their transmission rates for service on the HQ Interconnection may be too low, either now or in a few years when capacity has more value. HQUS states that such rate issues are irrelevant in the instant docket, and should instead be decided in a rate case. HQUS responds to PPL's comments by stating that while PPL concludes that IRHs should not be obligated to provide firm service in excess of 600 MWs, changing the

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[100] The netting provision states:

> **HQ Net Interconnection Capability Credit:** Of an IRH for a given month is its HQICC for that month, in Kilowatts, minus a number of Kilowatts equal to (1) the percent of its share of the Phase I/II HVDC-TF Transfer Capability committed or used by it for a UCAP Transaction for that month (*plus* any use during the same time period by an entity that obtained an OASIS transmission reservation from that IRH for service on the Phase I/II HVDC-TF for that same time period which was used to support a UCAP transaction), times (2) its HQICC for that month.

Section I.2.2(1) of the ISO-NE Tariff,.

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IRH's obligations would require amendments to existing market rules that are not at issue in this proceeding.

164. HQUS, in its initial comments, protests the proposed requirement for month-ahead around-the-clock transmission reservations to import one particular capacity product, HQI Capacity, over the HQ Interconnection. HQUS argues that this requirement violates section 11, Part VI of the Settlement Agreement, which provides that "market rules … shall be changed to allow External Resources to participate in the Forward Capacity Market … on a basis comparable to internal generation Resources." HQUS argues that no other resource must reserve transmission to sell capacity, and thus, that the requirement discriminates against imports over the HQ Interconnection. HQUS also disputes the ISO-NE's claim that the requirement is necessary to prevent double-counting, for the following reasons. First, the forward and reconfiguration auctions themselves prevent double-counting. Second, the requirement applies only to some of the capacity – HQI Capacity – imported over the HQ Interconnection. Third, there is no current around-the-clock transmission requirement for capacity imports, yet ISO-NE has not experienced double-counting. Fourth, ISO-NE has stated that it could accept HQUS's proposal regarding reservation requirements. HQUS proposes to replace ISO-NE's requirement with a rule that would limit transmission capacity reservation requirements to the MW amounts needed for the delivery of energy (which is the current requirement), and that meet all other offering and performance obligations.

165. In its answer, IRH Management Committee responds to the HQUS protest that the round-the-clock reservation requirement fails to allow HQI Capacity Contracts to participate in the FCM on a basis comparable to internal generation resources. IRH Management Committee responds that the HQUS protest ignores the differences between internal generation resources and resources delivered over the HQ Interconnection. IRH Management Committee states that internal generation that is a network resource receives, in effect, round-the-clock service over the Pool Transmission Facilities (PTF), but an internal generation resource may be required to enter into an interconnection agreement to pay for the interconnection facilities needed to get to the PTF.

166. In its answer, ISO-NE responds to HQUS by saying that the round-the-clock reservation requirement arises from the provisions of Schedule 20A of the ISO-NE Tariff. According to ISO-NE, if the round-the-clock reservation requirement is not in place, then Schedule 20A provides that 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. As a result, ISO-NE concludes, the reliability benefits could be double counted as capacity contracts and HQICCs.

c. <u>Commission determination</u>

167. In response to the comments of NSTAR and PPL, we conclude that ISO-NE's filing should be modified so that the maximum amount of import capacity contracts

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accepted in the auction over the HQ Interconnection should be limited to the total available capacity of the line minus the value of extant HQICCs, and we direct ISO-NE to file the modification in a compliance filing in the September 1, 2007 filing discussed above.

168. We agree with NSTAR that the issue presented here is the same as that presented in our Installed Capacity Requirement Order, and thus, a comparable policy should apply. In that order, we accepted ISO-NE's proposal to set aside interface transfer capability for tie benefits. Under ISO-NE's market rules, tie benefits reduce the Installed Capacity Requirement within New England by the amount of the tie benefits.[101] We concluded that loads that jointly share the costs of the transfer capability should jointly share the benefits of the transfer capability, including the tie benefits and the associated reduction in the Installed Capacity Requirement. We noted that capacity imports that reduce the tie benefit would increase the Installed Capacity Requirement by the amount of the lost tie benefit. As a result, purchasing imported capacity that reduces the tie benefit would unnecessarily increase the amount of capacity that must be purchased by customers in New England. The same principles apply in the instant docket with respect to capacity imports over the HQ Interconnection. Capacity imports in excess of the tie benefit associated with the HQ Interconnection (i.e., in excess of HQICCs) would unnecessarily increase the amount of capacity that must be purchased. As ISO-NE acknowledges in the instant docket, the costs of the HQ Interconnection are not shared by all New England loads, but rather only by the IRHs. Therefore, the tie benefits associated with the HQ Interconnection (i.e., HQICCs) should be shared by the IRHs but should not be extended to others that do not share in the HQ Interconnection's costs. Thus, we direct ISO-NE to amend the rules so that the Forward Capacity Auction will not accept more capacity contracts than can be accommodated by the transfer capability of the HQ Interconnection without reducing HQICCs.

169. In light of our ruling that the maximum amount of import capacity offered over the HQ Interconnection should be limited to the total available capacity of the line minus the value of extant HQICCs, ISO-NE's need for round-the-clock transmission reservations for HQI capacity contracts is rendered moot. ISO-NE states that the reservation requirement is needed so that it will be able to calculate correctly the amount by which HQICCs will be reduced by capacity contracts cleared in the auction. However, as we determined in the previous paragraph, we have concluded that capacity contracts should not be permitted to reduce HQICCs. Because the reservation requirement is not necessary, we direct ISO-NE to delete it in its September 1 compliance filing.

[101] Installed Capacity Requirement Order at P 30-31.

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F. Miscellaneous Technical Issues

1. Qualification process for new resources

a. Protests

170. Under the proposed market rules, new capacity resources wishing to participate in the Forward Capacity Auction must submit a Show of Interest Form within the submission window for Shows of Interest (section III. 13.1.1.2) and then must later submit a New Capacity Qualification Package by the New Capacity Qualification Deadline, roughly five and a half months after the Show of Interest window closes.[102] Absent timely submission of a Show of Interest Form, a resource may not receive capacity payments during the first commitment period for capacity, and after submission of that form, "material changes . . . may not be made to the information contained therein" (section III. 13.1.1.2.1).

171. International Power, Public Systems and Dominion raise issues with regard to the qualification process. International Power states that the Settlement Agreement provides that:

> [e]ach potential capacity Resource (Existing, New, or Imports) must submit qualification information to the ISO no later than the relevant bid qualification deadline, which shall be determined during the development of Market Rules. 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.[103]

172. International Power claims that this language demonstrates that parties contemplated that there would only be one bid qualification deadline for new capacity resources, approximately six weeks after the ISO's posting of de-list bids and exports – i.e., information showing the unavailability of capacity from existing resources. International Paper further states that the Settlement Agreement shows that the qualification deadline for New Resources must come *after* the qualification deadline for existing capacity, because the Settlement Agreement provides that de-list bids and export bids may submitted to the ISO up until the qualification deadline for existing capacity.[104] According to International Paper, these two sections, when read together, show that (i) the qualification deadline for existing capacity would precede the qualification deadline for new capacity resources by approximately six weeks; and (ii) there would be a single

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[102] For the first auction, the Show of Interest Form should have been submitted by January 2, 2007.

[103] Settlement Agreement, section 11.II.A.

[104] Settlement Agreement at 11.III. D.2.

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qualification deadline for new capacity resources. It states that ISO-NE's proposal violates this understanding, because it provides two qualification deadlines for new capacity resources, the first of which – the Show of Interest Form – precedes the qualification deadline that is mandated by the Settlement Agreement by five-and-a-half months. International Power further states that ISO-NE has not met its burden of showing that this violation of the Settlement Agreement is necessary. International Power claims that the parties provided, in the Settlement Agreement, that the single qualification deadline for new capacity would be six weeks following the qualification deadline for existing capacity, so that developers of new capacity could obtain information as to how much existing capacity would de-list, before deciding whether to enter an auction. According to International Power, ISO-NE's Show of Interest requirement would deprive developers of the opportunity to act upon accurate information about existing capacity levels and, instead would force them to make final decisions without information about the level of de-lists by existing capacity.

173. In its answer, ISO-NE states that the fact that it had already received 200 Show of Interest Forms by January 2, 2007 demonstrates that there is significant interest in serving as a capacity resource, and also makes clear that ISO-NE would need significant time to evaluate all of those applications, It further notes that, although the deadline to submit Show of Interest Forms for the first Forward Capacity Auction was January 2, 2007, in fact ISO-NE has received and accepted Show of Interest Forms filed after that date, and intends to review all Show of Interest Forms submitted by new entrants prior to February 20, 2007.

174. International Power additionally objects to ISO-NE's proposal to require each new capacity resource greater than 20 MW to submit a deposit of $25,000 by February 20, 2007, on the basis that this requirement was not provided in the Settlement Agreement, and ISO-NE has not explained why it is necessary. In its answer, ISO-NE states that requiring a deposit is the kind of reasonable, non-burdensome implementation mechanism that the Settlement Agreement contemplated that ISO-NE could undertake.

b. <u>Commission determination</u>

175. With regard to the issues raised by International Power, the Commission finds that ISO-NE's action does not violate the terms of the Settlement Agreement. According to the information provided by International Power, ISO-NE's proposed market rules provide for two different submissions by capacity resources:

> For a resource to qualify as a New Capacity Resource, the resource's Project Sponsor must make two separate submissions to the ISO: First, the Project Sponsor must submit a New Capacity Show of Interest Form during the New Capacity Show of Interest Submission Window. Second, the Project Sponsor must submit a New Capacity Qualification Package no

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later than the New Qualification Deadline.[105]

176. International Power views the Show of Interest Form and the new capacity Qualification Package as being two different forms of qualification application. But ISO-NE appears to anticipate using – and needing – the information provided by the two documents in different ways. The Show of Interest Form will provide ISO-NE with the information necessary to begin the transmission planning process to determine whether the new capacity resource can provide incremental capacity to the system.[106] The new capacity Qualification Package, on the other hand, will provide significantly more information to enable the ISO to evaluate the overall feasibility of the project.[107] We find

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[105] Proposed Tariff Section III. 13.1.1.2

[106] ISO-NE states:

> The Show of Interest Form is a short application that requests the minimum amount of information (e.g. interconnection point, equipment configuration, MW capacity, etc.) required by the ISO to undertake the needed transmission planning studies that determine whether . . . the proposed new resource can interconnect to the system without causing violations of system reliability or safety standards and whether the new resource, if interconnected, would cause overlapping impacts with other new or existing resources and therefore not provide incremental capacity to the New England electricity system.

Transmittal, February 15 filing, at 10

[107] ISO-NE states:

> The New Capacity Qualification Package includes a demonstration of site control (for the first Forward Capacity Auction) and a critical path schedule containing information sufficient for the ISO to evaluate the feasibility of the project to be constructed as well as to achieve Commercial Operation. If a Project Sponsor intends to submit offers in the Forward Capacity Auction at prices below 0.75 times Cost of New Entry, the qualification package must contain supporting information. . . . .
>
> There are additional requirements to be included in the qualification package for resources that were previously listed as capacity and are seeking treatment as new capacity resources. Such requirements include information about costs associated with repowering, adding incremental capacity, restoring de-rated capacity, or compliance with environmental regulations. [In some cases, Intermittent Resources must include] resource and site-specific data that will permit the determination of the Qualified Capacity of the resource, e.g., historical wind or solar data.

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these submissions necessary for ISO-NE to determine if a new resource qualifies to supply capacity in the FCM. We therefore disagree with International Power's view that ISO-NE has proposed two separate forms of qualification application.

177. Similarly, contrary to International Power's protest, we find that ISO-NE has provided a sufficient explanation as to why it will require certain resources above 20 MW to provide a $25,000 deposit:

> Submission of such a deposit is a strong indication that the Project Sponsor intends to proceed with development of a specific project and assists the ISO in focusing on only those projects where the sponsor is committed to going forward. Because conducting interconnection studies is time- and resource-consuming, as noted above, the ISO wishes to avoid spending scarce human and financial resources in reviewing frivolous applications.[108]

178. Because ISO-NE has provided a reasonable justification for requiring a deposit, the Commission will not require the elimination of this requirement.

2. Qualification Requirements for New Resources

a. Protests

179. Public Systems state that the proposed capacity qualification process is not consistent with the Settlement Agreement and therefore must be modified. Public Systems note that section II.B.3 of the Settlement Agreement states that any resource seeking to qualify for participation in the Forward Capacity Auction must meet various qualification requirements. Public Systems further note that that same provision of the Settlement Agreement states that qualification criteria "may vary based on the size,

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As part of the qualification process, New Import Capacity Resources are also required, no later than the New Capacity Qualification Deadline, to submit documentation of a contract to provide capacity in the New England Control Area from outside of the New England Control Area for the entire Capacity Commitment Period, proof of direct control or ownership over one or more External Resources to be utilized to back the New Import Capacity Resource during the Capacity Commitment Period, or documentation demonstrating that the import capacity will be backed by the external Control Area during the Capacity Commitment Period, as well as information to establish the summer and winter ratings of the resource(s) backing the import. Also, the Market Participant must specify the interface over which the New Import Capacity Resources will be imported.Transmittal, February 15 filing at 25-26.

[108]Filing letter at 14.

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technology, complexity, et cetera of the resource."[109] However, Public Systems contend that qualification criteria as set forth in the proposed rules do not vary based on the proposed resource's "size, technology, complexity, et cetera." Rather, Public Systems argue that the proposed FCM rules 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 an identical time schedule. Thus, Public Systems argue, the qualification process is neither consistent with nor in furtherance of the Settlement Agreement.

180. Public Systems assert 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 does not minimize barriers to entry. For example, Public Systems argue that requiring peaking facilities to demonstrate site control at the Show of Interest Form stage is not consistent with the Settlement Agreement. Public Systems argue that the need for and likelihood of being able to meet the proposed deadlines and information requirements will vary as a function of the type of capacity addition under consideration. For example, Public Systems states that, while a baseload nuclear plant 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. Public Systems asserts that treating all resources based on a single set of criteria and a single set of submission deadlines may create barriers to entry, limits the number of resources participating, and increases the likelihood of failed auctions and higher capacity market prices.[110]

181. However, Public Systems, mindful that the process for the first Forward Capacity Auction is currently underway, request that the Commission direct ISO-NE to develop a limited set of revised qualification requirements that reflect the flexibility for the June 2011 commitment period and for all periods thereafter. ISO-NE, in its answer, first notes that the provision of the Settlement Agreement that Public Systems quotes, section III.B.3, states that qualification criteria *may* vary based on factors such as size and technology, not that qualification criteria *must* vary based on those factors. It then states that it is willing to review this issue in the future and revisit the market rules, if necessary.

b. <u>Commission Determination</u>

182. The Commission finds that the provisions on the qualification of new capacity resources in the proposed rules on FCM meet the requirements articulated in section 11.II.B.3 of the Settlement Agreement. The Commission will not direct ISO-NE to develop a limited set of revised qualification requirements for the second Forward Capacity Auction. All of the four requirements listed in section 11.II.B.3 are required as

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[109] Settlement Agreement at 11.II.B.3.

[110] In its answer, the CT DPUC endorses Public Systems' position here.

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part of the qualification process in the proposed rules. Further, the Settlement Agreement states that qualification criteria may vary based on certain factors and that those requirements would be detailed during the development of market rules. The Commission finds that the proposed rules provide appropriate variability with regard to type of resource. Demand resources must provide information that is pertinent to their specific characteristics, though this may be different from that provided by generating resources. Intermittent resources are required to provide additional information with regard to wind speed or water-flow data. Moreover, the Commission finds that there is nothing in the Settlement Agreement that requires that peaking generation fulfill less stringent criteria than larger baseload generation.

183. In addition to the referenced statement regarding the possibility that qualification criteria may vary, based on size, technology, complexity, and other factors, the Settlement Agreement states that "such qualification requirements shall be further detailed as part of the development of Market Rules."[111] With regard to new capacity the Settlement Agreement expressly states that new capacity must fulfill certain qualification requirements: site control, critical path schedule, interconnection study, and financial assurance. In particular, Public Systems raises the issue of site control. The provision addressing site control provides that this requirement may be met one of four ways: ownership, leasehold interest, written option to purchase or lease the property, or executed, written contract to purchase or lease the property. The Commission finds that this provision provides reasonable opportunity for new capacity resources to fulfill the requirements by selecting from a range of options.

184. Finally, the Commission finds that, given that the FCM is a forward market for physical resources, it is reasonable for ISO-NE to require that site control be demonstrated as part of the Show of Interest Form.[112] Moreover, the interconnection analysis, which is based on information presented with the Show of Interest Form, will study overlapping impacts of new capacity resources and may result in one resource having priority over another. As a basic matter, the Commission finds it unreasonable for a resource that has not demonstrated site control to be in a prioritization position higher than a resource that has made such a demonstration.

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[111] Settlement Agreement at 11.II.B.3.

[112] The proposed rules require that, for the first Forward Capacity Auction, site control be demonstrated as part of the Qualification Package. For subsequent Forward Capacity Auctions, site control must be demonstrated as part of the Show of Interest Form. Section III.13.1.1.2.2.1.

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3. Exports through an import-constrained zone

a. Protests

185. LIPA complains that the ISO-NE filing fails to implement section 11.III.A.8 of the Settlement Agreement, which requires that where zonal separation is determined to exist, the market rules must specify a process for an export of capacity both from or through an import-constrained zone over tie lines to external regions. LIPA previously raised this issue in Docket No. ER07-365-000. LIPA notes that the Commission's Installed Capacity Requirement Order concluded that ISO-NE's filing in that docket did not provide the required process, and directed ISO-NE to file to propose a process by August 27, 2007.

186. ISO-NE notes in the instant filing that LIPA has argued that the proposed rules do not provide for the ability to buy through congestion. ISO-NE disagrees with LIPA; in ISO-NE's view, the proposed design enables LIPA to achieve the intended result, even though the design does not explicitly include provisions for buying through congestion. That is because, according to ISO-NE, LIPA could sell its resource into the Forward Capacity Market and then enter into a bilateral arrangement with a unit in Connecticut that de-lists, thereby achieving the objective of buying through congestion and delivering a resource to Connecticut.

187. LIPA responds that the ISO-NE proposal fails to implement the Settlement Agreement. Under the ISO-NE proposal, LIPA states, it would be required to bid its Bear Swamp contracted capacity (which is located in the interior of New England) into the auction, assume the risk of being chosen, and then re-purchase from a de-listed unit in Connecticut to effectuate the export, and assume the risk of being curtailed. LIPA states that it is willing to pay the price differential across a congested capacity zone to export capacity to preserve the long-term firm capacity contract. In LIPA's view, ISO-NE has failed to explain why its proposed market rules abandon the approach of buying through congestion across a congested capacity zone, and instead require the negotiation of a wholly separate bilateral agreement outside of the Forward Capacity Market. LIPA further argues that ISO-NE's proposal is also inconsistent with the portion of the proposed market rules that address exports, for the following reason. To export capacity, a resource must qualify for an Administrative Export de-listing, the pre-requisite for which is a long-term firm contract between the resource owner and the purchaser outside the ISO-NE control area. Then the purchaser of the resource owner must disrupt the contract and bid the capacity into a New England constrained region rather than arranging for the through export transaction. Finally, LIPA argues that section III.13.1.3.5.3.1 of the proposed market rules requires that external intervening control areas treat exports as native load when it comes to curtailment, that ISO-NE should provide equivalent treatment for the curtailment of exports out of New England, but that such equivalent treatment may not occur if the New England market rules fail to allow

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entities to buy through congestion across a congested capacity zone in order to export capacity.

188. In its answer, ISO-NE argues that LIPA's protest should be rejected because the Commission has already addressed these arguments and set forth a process for addressing them in the Installed Capacity Requirement Order – where the Commission required ISO-NE to file to propose a process for such exports by August 27, 2007.

b. Commission Determination

189. We agree with LIPA that ISO-NE has not implemented section 11.III.A.8 of the Settlement Agreement. ISO-NE concedes that its proposal does not include explicit provisions for buying through congestion. We agree with ISO-NE that the Commission has already addressed these arguments and set forth a process for addressing them in the Installed Capacity Requirement Order. We therefore reiterate the requirement already imposed on ISO-NE in the Installed Capacity Requirement Order that ISO-NE must file to propose a process for an export of capacity both from or through an import-constrained zone over tie lines to external regions by August 27, 2007.

4. Prohibition on Intermittent Resources backing capacity exports to external control areas

190. Brookfield argues that the Settlement Agreement did not contemplate the proposal contained in the market rules that intermittent resources may not back capacity exports to external control areas. Specifically, Brookfield protests language contained in section 13.III.6.2.2.

191. The Commission, in this order, is addressing only sections III.13.1 and III.13.2 of the proposed rules on FCM. We will address Brookfield's protest in the order in Docket No. ER07-547-000.

5. Development of Capacity Transfer Rights

192. Public Systems seek clarification of section III.13.1.6.2, which states that Self-Supplied resources must be located in the same capacity zone as the associated load, unless the Self-Supplied resource is a pool-planned unit or other unit with a special allocation of Capacity Transfer Rights (CTRs). Public Systems state that ISO-NE should consider and address the interface between CTRs that are not allocated based on pool-planned unit entitlement ownership or through other "special" allocation arrangements and self-supplied resources.

193. In its answer, ISO-NE states that resources located within an import-constrained zone as well as pool planned units with a special allocation of CTRs may be used toward satisfying a load serving entity's Local Sourcing Requirement. ISO-NE asserts that any

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additional CTRs allocated to a load-serving entity are based on its obligation and cannot be used to meet a local sourcing requirement.

194. The Commission denies Public Systems' request. The Settlement Agreement requires that for Self-Supplied resources to fulfill a Local Sourcing Requirement, they must be located within the same capacity zone and the load to which they are designated, unless the Self-Supplied resource is a pool-planned unit with a special allocation of CTRs.[113] Section III.13.1.6.2 of the proposed rules reiterates this standard, stating that, in order to fulfill a Local Sourcing Requirement applicable to a load in an import-constrained capacity zone, a Self- Supplied resource "must be located in the same Capacity Zone as the associated load, unless the Self-Supplied [Forward Capacity Auction] Resource is a pool-planned unit or other unit with a special allocation of Capacity Transfer Rights."[114] The Commission finds that section III.13.1.6.2 appropriately comports with the Settlement Agreement and, as such, requires no modification.

6. Extraordinary Fuel Expenses

195. NSTAR asks that the Commission clarify when pipeline imbalance charges are recoverable by a gas-fired generator as Extraordinary Fuel Expenses. NSTAR raises an issue in connection with section III.13.6.1.1.3 of the proposed rules on FCM.

196. The Commission, in this order, is addressing only sections III.13.1 and III.13.2 of the proposed rules on FCM. We will address NSTAR's protest in the order in Docket No. ER07-547-000.

7. External node issue

197. CT DPUC argues that in mapping external nodes through which imports may flow, ISO-NE identifies the Cross Sound Cable connecting Connecticut with Long Island but does not identify the 1385 Cable.[115] The CT DPUC asserts that ISO-NE offers no explanation for its omission of the 1385 Cable from the list of external nodes, and the CT DPUC requests that the Commission require clarification from ISO-NE on this point.

198. In its answer, ISO-NE states that it is working to allow the use of the 1385 line as a separate scheduling node in the energy market, but that rules governing the use of the 1385 Cable do not permit that line to be used for capacity contracts. According to ISO-NE, flows on this line are subject to frequent interruption based on operating conditions

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[113] Settlement Agreement at 11.II.F.

[114] Section III.13.1.6.2.

[115] The 1385 Cable connects southwest Connecticut and Northport, Long Island.

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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.

199. The Commission is satisfied with ISO-NE's clarification that the 1385 Cable cannot be relied upon to provide capacity as a separate path. We add that it is our understanding that the 1385 Cable is one of the transmission facilities associated with the NY-NE external node.[116]

G. Legal Issues

1. Standard of review

a. Protests

200. During a "waiver period,"[117] ISO-NE may use its authority under section 205 to file modifications of the Market Rules that address the terms of the Settlement Agreement, but ISO-NE may only exercise that authority if it demonstrates 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.

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[116] *See* ISO New England, ATC Methodology, Appendix C: Detailed Interfaces, available at http://www.iso-ne.com/trans/ops/limits/iso_ne_ttc_atc_method.doc (2005), and Coordination Agreement between ISO New England Inc. and New York Independent System Operator, Schedule A: Description of Interconnection Facilities, FERC Docket ER06-421 (2005).

[117] *See Devon Power*, 115 FERC ¶ 61,340 at P 35 (2006):

> Settling Parties waive their rights under section 206 of the FPA to seek a change in the Settlement Agreement or the market rules implementing the agreement for the period beginning March 6, 2006 through the earlier of September 5, 2008 or the date on which the prices from the second [Forward Capacity Auction] become final . . .. During this period, ISO-NE will retain its authority under section 205 of the FPA . . . to file modifications of the market rules that address the terms of the Settlement Agreement. ISO-NE may exercise that authority only where it can demonstrate that failure to implement the proposed change would have a negative effect on 1) system reliability or security, or 2) the competitiveness or efficiency of the forward capacity or forward reserve markets. Were ISO-NE to make such a filing, Settling Parties will retain all of their rights to challenge the proposed modifications before the Commission.

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201. As discussed above, in section III.13.2.5.2.5(f), ISO-NE proposed to "evaluate . . . whether to modify the treatment of de-list bids rejected for reliability reasons pursuant to this section, including but not limited to an evaluation of the applications of the Alternative Capacity Price Rule . . . to [Forward Capacity Auctions] affected by de-list bids rejected for reliability reasons."[118] Mass DTE claims that ISO-NE's proposal does not meet the above requirements of the Settlement, since ISO-NE has not demonstrated that such a rule change is necessary at this time.

202. International Power makes a similar argument with respect to imposition of the Show of Interest requirement, stating that ISO-NE cannot satisfy this standard, because the Show of Interest procedures impose an unwarranted barrier to entry upon new capacity resources that will (i) lead to less reliability and security and (ii) result in a less competitive and efficient market.

b. <u>Commission Determination</u>

203. With regard to Mass DTE's argument regarding proposed changes to the Alternative Price Rule, as noted above, ISO-NE's proposed change does not effectuate a change to the applications of the Alternative Price Rule. Rather, ISO-NE proposes to evaluate whether such a change might be necessary – an action which, as we point out *supra*, it could take even absent section III.13.2.5.2.5. Thus, the problem of ISO-NE's authority to "make a modification of the market rules that address the terms of the Settlement Agreement" is not at issue: ISO-NE is not proposing to make a change in the market rules that would actually alter the terms of the Settlement Agreement, it is simply proposing to discuss them.

204. As to International Power's argument with regard to the Show of Interest procedures, we find that ISO-NE has shown that, absent the Show of Interest procedures, system reliability or security might be compromised. ISO-NE stated that the information that the Show of Interest Form provides is:

> required by the ISO to undertake the needed transmission planning studies that determine whether a new capacity resource can provide incremental capacity to the system. These studies determine whether the proposed new resource can interconnect to the system without causing violations of system reliability or safety standards.[119]

205. Thus, because ISO-NE has stated, without contradiction by International Power, that it requires the Show of Interest Form's information to determine whether that

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[118] Section III.13.2.5.2.5

[119] Filing Letter at 10, footnote omitted.

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resource can interconnect without violating reliability or safety standard, it has met the standard of review for such modifications.

2. Waiver of 60-day notice period

a. Protest

206. The Commission's regulations provide that:

> All rate schedules or any part thereof shall be tendered for filing with the Commission and posted not less than sixty days . . . prior to the date on which . . . the filing party proposes to make any change in electric service and/or rate, charge, classification, practice, rule, regulation, or contract effective as a change in rate schedule . . . unless a different period of time is permitted by the Commission.[120]

207. The Commission also provides for waivers to this 60-day notice requirement:

> Upon application and for good cause shown, the Commission may, by order, provide that a rate schedule, or part thereof, shall be effective as of a date prior to the date of filing or prior to the date the rate schedule would become effective in accordance with these rules. Application for waiver of the prior notice requirement shall show (a) how and the extent to which the filing public utility and purchaser(s) under such rate schedule, or part thereof, would be affected if the notice requirement is not waived, and (b) the effects of the waiver, if granted, upon purchasers under other rate schedules. The filing public utility requesting such waiver of notice shall serve copies of its request therefor upon all purchasers.[121]

208. ISO-NE made its filing containing these market rules on February 15, 2007. It asks for an effective date of February 16, 2007 for the rules. In its filing, ISO-NE asks for a waiver of the 60-day requirement for the tariff sheets related to the qualification rules. It states that it requires this waiver because:

> the qualification process . . . is a linchpin of the market design and

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[120] 18 C.F.R. § 35.3 (2006). Additionally, section 205(d) of the FPA provides that, as a general matter, tariff changes may not become effective "except after sixty days' notice to the Commission and to the public." However, that section also provides that "(t)he Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice."

[121] 18 C.F.R. § 35.11 (2006).

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> [is necessary] to properly receive and begin evaluating the impacts on the transmission system of the many thousand of megawatts of projects that have been proposed. These studies must be completed in a timely manner to enable the first [Forward Capacity Auction] to occur in February, 2008, as contemplated by the Settlement. The Show of Interest Forms for New Generating Capacity Resources solicit the data needed to conduct these studies, are an essential building block in the process leading up to the [Forward Capacity Auction], and are needed at the earliest possible time.[122]

Thus, ISO-NE claims that good cause exists to grant a waiver of the 60-day notice requirement.

209. International Power states that ISO-NE has not shown good cause to waive the 60-day notice requirement with regard to the Show of Interest procedures. It states that under *Central Hudson Gas & Electric Corporation* (*Central Hudson*),[123] the Commission set forth the standard for the granting of waiver,[124] and ISO-NE cannot meet that standard. According to International Power, the Show of Interest procedures are protested, are not provided by the Settlement Agreement, and have the potential to raise capacity prices by serving as a barrier to some resources from entering the Forward Capacity Auction. Finally, International Power states that ISO-NE has not demonstrated "extraordinary circumstances" requiring a waiver, since the commitment period for the first Forward Capacity Auction begins on June 1, 2010 -- approximately three and a half years from now.

210. ISO-NE, in its answer, responds that the February 15 Filing implementing the Settlement Agreement is not a rate increase, and therefore *Central Hudson* is distinguishable on its face. It further states that, if ISO-NE does not have adequate time to perform the transmission analyses of the project proposals outlined on the Show of

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[122] Filing letter at 12.

[123] 60 FERC ¶ 61,106 at 61,338 (1992), *reh'g denied*, 61 FERC ¶ 61,089 (1992).

[124] In *Central Hudson*, the Commission stated that waiver of the 60-day prior notice requirement generally only will be appropriate where: (i) the filing is uncontested and has no rate impact, (ii) the filing reduces rates and charges or (iii) a rate change and its effective date are prescribed by an agreement on file with the Commission or by a settlement agreement accepted by the Commission. *Id*. at 61,338. The Commission stated that in other circumstances, such as rate increases not provided for in a contract or settlement on file with the Commission, a strong showing of good cause would be required for waiver of the notice period, *id*. at 61,339. The Commission also stated that "absent extraordinary circumstances, [it] would not grant waiver of notice when an agreement for new service is filed on or after the day service has commenced." *Id*.

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Interest Forms, it may not be able to identify, prior to the Forward Capacity Auction, all of the projects that may not be able to be interconnected to the system, and 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. ISO-NE argues that even a few such incidents, and the resulting uncertainty, could 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.

211. ISO-NE further states that market participants had ample notice of the Show of Interest Procedures (including the necessity of making a $25,000 deposit), due to the many months of discussion among market participants prior to the February 15 filing; thus, according to ISO-NE, there was no element of the kind of surprise that the 60-day notice requirement is designed to prevent.

b. <u>Commission Determination</u>

212. The Commission grants the waiver requested by ISO-NE. We find that ISO-NE has presented good cause for a waiver, as discussed above.[125] At this critical time, when ISO-NE is preparing for the first Forward Capacity Auction, we will grant some leeway in terms of notice. Moreover, as ISO-NE noted, ISO-NE notified its market participants of the Show of Interest procedures as early as the September 22, 2006 Joint NEPOOL

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[125] ISO-NE has also stated that it required the information contained in the Show of Interest Forms at an early date, because

> the required interconnection studies were time consuming, [so that] early participation in the process by Market Participants was important to the success of the auction. . . . [T]he ISO estimated that if approximately twelve Show of Interest Forms were received that required initial interconnection analysis, then up to twelve weeks of effort would be required to perform initial interconnection analyses and, in addition, up to twelve weeks of effort would be required to evaluate possible overlapping impacts. 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. More applications results in more iterations.

Transmittal, February 15 filing at 13.

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Reliability Committee/Markets Committee Meeting, and posted the same information on its web site on October 19, 2006.[126] Thus, we find good cause to grant a waiver of the 60-day notice requirement, both for the February 16 effective date requested for the definitions and those tariff sheets related to the qualification process, and for the March 1 effective date requested for conforming, non-substantive changes to the market rules and definitions governing the Installed Capacity Requirement.

3. Request for suspension

213. The DR Coalition requests that the Commission impose a nominal suspension of one day on the relevant tariff provisions enumerated on Attachment A, allowing these provision to become effective as of February 17, 2007, subject to refund.

214. We believe that ISO-NE's market rules will benefit all of its market participants by enabling implementation of the FCM. Additionally, based on a review of the filing, the Commission finds that the proposed tariff changes have been shown to be just and reasonable. We therefore deny the DR Coalition's request for suspension.

4. Filing of bidder manuals and clarification of terminology

215. CT DPUC and NECPUC raise issues with regard to the filing of bidder manuals and clarification of terminology. They ask the Commission to require ISO-NE to clarify certain terminology and mechanics of the Forward Capacity Auction process,[127] and also ask the Commission to order ISO-NE to file the manual for bidders that ISO-NE is currently preparing with the Commission.

216. In its answer, ISO-NE agrees with the requests for clarification of terminology and Forward Capacity Auction mechanics that these parties request.[128] As to the bidders manuals, ISO-NE states that it will carefully review whether any of the provisions therein 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, ISO-

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[126] *Id*. at 12-13.

[127] The CT DPUC states that the proposed rules and ISO-NE's Cover Letter sometimes confuse "offers" and "bids," noting that only resources wishing to de-list or export submit bids, and all other resources make offers into the auction. Similarly, the CT DPUC states that parties may be confused as to the particulars of the supply curve for the auction.

[128] As requested by the CT DPUC and NECPUC, ISO-NE clarifies that a capacity resource participating in the Forward Capacity Auction must have included such offers in the form of a supply curve with multiple price-quantity pairs, but every offer during every round of the Forward Capacity Auction need not be in the form of a supply curve.

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NE states that, prior to the development and completion of the manuals, it would be premature to make a determination as to whether the manuals need to be filed.

217. The Commission grants the request of CT DPUC and NECPUC with request to terminology and Forward Capacity Auction mechanics. With regard to the bidders manual, we agree that it is premature to determine whether a manual needs to be filed with the Commission, before that manual is prepared.

5. Other Issues

218. In its September 1 compliance filing, we will require ISO-NE either to make the following tariff changes which appear to be simply corrections of typographical or similar administrative errors, or else to explain why those tariff provisions are, in fact, correct as they stand.

219. The proposed rules on FCM contain provisions that enable a resource that has previously been counted as a capacity resource (including one that had been deactivated or retired) to participate in a Forward Capacity Auction as a new generating capacity resource.[129] Such a resource must undertake certain, specified investments in order to do so. If one of the certain, specified conditions is met, such resources may participate in the Forward Capacity Auction, in its entirety, as new capacity. Similarly, the proposed rules on FCM provide that a resource that has previously listed capacity may select to have a portion of its capacity counted as new generating capacity, if specified investment requirements are met.[130] The Commission notes that the transmittal letter states that, in reference to section III.13.1.1.1.3 of the proposed rules on FCM, the owner "may make this election when investment in the Resource either (i) results in an increase in output greater than certain thresholds, or (ii) will be equal to or greater than $200 (as adjusted annually) per kilowatt of the amount of increase in summer Qualified Capacity resulting from the investment." However, section III.13.1.1.1.3 appears to require that the capacity resource meet both of the condition listed above. Specifically, the tariff employs "and" between conditions (a) and (b), requiring that both conditions be met, as opposed to "either," as stated in the transmittal letter.[131] Based on a similar provision in section III.13.1.1.1.2 as well as the transmittal letter, the Commission believes that "or" should be substituted for "and" at the end of section III.13.1.1.1.3(a).

220. With regard to another portion of the tariff, the Commission is concerned that certain proposed tariff sheets do not reflect the intent of the FCM design as described in ISO-NE's transmittal letter. Specifically, with regard to section III.13.2.3.2(c) of the proposed rules, ISO-NE refers to existing generating and existing demand resources to

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[129] Section III.13.1.1.1.2.

[130] Section III.13.1.1.1.3.

[131] *See* Section III.13.1.1.1.3(a) at Original Sheet No. 7308H.

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which this provision applies as "price takers."[132] It does not appear as though section III.13.2.3.2(c) contemplates any difference in the treatment of existing generating and existing demand resources. However, the Commission notes that section III.13.1.4.2.5.2 (Notification of Qualification for Existing Demand Resources) states that:

> if an Existing Demand Resource is not submitting a change in its Demand Resource type, a Permanent De-List Bid or Static De-List Bid for the Forward Capacity Auction, then no further submissions or actions for that resource are necessary, and the resource shall participate in the Forward Capacity Auction as a price-taker with Qualified Capacity as indicated in the ISO's notification.

221. The corresponding provision that applies to existing generating resources is contained in Section III.13.1.2.3 (Qualification Process for Existing Generating Capacity Resources). The language contained in that section includes the following:

> If an Existing Generating Capacity Resource does not submit a Static De-List Bid, an Export Bid, an Administrative Export De-List Bid, or a Permanent De-List Bid in the Forward Capacity Auction qualification process, then no further submissions or actions for that resource are necessary, and the resource shall be entered into the Forward Capacity Auction as described in Section III. 13.2.3.2(c)[133]

Both sections III.13.1.4.2.5.2 and III.13.1.2.3 appear to indicate that where de-list bids do not apply to existing generating and demand resources, those resources will be subject to III.13.2.3.2(c). Moreover, the transmittal language clearly indicates that both types of resource would operate as price-takers in the Forward Capacity Auction. However, the tariff clearly states that existing demand resources will be price takers, whereas there is no such declaration applicable to existing generating resources. The Commission directs ISO-NE to clarify this ambiguity.

222. The Commission notes that section III.13.1.4.1.1 of the proposed rules on FCM (Existing Demand Resources) states that: "Existing Demand Resources shall be subject to section III.13.1.2.2.2.6." The Commission, however, is unaware of any such provision in the proposed rules and, thus, directs ISO-NE to change this section of the proposed tariff language or otherwise provide clarification.

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[132] *See* ISO-NE's transmittal letter at 72 (existing generation) and at 92 (existing demand resources).

[133] Section III.13.1.2.3.

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223. The Commission notes that section 13.1.7, as filed, states that: "…the Internal Market Monitor shall take appropriate steps to ensure that the resource bid to de-list or export in the Forward Capacity Auction is not inappropriately replaced by that new capacity in a subsequent reconfiguration action." This final word – "action" – appears to be a misspelling of "auction." The Commission directs ISO-NE to make the above changes or provide clarification as necessary in the September 1 filing discussed above.

The Commission orders:

(A) We hereby accept the filing as discussed above, subject to the condition of ISO-NE filing the changes set forth in the body of this order.

(B) ISO-NE is required to file, on or before September 1, 2007, the modifications set forth above, as follows:

1. ISO-NE is required to revise its proposed tariff to state that if the Market Monitor determines that a bid or offer may be an attempt at manipulating the auction or the Forward Capacity Market or if it finds in its review of a resource's summer historical values that there may be an attempt to exercise physical withholding, the Market Monitor shall refer those matters to the Commission.

2. ISO-NE is required to revise its market rules to permit generators with temperature-dependent capacity to de-list at prices below 2 times Cost of New Entry

3. ISO-NE is required to modify its filing so that the maximum amount of import capacity contracts accepted in the auction over the HQ Interconnection should be limited to the total available capacity of the line minus the value of extant HQICCs, and to delete the requirement for reservations

(C) In its September 1 filing, ISO-NE is also required either to make the tariff changes discussed in paragraphs 218-224 above, which appear to be simply corrections of typographical or similar administrative errors, or else to explain why those tariff provisions are, in fact, correct as they stand.

(D) ISO-NE is required to file a report by July 15, 2007 on the status of the composite bid process in light of the June 15 deadline for submitting composite bids.

(E) ISO-NE is directed to adopt NECPUC's recommendation for a stakeholder process with regard to the accommodation of seasonal bids in the FCM. This stakeholder process should consider any option that better optimizes seasonal bids (particularly summer only) in the FCM. ISO-NE is also directed to submit, by February 29, 2008, a compliance filing that reports both on the composite bid process and on the status of this

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stakeholder process, including, if appropriate, a schedule for implementing options that better optimize seasonal bids for the second auction scheduled for December 2008.

(F) Also as discussed above, ISO-NE is required to include, in the informational filing to be made 90 days prior to the Forward Capacity Auction, an analysis of evidence, if any, of price searching behavior on behalf of existing generating capacity resources.

By the Commission.

(S E A L)

Philis J. Posey,
Deputy Secretary.

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Appendix A

Timely motions to intervene:

American Wind Energy Association
J. Aron and Company
Bridgeport Energy Company
Richard Blumenthal, the Attorney General of Connecticut
Casco Bay Energy Company
Conservation Law Foundation
Energy Management
Fitchburg Gas and Electric Light Company
Massachusetts Attorney General
Massachusetts Division of Energy Resources
United Illuminating Company

Timely motions to intervene, comments and protests:

Con Edison Energy (Con Ed)
New England Conference of Public Utilities Commissioners (NECPUC)
PSEG Power Companies (PSEG)
National Grid USA (National Grid)
Massachusetts Department of Telecommunications and Energy (Mass DTE)
Comverge, Inc., *et al.* (the DR Coalition)
H.Q. Energy Services, U.S. (HQUS)
New England Power Pool Participants Committee (NEPOOL)
New Hampshire Public Utilities Commission (NHPUC)
Capacity Suppliers[134]
NRG Companies (NRG)
Conservation Law Foundation
PPL Companies (PPL)
NSTAR Electric and Gas Corporation (NSTAR)
Milford Power Company (Milford)
Connecticut Department of Public Utility Control (CT DPUC)
Massachusetts Municipal Wholesale Electric Company and Connecticut Municipal Electric Energy Cooperative (Public Systems)
IRH Management Committee (IRH)
Maine Public Utilities Commission (Maine PUC)
Long Island Power Authority (LIPA)

[134] The Capacity Suppliers consist of Boston Generating, FPL Energy, and the Mirant Parties (Mirant Energy Trading, Mirant Canal, and Mirant Kendall).

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FirstLight Parties (FirstLight)
Vermont Department of Public Service and Vermont Public Service Board (VDPS),
Connecticut Office of Consumer Council (CT OCC)
International Power America and ANP Northeast Development (International Power)
Brookfield Energy Marketing
Conservation Services Group (Conservation Services)
Exelon Corporation (Exelon)
Cape Light Compact
Dominion Resources Services (Dominion)
EnerNOC
Pinpoint Power
Northeast Utilities Service Company (Northeast Utilities).

Motion to intervene out of time:

NEPOOL Industrial Customer Coalition (NICC).
BG Energy Merchants, LLC, BG Dighton Power, LLC, and Lake Road Generating, LP (BG Entities)

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Appendix B

Forward Capacity Auction	Commitment Period	Show of Interest Window for New Capacity		Existing Capacity Qualification Deadline	New Capacity Qualification Deadline	First Day of Forward Capacity Auction
1	June 1, 2010 - May 31, 2011	Nov. 1, 2006	Jan. 3, 2007	April 30, 2007	June 15, 2007	Feb. 4, 2008
1 (Demand Resources)	June 1, 2010 - May 31, 2011	Dec. 18, 2006	Feb. 28, 2007	April 30, 2007	June 15, 2007	Feb. 4, 2008
2	June 1, 2011 - May 31, 2012	Sept. 4, 2007	Oct. 21, 2007	Feb. 29, 2008	April 15, 2008	Dec. 1, 2008
3	June 1, 2012 - May 31, 2013	July 1, 2008	Sept. 2, 2008	Dec. 31, 2009	Feb. 17, 2009	Oct. 5, 2009
4	June 1, 2013 - May 31, 2014	May 1, 2009	June 30, 2009	Nov. 2, 2009	Dec. 15, 2009	Aug. 2, 2010
5	June 1, 2014 - May 31, 2015	March 1, 2010	April 30, 2010	Aug. 31, 2010	Oct. 15, 2010	June 6, 2011
6	June 1, 2015 - May 31, 2016	Jan. 3, 2011	Feb. 28, 2011	June 30, 2011	Aug. 15, 2011	April 2, 2012
7	June 1, 2016 - May 31, 2017	Nov. 1, 2011	Jan. 2, 2012	April 30, 2012	June 15, 2012	Feb. 4, 2013
8	June 1, 2017 - May 31, 2018	Nov. 1, 2012	Dec. 31, 2012	April 30, 2013	June 17, 2013	Feb. 3, 2014