UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

New England Power Generators Association, Inc.	)	
	)	Docket No. EL14-7-000
v.	)	
ISO New England Inc.	)	
ISO New England Inc.	)	Docket No. ER14-463-000 (not consolidated)

REQUEST FOR REHEARING AND CLARIFICATION OF THE NEW ENGLAND POWER GENERATORS ASSOCIATION

Pursuant to Section 313 of the Federal Power Act ("FPA"), 16 U.S.C. § 825l (2012), and Rule 713 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission ("FERC" or "Commission"), 18 C.F.R. § 385.713 (2013), the New England Power Generators Association, Inc. ("NEPGA") submits this request for rehearing and clarification of the Commission's Order on Complaint, issued in Docket No. EL14-7-000 on January 24, 2014,[1] and the Commission's Order on Tariff Filing, issued in Docket No. ER14-463-000 on January 24, 2014[2] (collectively, the "January 24 Orders"). In support of this request, NEPGA states as follows:

[1] *New England Power Generators Association, Inc. v. ISO New England Inc.*, 146 FERC ¶ 61,039 (2014) ("Complaint Order").

[2] *ISO New England Inc.*, 146 FERC ¶ 61,038 (2014) ("Tariff Order").

I. INTRODUCTION AND SUMMARY

On October 31, 2013, NEPGA filed a Complaint against ISO New England Inc. ("ISO-NE"), asserting that the administrative pricing rules applicable in circumstances of Inadequate Supply and Insufficient Competition and the zero-price bidding requirement applicable to new capacity resources under the Capacity Carry Forward Rule suppressed market prices, resulted in unjustified and detrimental price discrimination between new and existing resources, and were unjust, unreasonable and unduly discriminatory. NEPGA urged that the Commission replace the existing pricing rules for Inadequate Supply and Insufficient Competition with prices previously recommended by ISO-NE which were based on the Offer Review Trigger Prices ("ORTPs") developed by ISO-NE to replace the pre-existing cost of new entry ("CONE") values and that the Commission eliminate the requirement that new capacity resources subject to the Capacity Carry Forward Rule offer capacity at $0/kW-month.

ISO-NE did not defend the existing Inadequate Supply and Insufficient Competition pricing rules, but opposed the use of the recently-approved ORTPs and argued instead for prices based on the discredited and superseded CONE values. ISO-NE opposed NEPGA's Complaint with regard to the Capacity Carry Forward Rule. On January 24, 2014, the Commission issued the Complaint Order and the Tariff Order. The Commission granted NEPGA's Complaint with regard to the existing Inadequate Supply and Insufficient Competition pricing rules, but declined to adopt ORTP-based pricing and approved instead the CONE-based values proposed by ISO-NE. The Commission denied NEPGA's Complaint with regard to the Capacity Carry Forward Rule. In addition, the Commission directed ISO-NE to make a tariff filing by April 1, 2014, to implement a sloped demand curve for the Forward Capacity Market ("FCM"), to be effective for the next capacity auction, FCA 9.

In declining to rely upon the Commission-approved ORTPs and in denying NEPGA's Complaint with regard to the Capacity Carry Forward Rule, the Commission erred and it should grant rehearing to correct these errors and to remedy the capacity market price suppression and price discrimination that will continue absent administratively-determined prices that more accurately reflect the cost of new entry and bidding rules for new entrants that do not skew capacity prices for existing suppliers. The Commission should also clarify certain aspects of the January 24 Orders in order to ensure that the Commission's intended directives are fully implemented for FCA 9.

NEPGA requests that the Commission grant rehearing or clarification of three aspects of the January 24 Orders. First, the Commission should grant rehearing and require that prospective auctions utilize ORTP-based prices, which more accurately reflect the cost of new entry and which will provide for capacity market prices that retain existing resources and incent new entry. The Commission concluded that capacity prices must meet this standard and correctly determined that the current market rules produced capacity prices in instances of Inadequate Supply and Insufficient Competition that are far below the cost of new entry. Yet the Commission erred when it failed to apply this same standard to the $7.025/kW-month adopted by the January 24 Orders. The methodology used to calculate the $7.025/kW-month value is flawed and was previously rejected by the Commission in favor of the ORTPs. While NEPGA does not support reopening the FCA 8 auction results, NEPGA is concerned that the administrative pricing rules may have other applications going forward. Thus, for all prospective applications the Commission should grant rehearing and should direct that capacity prices be set in a manner that most accurately reflects the cost of new entry in order to retain existing resources, incent new entry, and ensure reliability.

Second, notwithstanding the Commission's order that ISO-NE limit the $7.025/kW-month proxy to FCA 8 only, it is NEPGA's understanding that ISO-NE intends to propose a sloped demand curve for pool-wide purposes for FCA 9, but will not implement sloped demand curves for individual capacity zones for FCA 9 and will continue to utilize administrative prices for intra-zonal capacity price determinations. The Commission should clarify the Tariff Order to direct ISO-NE to implement a market design utilizing a sloped demand curve for all aspects of the FCM so that there is no continuation of the current unjust and unreasonable and unduly discriminatory administrative price rules for Insufficient Competition and Inadequate Supply for FCA 9. The Tariff Order found that the current administrative pricing rules are unjust and unreasonable and did not provide for a phased implementation of the sloped demand curve.

Finally, the Commission should grant rehearing and should conclude that the zero bid requirement associated with the Capacity Carry Forward Rule is unjust and unreasonable and unduly discriminatory and should adopt the remedy recommended by NEPGA and currently in place in other markets. In rejecting arguments that the zero price bid requirement suppresses prices and promotes unreasonable price discrimination, the Commission mistakenly failed to account for the link between the applicable Capacity Supply Obligation and the price suppression resulting from zero-price bids and incorrectly linked Commission precedent barring zero-price bids to capacity markets utilizing a sloped demand curve when, in fact, the Commission has correctly rejected zero-price bids in multiple market designs. Substantial record evidence shows that zero price bids consistently suppress prices and lead to price discrimination regardless of the specific context in which such flawed bidding rules are applied. The Commission should grant rehearing and should require ISO-NE to eliminate the zero-bid requirement and implement the bidding protocols requested by NEPGA in its Complaint.

II. STATEMENT OF ISSUES

Pursuant to Rule 713(c)(2), 18 C.F.R. § 385.713(c)(2) (2013), NEPGA provides the following statement of issues:

A. The January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to reconcile the acceptance of ISO-NE's proposed capacity price of $7.025/kW-month with prior Commission precedent holding that capacity prices must be sufficient to incent new entry, retain existing capacity and provide price signals to the market that accurately reflect the cost of new entry. *See, e.g., ISO New England Inc.*, 125 FERC ¶ 61,102 (2008), *reh'g denied*, 130 FERC ¶ 61,089 (2010); *Blumenthal v. ISO New England Inc.*, 117 FERC ¶ 61,038 (2006), *reh'g denied,* 118 FERC ¶ 61,205 (2007), *review denied sub nom. Blumenthal v. FERC*, 552 F.3d 875 (D.C. Cir. 2009); *see also PJM Interconnection, L.L.C.*, 126 FERC ¶ 61,275, *clarified*, 127 FERC ¶ 61,104, *on reh'g*, 128 FERC ¶61,157 (2009); *New York Independent System Operator, Inc.*, 103 FERC ¶ 61,201 (2003), *reh'g denied*, 105 FERC ¶ 61,108 (2003), *review denied sub nom. Electricity Consumers Resource Council v. FERC*, 407 F.3d 1232 (D.C. Cir. 2005). The Commission must explain a departure from prior precedent, and the January 24 Orders fail to adequately address the Commission's departure from its prior holdings regarding the appropriate pricing of capacity. *See, e.g, Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970) ("an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion it may cross the line from the tolerably terse to the intolerably mute") (footnotes omitted); *La. Pub. Serv. Comm'n v. FERC*, 184 F.3d 892, 897 (D.C. Cir. 1999) ("for the agency to reverse its position in the face of a precedent it has not persuasively distinguished is quintessentially arbitrary and capricious").

B. The January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to address the substantial record evidence establishing that the Offer Review Trigger Prices are a more accurate measure of the cost of new entry than the historic CONE that forms the basis of the capacity rates approved by the Commission for FCA 8. Courts have repeatedly held that the Commission is obligated to address issues raised before it, and that a "'failure to respond meaningfully' to objections raised by a party renders its decision arbitrary and capricious." *PPL Wallingford Energy LLC v. FERC*, 419 F.3d 1194, 1198 (D.C. Cir. 2005) (*quoting Canadian Association of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001)). An agency must "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'" *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (*quoting Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)); *see also Ass'n of Data Processing Serv. Org. v. Bd. Of*

Governors of the Fed. Reserve Sys., 745 F.2d 677, 684 (D.C. Cir. 1984) (holding that an agency's decisions must be supported by substantial evidence contained within the record); *Tarpon Transmission Co. v. FERC*, 860 F.2d 439, 442 (D.C. Cir. 1988) (agency decision must be "result of reasoned and principled decisionmaking that can be ascertained from the record"); *Florida Gas Transmission Co. v. FERC*, 604 F. 3d 636 (D.C. Cir. 2010) ("Under [the arbitrary and capricious] standard, the Commission 'must be able to demonstrate that it has made a reasoned decision based upon substantial evidence in the record.'") (*quoting Pac. Gas & Elec. Co. v. FERC*, 373 F. 3d 1315, 1319 (D.C. Cir. 2004).

C. The January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to justify the Commission's departure from the market design approved by the Commission for the FCM and the principles that underlie that market design. *See, e.g., ISO New England Inc.*, 125 FERC ¶ 61,102 (2008), *reh'g denied*, 130 FERC ¶ 61,089 (2010); *Blumenthal v. ISO New England Inc.*, 117 FERC ¶ 61,038 (2006), *reh'g denied,* 118 FERC ¶ 61,205 (2007), *review denied sub nom. Blumenthal v. FERC*, 552 F.3d 875 (D.C. Cir. 2009); *see also PJM Interconnection, L.L.C.*, 126 FERC ¶ 61,275, *clarified*, 127 FERC ¶ 61,104, *on reh'g*, 128 FERC ¶ 61,157 (2009); *New York Independent System Operator, Inc.*, 103 FERC ¶ 61,201 (2003), *reh'g denied*, 105 FERC ¶ 61,108 (2003), *review denied sub nom. Electricity Consumers Resource Council v. FERC*, 407 F.3d 1232 (D.C. Cir. 2005). The Commission must explain a departure from prior precedent, and the January 24 Orders fail to adequately address the Commission's departure from its prior holdings regarding the appropriate pricing of capacity. *See, e.g., Motor Vehicle Mfrs. Assn. of the U.S., Inc. v. State Farm Mutual Automobile Ins. Co.*, 463 U.S. 29, 54-56 (1983); *Burlington Truck Lines, Inc. v. U.S.*, 371 U.S. 156, 166-68 (1962); *ANR Pipeline Co. v. FERC*, 71 F.3d 897, 902-03 (D.C. Cir. 1995); *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970) ("an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion it may cross the line from the tolerably terse to the intolerably mute") (footnotes omitted); *La. Pub. Serv. Comm'n v. FERC*, 184 F.3d 892, 897 (D.C. Cir. 1999) ("for the agency to reverse its position in the face of a precedent it has not persuasively distinguished is quintessentially arbitrary and capricious").

D. The January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to justify and explain the Commission's use of a balancing approach to depart from the market design approved for the FCM. *See, e.g, Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970) ("an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion it may cross the line from the tolerably terse to the intolerably mute") (footnotes omitted); *La. Pub. Serv. Comm'n v. FERC*, 184 F.3d 892, 897 (D.C. Cir. 1999) ("for the agency to reverse its position in the face of a precedent it has not persuasively distinguished is

quintessentially arbitrary and capricious"); *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (An agency must "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'") (*quoting Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)).

E. Absent clarification, the January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to support the prospective use within individual capacity zones of administrative pricing rules determined to be unjust and unreasonable. *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (An agency must "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made,'" and it is error for an agency to "entirely fail[] to consider an important aspect of the problem") (*quoting Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)).

F. The January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to address the price suppressing effects and price discrimination that result from the zero bid requirement of the Capacity Carry Forward Rule. Courts have repeatedly held that the Commission is obligated to address issues raised before it, and that a "'failure to respond meaningfully' to objections raised by a party renders its decision arbitrary and capricious." *See PPL Wallingford Energy LLC v. FERC*, 419 F.3d 1194, 1198 (D.C. Cir. 2005) (*quoting Canadian Association of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001)). Unless the Commission "answers objections that on their face seem legitimate, its decisions can hardly be classified as reasoned." *See Motor Vehicle Mffrs. Ass'n v. State Farm Mu. Auto Insurance Co.*, 463 U.S. 29, 43 (1983) (error for agency to "entirely fail[] to consider an important aspect of the problem"); *NorAm Gas Transmission Co. v. FERC, 148 F.3d 1158* (D.C. Cir. 1998) ("It most emphatically remains the duty of this court to ensure that an agency engage the arguments raised before it-that it conduct a process of reasoned decision-making.") (*quoting K N Energy, Inc. v. FERC*, 968 F.2d 1295, 1303 (D.C. Cir. 1992)).

G. The January 24 Orders are arbitrary and capricious, and are not the product of reasoned decisionmaking, because they fail to adequately distinguish prior Commission findings that $0 bids distort markets and are unduly discriminatory. The Commission must explain a departure from prior precedent, and the January 24 Orders fail to adequately address the Commission's departure from its prior holdings regarding the detrimental impacts zero bids have on markets. *See, e.g., Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970) ("an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion it may cross the line from the tolerably terse to the intolerably mute") (footnotes omitted); *La. Pub. Serv. Comm'n v. FERC*, 184 F.3d 892, 897 (D.C. Cir. 1999) ("for the agency to reverse its position in the face of a precedent it has not persuasively distinguished is quintessentially arbitrary and capricious").

III. ARGUMENT

A. The Commission Should Grant Rehearing And Should Require Capacity Prices To Be Based On Offer Review Trigger Prices, Which More Accurately Reflect The Cost Of New Entry And Provide For Prices Consistent With FCM Market Design.

The Commission has routinely found that capacity prices must be sufficient to incent new entry and to retain existing capacity resources.[3] In New England, the FCM market design is based on competitive market outcomes and a single clearing price and relies on market signals to ensure efficiency and reliability.[4] Accurate price signals are the cornerstone of the FCM market design. The Commission has previously stated that "[t]he purpose of the New England FCM is to attract and retain sufficient capacity to maintain ISO-NE's Installed Capacity Requirement [("ICR")], and to do so, FCM capacity prices will need to average out over time to the cost of new entry."[5] In this proceeding, ISO-NE conceded that the administrative pricing rules applicable in cases of Insufficient Competition and Inadequate Supply produced capacity prices that were so low that they undermined investor confidence[6] and the Commission found those rules to be unjust and unreasonable.[7]

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[3] *See Blumenthal v. ISO New England Inc.*, 117 FERC ¶ 61,038, at P 83 (2006), *reh'g denied,* 118 FERC ¶ 61,205 (2007), *review denied sub nom. Blumenthal v. FERC*, 552 F.3d 875 (D.C. Cir. 2009).

[4] *ISO New England Inc.*, 125 FERC ¶ 61,102 at P 43 (2008), *reh'g denied*, 130 FERC ¶ 61,089 (2010). The Commission stated this point clearly: "properly constructed capacity markets can . . . encourage reliable and efficient levels of investment only if market participants can expect prices that provide a reasonable opportunity to recover the costs of needed investment." *New York Independent System Operator*, 122 FERC ¶ 61,211 at P 105, *on reh'g*, 124 FERC ¶ 61,301 (2008), *on reh'g and clarification*, 131 FERC ¶ 61,170 (2010).

[5] *ISO New England Inc.,* 125 FERC ¶ 61,102 at P 43.

[6] Exigent Circumstances Filing of Revisions to Forward Capacity Market Rules at p. 13, Docket No. ER14-463-000 (Nov. 25, 2013).

[7] *See* Tariff Order at P 1; *see* Complaint Order at PP 1, 46-49.

In the Tariff Order, the Commission acknowledged that just and reasonable rates for the FCM must accurately reflect the cost of new entry,[8] but failed to apply this same standard to evaluate the $7.025/kW-month price ISO-NE sought to adopt in place of the current tariff provisions. In so holding, the Commission failed to properly account for substantial record evidence that shows that the ORTP values recently approved by the Commission are a much more accurate reflection of the cost of new entry, and that administratively-determined prices that are based on such values provide prices that more clearly meet the Commission's requirement that capacity prices be sufficient to incent new entry and retain existing capacity resources. Moreover, the Commission erred when it failed to justify or explain its departure from its prior orders and from the prevailing FCM market design, which mandate that capacity prices should reflect the costs of new entry.

Accordingly, the Commission should grant rehearing of the January 24 Orders and should provide for the administrative prices applicable in cases of Inadequate Supply and Insufficient Competition to be based on ORTPs, which are a more accurate measure of the cost of new entry and which will result in prices that are consistent with FCM market design. While NEPGA does not support reopening the FCA 8 auction results, as discussed in section III.B., NEPGA is concerned that the administrative pricing rules may have other applications going forward. Thus, for all prospective applications the Commission should grant rehearing and should direct that capacity prices be set in a manner that most accurately reflects the cost of new entry in order to retain existing resources, incent new entry, and ensure reliability.

[8] Tariff Order at P 26 ("It is undisputed that the administrative pricing provisions applicable to existing capacity resources under the Inadequate Supply and Insufficient Competition provisions are intended to establish just and reasonable prices adequate to incent new entry and retain existing resources – both of which help ensure reliability."); *id.* at P 28 ("we find that the tariff's current administrative pricing for existing resources in situations of Inadequate Supply and Insufficient Competition are unjust and unreasonable, as the provisions result in prices that are likely inadequate to incent new entry and retain existing resources.").

1. Substantial record evidence shows that ORTPs are far more accurate measures of the cost of new entry than the "historic CONE" that is the basis for the rates for FCA 8 approved by the Tariff Order.

The ORTP values were proposed by ISO-NE and approved by the Commission in order to remedy the pervasive flaws in the prior CONE values, and the Commission erred when it rejected administrative prices based on ORTPs and adopted prices based on the superseded and discredited "historic CONE" values.[9]

First, substantial evidence shows that the ORTPs more accurately reflect the cost of new entry. Indeed, the only reason ORTPs exist is because the Commission specifically directed ISO-NE to eliminate the use of CONE values and to rely instead on ORTPs.[10] The ORTPs applicable for FCA 8 were based on a detailed bottom-up study performed by Shaw Consultants and ISO-NE's Internal Market Monitor ("IMM") relying on a process similar to that used by PJM and NYISO to develop cost of new entry values for their respective capacity markets.[11] The ORTPs are based on estimates of the 20 year levelized cost of new entry for various technologies, which values are an estimate of the competitive cost of new entry under long term equilibrium assumptions.[12] These values were subsequently reviewed and approved in a

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[9] *See* Tariff Order at P 13 ("ISO-NE explains that this value is derived by applying the rules in place for FCA 7 (*i.e.*, the administrative price is equal to Cost of New Entry (CONE) times 1.1). ISO-NE states that, if the historical CONE were still applicable for FCA 8, it would be $6.386 (the FCA 7 historical CONE of $6.055 escalated using the Handy-Whitman Index of 1.0546)." (footnote omitted)). Pursuant to the ISO-NE Tariff, the administrative price is 1.1 times CONE, which produces $7.025/kW-month.

[10] *ISO New England Inc. and New England Power Pool Participants Committee*, 135 FERC ¶ 61,029 at PP 166-69 (2011) ("we find that applying offer-floor mitigation to the ISO-NE capacity market with values based on the proposed benchmarks from the July 1 proposal would render the FCM just and reasonable . . . The auction would select the lowest-cost set of resources needed to meet the ICR, and no more."), *order on reh'g and clarification*, 138 FERC ¶ 61,027 (2012).

[11] *See* Prepared Direct Testimony of Michael M. Schnitzer at p. 8 ("Schnitzer Testimony"), included as Exhibit 1 to the *Complaint of the New England Power Generators Association, Inc. and Request for Fast Track Processing*, Docket No. EL14-7-000 (Oct. 31, 2013) ("Complaint").

[12] ORTPs are calculated in accordance with ISO-NE Tariff § III.A.21.1.2 and the specific ORTPs are set out at ISO-NE Tariff § III.A.21.1.1. ISO-NE has adopted the Offer Review Trigger Prices ORTPs For FCA 8; the ISO's ORTP values are $10.00/kW-month and $11.00/kW-month for combustion turbines and combined cycle gas

stakeholder process.[13] The Commission approved these values for use in FCA 8, holding the assumptions behind the ORTPs, as well as the ORTPs themselves, were "well within the range of reasonableness." [14]

In fact, ORTPs are conservative and likely understate the actual cost of new entry. The ORTP values were "designed to represent prices at the low end of the range of competitive offers for each resource type."[15] As ISO-NE explained when proposing the ORTPs, it "would be improbable that a new resource of a given type could rationally enter the market at a price below the applicable Offer Review Trigger Price absent a subsidy of some kind."[16] In its December 2012 compliance filing ISO-NE explained that it believed the ORTPs "would be a far better estimate of the revenues that a new peaking resource would need to recover from the capacity market."[17]

The record is equally clear that the historic CONE values that are the basis for the $7.025/kW-month administrative price approved by the Tariff Order are profoundly flawed and that there was good reason to reject these values in favor of ORTPs. The concept of CONE began in the initial FCM settlement, and was an agreed-upon "black box" value of $7.50/kW-

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turbines, respectively, and are subject to annual adjustment. *ISO New England Inc.*, 142 FERC ¶ 61,107 at PP 37-38 ("February 2013 Order").

13 *See* Forward Capacity Market Redesign Compliance Filing and Request for Waiver of Compliance Obligation, or, In The Alternative, Limited Filing Pursuant to Section 205 of the Federal Power Act at p. 44, Docket No. ER12-953-001 (Dec. 3, 2012) ("December 2012 Compliance Filing").

14 February 2013 Order at PP 37-38.

15 December 2012 Compliance Filing, Joint Testimony of Marc D. Montalvo and David H. Naughton, at p. 4 ("Montalvo and Naughton Testimony"). To calculate the ORTP for generation resources, capital costs, expected non-capacity revenues and operating costs, assumptions regarding depreciation, taxes and discount rate are input into a capital budgeting model which is used to calculate the level of FCM revenues necessary to yield a discounted cash flow with a net present value of zero for the resource. *Id*. at p. 6.

16 *Id*. at p. 4.

17 *See* December 2012 Compliance Filing at p. 44.

month for FCA 1. This FCA 1 CONE figure was then reduced from $7.50/kW-month to $6.00/kW-month in FCA 2 and to $4.92/kW-month in FCA 3 by applying a formula that averaged the prior year's CONE and the prior year's auction clearing price. This averaging process caused the resulting CONE values to diverge substantially from the true cost of new entry because no new entry was required in FCA 1 and FCA 2, and the clearing prices in such auctions – a substantial factor in the formulaic determination of CONE – were set by the auction floor price which bore no relation to the cost of new entry.[18] As a result, by FCA 4, CONE had *declined* from $7.50/kW-month to $4.918/kW-month.[19]

At that time, ISO-NE acknowledged that the flawed methodology used to recalculate CONE had produced values that no longer represented a credible estimate of the cost of new entry. In a joint filing submitted by ISO-NE and NEPOOL on February 22, 2010, ISO-NE explained that $4.918/kW-month was "significantly below most estimates of the cost of new entry for generating resources."[20] However, ISO-NE did not adjust the CONE values to correct for the distortion attributable to the prior averaging process. Instead ISO-NE held the FCA 4 CONE value constant at its artificially depressed level for one year, and then escalated it thereafter using the Handy Whitman Index. The resulting CONE trajectory is shown in the figure below.

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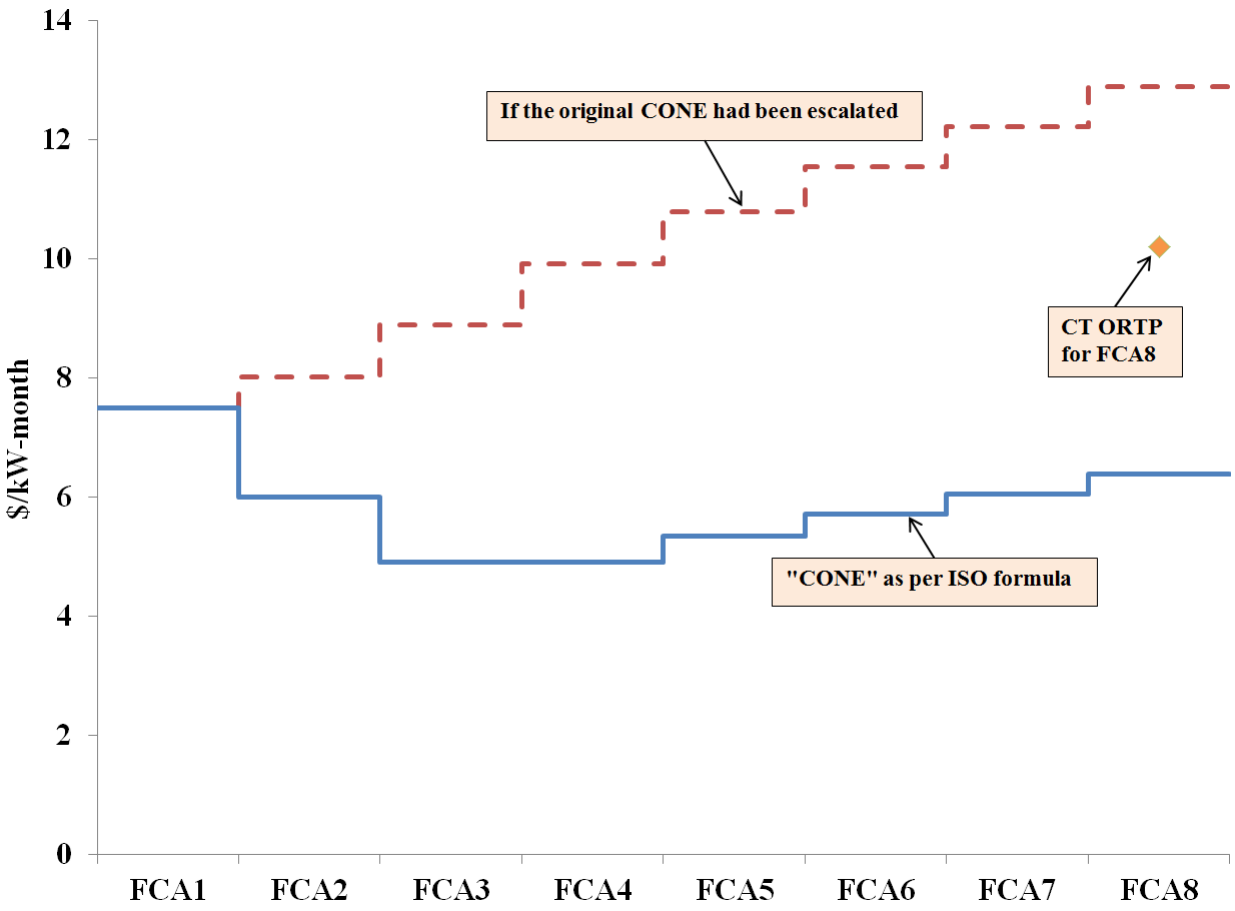
[18] *See* Prepared Supplemental Testimony of Michael M. Schnitzer ("Schnitzer Supplemental Testimony"), included as Exhibit 1 to the *Protest of Tariff Filing and Motion for Leave to Answer and Answer of the New England Power Generators Association*, Docket Nos. EL14-7-000 and ER14-463-000 (Dec. 16, 2013) ("Protest").

[19] Protest at p. 30; Schnitzer Supplemental Testimony at pp. 8-9.

[20] Various Revisions to FCM Rules Related to FCM Redesign at p. 22, Docket No. ER10-787-000 (Feb. 22, 2010).

FIGURE 1



The $7.025/kW-month approved in the Tariff Order is simply a further escalation of the $4.918/kW-month CONE value from FCA 4, escalated in accordance with the Handy-Whitman Index.[21]

This figure illustrates clearly the error of relying on the historic CONE values to set administrative prices for Inadequate Supply and Insufficient Competition. As the figure illustrates, by FCA 4 the flawed "floor price" averaging formula created a $5 per kW-month deficit between the "CONE" value under the tariff, and what the FCA 1 CONE value would have

[21] *See* Tariff Order at PP 13-14; *see* Exigent Circumstances Filing of Revisions to Forward Capacity Market Rules at pp. 10-13, Docket No. ER14-463-000 (Nov. 25, 2013).

been if the $7.50/kW-month FCA 1 value had been escalated using the same Handy Whitman Index from the beginning. The figure also illustrates that the $7.025/kW-month approved in the Tariff Order is roughly 40 percent lower than the IMM's detailed and well supported estimate of the FCA 8 ORTP for a combustion turbine. $7.025/kW-month is also less than one-half of the price needed to produce new entry in FCA 7, in which Footprint Power cleared 647 MW at $14.99/kW-month.

The Tariff Order contains no substantive discussion of the methodology used to support the ORTP values or the $7.025/kW-month or any analysis of whether $7.025/kW-month represents the cost of new entry in FCA 8. At most, the Commission states that "ISO-NE's proposal . . . is more consistent with the provisions' intent because it pays existing resources a price that is more reflective of supply conditions."[22] However, even this comparison is flawed because it contrasts $7.025/kW-month to the much lower prices that would result from the tariff provisions the Commission finds to be unjust and unreasonable and does not evaluate ISO-NE's proposal against ORTPs. The comparison is also flawed in that the $7.025/kW-month does not actually reflect supply conditions.

The FCM market design is built on the foundation that capacity prices should mirror the cost of new entry and that such prices will retain existing resources, incent new entry, and ensure reliability. Having relied upon this standard to determine that the existing tariff is unjust and unreasonable, the Commission erred when it did not evaluate the $7.025/kW-month price using that same standard, particularly when, as detailed above, substantial record evidence shows that $7.025/kW-month falls far short of a price that is consistent with Commission precedent and

[22] Tariff Order at P 28.

FCM market design.[23] The Commission's failure to follow its well-established practice that capacity prices accurately reflect the cost of new entry in order to retain existing resources and incent new entry and its failure to justify or explain its apparent departure from that practice is arbitrary and capricious.[24] Accordingly, the Commission should grant rehearing and should direct ISO-NE going forward to use the ORTP-based values, which are far better estimates of the cost of new entry and which are in line with the prevailing FCM market design.

2. The Commission failed to justify or explain its use of a "balancing" approach to depart from the market design approved for the FCM.

The Tariff Order appears to concede that its approval of the $7.025/kW-month proxy price departs from a result that would more closely follow the FCM market design. In the Tariff Order, the Commission frames its decision-making as balancing on the one hand the need to promote prices which accurately reflect the cost of new entry, the market design that underlies the FCM market, against, on the other hand, the need to restrain excessive price volatility.[25] The Commission then concludes that $7.025/kW-month represents a reasonable balance "of these somewhat competing principles."[26]

The Commission should grant rehearing and provide for rates that reflect the appropriate cost of new entry consistent with the market design found to be just and reasonable. The magnitude of the current market rules' failure to produce just and reasonable rates should not be

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[23] In the Tariff Order, the Commission does not conclude that $7.025/kW-month is sufficient to incent new entry or to retain existing resources, nor does the Commission countermand its prior determination that ORTPs more accurately reflect prices needed to incent new entry and retain existing resources.

[24] *See, e.g., Motor Vehicle Mfrs. Assn. of the U.S., Inc. v. State Farm Mutual Automobile Ins. Co.*, 463 U.S. 29, 54-56 (1983); *Burlington Truck Lines, Inc. v. U.S.*, 371 U.S. 156, 166-68 (1962); *ANR Pipeline Co. v. FERC*, 71 F.3d 897, 902-03 (D.C. Cir. 1995).

[25] Tariff Order at PP 26-27.

[26] *Id.* at P 26.

a bar to implementing the intended, appropriate market design. Just and reasonable capacity prices track the cost of new entry and thereby produce a single price that is sufficient to retain existing resources and incent new entry. As Mr. Schnitzer explained in his supplemental testimony, prices that change in response to changes in the supply/demand balance in a market are efficient, not "lurching."[27] Where, as is the case here, the existing tariff fails to produce just and reasonable rates, the correct response is to establish new tariff rules that result in rates that mirror the cost of new entry. However, as is also the case here, where the flawed market rules produce rates that are far below a just and reasonable level, that fact should not be a reason to abandon the well-founded principles upon which the market is designed in order to adopt an equally flawed "middle ground." NEPGA supports the Commission's long-held principles favoring contract certainty emerging from auctions and does not dispute the FCA 8 auction results. Instead, NEPGA stresses that the ORTP-based benchmarks must be used going forward to ensure sound market outcomes supporting necessary investment to meet resource adequacy.

A substantial departure from the market design principles that produce just and reasonable rates is of course not without cost. Administrative pricing rules that perpetuate artificially low capacity prices mute price signals, institutionalize two tier pricing and reinforce the need for new entrants to recover a disproportionate amount of their investment during the NEPA period, because once they become existing resources they will see their capacity revenues decline precipitously. As Mr. Schnitzer explained in his prepared direct testimony, "existing ISO-NE market rules promote, rather than prevent, structural price discrimination between new

[27] Schnitzer Supplemental Testimony at p. 12.

and existing resources – with results that are neither efficient nor sustainable."[28] The result is a two-tiered rate structure in which new resources are paid a high price to incent new entry while existing resources are mitigated to an artificially low level well below the level needed to retain existing resources or to incent new entry. Given that the FCM market design is based on competitive market outcomes and a single clearing price, it is axiomatic that tariff-imposed capacity prices for all vintages of resources should be the same and should be sufficient to support existing economic resources and to provide for new entry when needed.[29] As the Commission explained in addressing similar issues in the PJM market: "A market should be designed correctly so that the contribution to reliability from both new entrants and existing suppliers is compensated comparably."[30]

Where the Commission departs from established market design principles without examining the costs and risks of such departure or explaining the specific reasons for such departure, its decision-making is properly held to be arbitrary and capricious.[31] Broad, general statements concerning the need to "balance" various factors, without more, do not cure this deficiency.[32] Accordingly, the Commission should grant rehearing and should adopt

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[28] Schnitzer Testimony at p. 3. These practices are discouraging market based entry, because potential entrants know they will likely never have an opportunity to realize new entry level prices once they are treated as an existing resource. Schnitzer Supplemental Testimony at p. 12.

[29] *See, e.g., PJM Interconnection, L.L.C.,* 126 FERC ¶ 61,275 at P 149, *clarified*, 127 FERC ¶ 61,104, *on reh'g*, 128 FERC ¶ 61,157 at PP 101-02 (2009) ("In order to assure reliability, PJM needs to attract new entry when needed, but also assure that prices are sufficient to retain existing efficient capacity. Both new entry and retention of existing efficient capacity are necessary to ensure reliability and both should receive the same price so that price signals are not skewed in favor of new entry."); *New York Independent System Operator, Inc*., 103 FERC ¶ 61,201 at P 81 (2003) ("all capacity suppliers, regardless of the age of their resources, are entitled to the same treatment in the ICAP market"), *reh'g denied*, 105 FERC ¶ 61,108 (2003), *review denied sub nom. Electricity Consumers Resource Council v. FERC*, 407 F.3d 1232 (D.C. Cir. 2005).

[30] *PJM Interconnection, L.L.C*., 128 FERC ¶ 61,157 at P 103.

[31] *See, e.g., La. Public Service Comm'n v. FERC*, 184 F.3d 892, 897 (D.C. Cir. 1999).

[32] *See, e.g., Philadelphia Gas Works v. FERC*, 989 F.2d 1246, 1251 (D.C. Cir. 1993).

prospectively ORTP-based prices that are well-supported in record evidence and which will result in prices that are consistent with the FCM market design. Commissioner Clark stated this clearly in his dissent to the Tariff Order.[33]

B. The Commission Should Clarify That The $7.025/kW-Month Proxy Price May Be Used Only In FCA 8 And That The Sloped Demand Curve Shall Replace The Current Administrative Pricing Provisions In All Respects For FCA 9.

In the Tariff Order, the Commission stated in several instances that the $7.025/kW-month value proposed by ISO-NE is to be applied for FCA 8 only, and that the current administrative pricing rules are to be replaced by a sloped demand curve to be in place for FCA 9.[34] It is NEPGA's understanding, however that ISO-NE intends to propose a sloped demand curve for pool-wide purposes for FCA 9, but that it does not intend to implement sloped demand curves for individual capacity zones for FCA 9, deferring this step until a subsequent auction. As a result, ISO-NE will continue to utilize administrative prices for FCA 9 for intra-zonal capacity price determinations. The Commission should clarify the Tariff Order to direct ISO-NE to implement a market design utilizing a sloped demand curve for all aspects of the FCM so that there is no continuation of the current unjust and unreasonable and unduly discriminatory administrative price rules for Insufficient Competition and Inadequate Supply for FCA 9.

The FCM determines capacity prices based on supply curves established separately for the entire New England Control Area and for each of the individual Capacity Zones within that

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[33] *See* Tariff Order (Clarke, Commissioner, dissenting) ("While I believe today's order in this docket and EL14-7-000 appropriately relies on market fundamentals as a basis for finding the current tariff provisions no longer just and reasonable, the determination in these orders to accept ISO-NE's proposed administrative price is not supported by the record. While it may be a tough call, in the long-term the New England region would be better served by this Commission making a decision based on market fundamentals.").

[34] *See* Tariff Order at P 30.

control area.[35] For Import-Constrained Capacity Zones, such as the NEMA/Boston and Connecticut Zones,[36] the forward capacity auction concludes when either (i) the aggregate supply curve for the Import-Constrained Capacity Zone is equal to or less than the Local Sourcing Requirement ("LSR") for that Capacity Zone, or (ii) the Total System Capacity is equal to or less than the ICR.[37] The Capacity Clearing Price for the Import-Constrained Capacity Zone is set at the highest price at which either of these conditions is met.[38] For Export-Constrained Capacity Zones, such as the Maine Zone,[39] the forward capacity auction concludes when both the aggregate supply curve for the Export-Constrained Capacity Zone is equal to or below the Maximum Capacity Limit for the Zone and the Total System Capacity is equal to or less than the ICR.[40] The Capacity Clearing Price for the Export-Constrained Capacity Zone is set at the highest price at which both of these conditions are met.[41] For the Rest-of-Pool Capacity Zone, the forward capacity auction concludes when the Total System Capacity is equal to or less than the ICR.[42] The Capacity Clearing Price for the Rest-of-Pool Capacity Zone is set at the highest price at which Total System Capacity is less than or equal to the ICR.[43]

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35 ISO-NE Tariff § III.13.2.3.3 ("The auctioneer shall use the offers and bids for the round . . . to determine the aggregate supply curves for the New England Control Area and for each modeled Capacity Zone included in the round."). Currently, there are four capacity zones within the New England Control Area: the Maine Load Zone; the Connecticut Load Zone; the Northeastern Massachusetts Load Zone; and the Rest of Pool Capacity Zone. ISO-NE Tariff § III.12.4.

36 *See* Informational Filing for Qualification in the Forward Capacity Market at p. 4, Docket No. ER14-329-000 (Nov. 5, 2013).

37 ISO-NE Tariff § III.13.2.3.3(a).

38 *Id.*

39 *See* Informational Filing for Qualification in the Forward Capacity Market at p. 4.

40 ISO-NE Tariff § III.13.2.3.3(c).

41 *Id.*

42 ISO-NE Tariff § III.13.2.3.3(b).

43 *Id.*

This structure can produce different capacity prices for individual capacity zones. For example, in FCA 7, the Maine (Export-Constrained), Connecticut (Import Constrained) and Rest of Pool Capacity Zones cleared at the Capacity Clearing Price Floor of $3.15/kW-month.[44] In the NEMA/Boston Capacity Zone (Import Constrained), however, a new resource (Footprint Power) submitted an offer to withdraw from the auction at a price of $14.998/kW-month.[45] As a result, in FCA 7 new resources in NEMA/Boston were paid $14.99/kW-month and existing resources were paid $6.66/kW-month.

This structure may also result in Inadequate Supply or Insufficient Competition being declared in one capacity zone but not in all zones. For example, in an Import Constrained zone, such as the NEMA/Boston Capacity Zone, if at the FCA Starting Price the amount of capacity offered from existing resources is less than the LSR for that Capacity Zone and either (i) less than 300 MW of capacity is offered from new resources, (ii) the amount of capacity offered from new resources is less than twice the amount of new capacity required, or (iii) any Market Participant's capacity from a new resources is pivotal,[46] the Insufficient Competition rule would be invoked for that Capacity Zone.[47] New entrants in the relevant Import Constrained Capacity Zone would be paid the Capacity Clearing Price (*i.e.,* the price at which they withdrew from the auction), and existing resources in that Capacity Zone would be paid the lower of the Capacity

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44 *See* Forward Capacity Auction Results Filing at p. 2, Docket No. ER13-992-000 (Feb. 26, 2013).

45 *Id.* at p. 5. Without the capacity from Footprint Power, the NEMA/Boston Capacity Zone would not have met its Local Sourcing Requirement. Consistent with the ISO-NE Tariff, ISO-NE Tariff § III.13.2.3.3(a), the auction closed for the NEMA/Boston Capacity Zone when Footprint Power submitted its offer to withdraw from the auction. *See* Forward Capacity Auction Results Filing at p. 5.

46 A Market Participant's capacity is considered pivotal if, at the FCA Starting Price, some of the capacity is required to satisfy the LSR.

47 ISO-NE Tariff § III.13.2.8.2.

Clearing Price or the administratively-determined price.[48] The auction would continue to run for the other Capacity Zones where the Insufficient Competition rule was not triggered.

Likewise, if at the FCA Starting Price the amount of capacity offered in an Import Constrained Capacity Zone through New Capacity Offers is less than the amount of New Capacity Required in that Capacity Zone, the Inadequate Supply rule would be triggered for that Capacity Zone.[49] New entrants would receive the FCA Starting Price and existing resources would receive the administratively-determined price.[50] The auction would continue for the other Capacity Zones where the Inadequate Supply rule is not invoked, as Inadequate Supply in one or more Import Constrained Capacity Zones does not affect Capacity Zones having adequate supply.[51]

The Tariff Order found that the current administrative pricing rules are unjust and unreasonable and that the sloped demand curve should eliminate the need for the administrative pricing rules beginning in FCA 9. The Tariff Order did not provide for a phased implementation of the sloped demand curve. Accordingly, NEPGA respectfully requests that the Commission clarify that the Tariff Order requires ISO-NE to implement fully the sloped demand curve for FCA 9, *i.e.*, that the remedy prescribed for FCA 9 be in place fully for FCA 9.

However, in the event that good cause exists to excuse ISO-NE from its obligations under the Tariff Order, the Commission should clarify that the $7.025/kW-month authorized for use in FCA 8 only may not be carried forward into FCA 9 for any purpose, and that if an administrative

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48 *Id.*

49 ISO-NE Tariff § III.13.2.8.1.1.

50 ISO-NE Tariff § III.13.2.8.1.1(a).

51 ISO-NE Tariff § III.13.2.8.1.1(c).

price mechanism is necessary for FCA 9 that such mechanism be based on the pool-wide cost of new entry values that are used to develop the pool-wide sloped demand curve, as adjusted to account for locational factors. As noted above, the $7.025/kW-month value approved for use in FCA 8 does not represent a credible measure of the actual cost of new entry and should not displace more accurate analyses of the cost of a new resource.

C. The Commission Should Grant Rehearing And Require ISO-NE To Eliminate The Zero Bid Requirement For Capacity That Is Subject To Multi-Year Price Protection.

When capacity offered by a new entrant clears in excess of the amount needed to meet the applicable capacity requirement, the capacity supplier may elect to receive the capacity clearing price paid in the initial auction for up to four successive capacity commitment periods, and thereby be shielded from the price depression that may result from the introduction of excess capacity into the market. In such circumstances, the ISO-NE Tariff requires the capacity supplier to offer its capacity at a zero-price bid, *i.e,* as a "price-taker." As explained in NEPGA's Complaint, the zero bid requirement acts to suppress market prices and exacerbates price discrimination between existing resources and new entrants.[52] In its Complaint, NEPGA argued that the current market rules are unjust and unreasonable and that the Commission should require capacity suppliers that elect the multi-year price protection to offer their capacity at a price that is no less than the clearing price to be paid to the supplier or the applicable benchmark price for new entry.

In the Complaint Order, the Commission stated that NEPGA had failed to show that the zero bid requirement was unjust and unreasonable or unduly discriminatory.[53] In so holding, the

[52] Complaint at pp. 24-34; Schnitzer Testimony at pp. 17-24.

[53] Complaint Order at P 56.

Commission appears to have relied upon arguments that mischaracterize NEPGA's Complaint, misstate aspects of the current ISO-NE market rules, and improperly distinguish relevant experience and precedent from ISO-NE and other regional markets. Accordingly, the Commission should grant rehearing and should conclude that the zero bid requirement is unjust and unreasonable and unduly discriminatory and that the remedy recommended by NEPGA and which is currently in place in other markets is just and reasonable and should be adopted for ISO-NE.

1. The Commission mistakenly failed to account for the link between the applicable Capacity Supply Obligation and the price suppression resulting from zero-price bids.

In the Complaint Order, the Commission stated that NEPGA had failed to show that zero-price bids suppress market prices because it had not shown a link between the amount of capacity carried forward from one auction to the next and the amount of excess capacity that may exist during the multi-year price guarantee period in which a new capacity supplier receives the initial clearing price, as escalated.[54] This reasoning misses the point. The "link" that is the basis for the price suppression in subsequent auctions is the link between the zero bid requirement and the Capacity Supply Obligation. This component of the current ISO-NE market rules suppresses market prices and is unjust and unreasonable. The Commission should grant rehearing and should require ISO-NE to eliminate the requirement that capacity suppliers offer their capacity as price-takers.

[54] *Id.* at P 57.

When a "lumpy" resource clears in a capacity auction, it is awarded a Capacity Supply Obligation that is a fixed quantity.[55] In subsequent auctions a capacity supplier that elects the multi-year price protection offers the full amount of its Capacity Supply Obligation at a zero-price bid. The link between the amount of the Capacity Supply Obligation set by the initial auction and the zero-bid requirement is clear and certain and is not affected by the amount of capacity associated with that resource that is considered to be "excess" in subsequent auctions. For example, if a region requires 150 MW of capacity, but clears a 650 MW resource in the FCA and the resource elects multi-year pricing, the resource's Capacity Supply Obligation for the Capacity Commitment Period is 650 MW and all 650 MW are offered into subsequent auctions at $0/kW-month.

As a result, the price suppression is comparable in each subsequent auction due to the requirement that the capacity resources offer the quantity of capacity defined by its Capacity Supply Obligation at $0. The zero-price bid requirement suppresses capacity prices and results in discriminatory pricing.[56] When capacity resources are offered as price-takers, the zero-price bids shift the demand curve to the right, suppressing the eventual clearing price and displacing other non-zero-price offers. The following graph, taken from Mr. Schnitzer's initial testimony, illustrates this effect:

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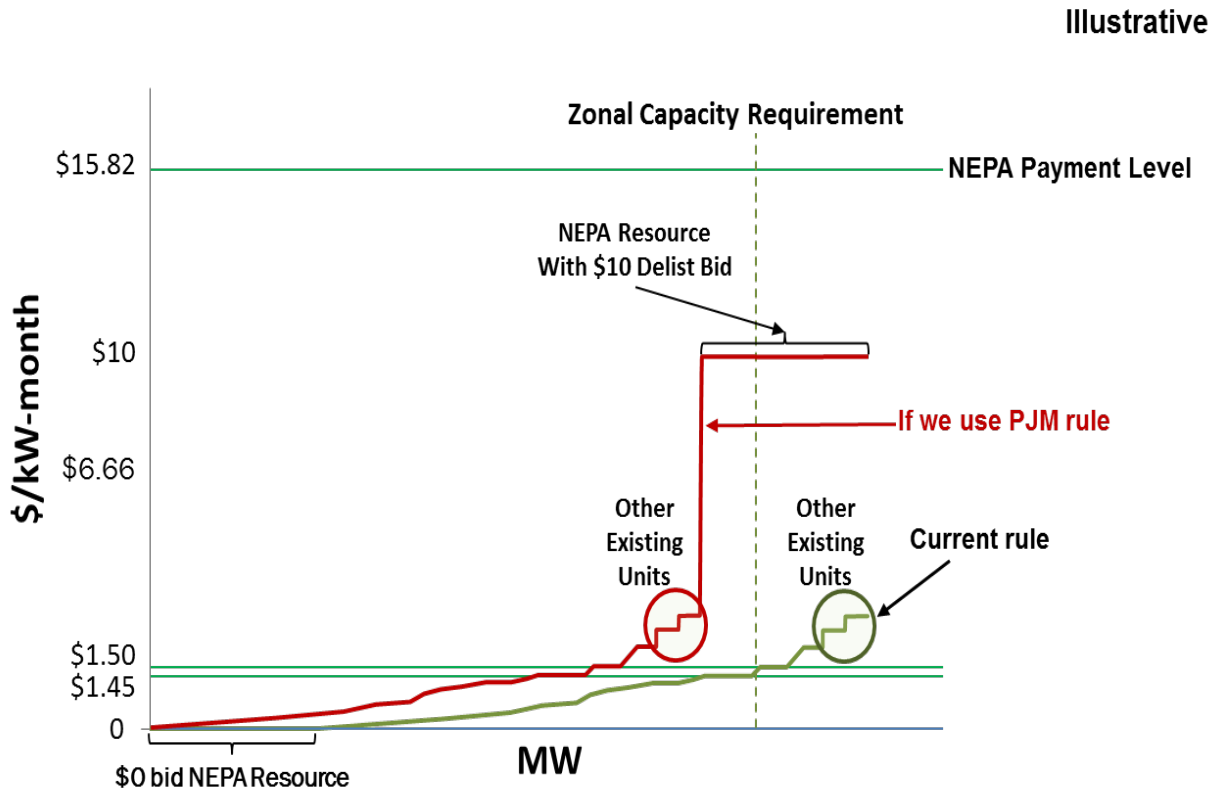
[55] A Capacity Supply Obligation is an obligation to provide capacity from a resource, or a portion thereof, that is acquired through a Forward Capacity Auction, a reconfiguration auction, or a Capacity Supply Obligation Bilateral. ISO-NE Tariff § I.2.2. The amount of the Capacity Supply Obligation is set by the auction and that quantity remains fixed for the term of the Capacity Commitment Period. The Capacity Commitment Period is the one-year period from June 1 through May 31 for which Capacity Supply Obligations are assumed and payments are made in the Forward Capacity Market. ISO-NE Tariff § I.2.2. A Generating Capacity Resource having a Capacity Supply Obligation must be offered into both the Day-Ahead Energy Market and Real-Time Energy Market at a MW amount equal to or greater than its Capacity Supply Obligation for the duration of the Capacity Commitment Period whenever the resource is physically available. ISO-NE Tariff § III.13.6.1.1.1.

[56] Complaint at pp. 24-34; Schnitzer Testimony at pp. 15-30.



Further, the zero-price bid requirement perpetuates detrimental price discrimination between new and existing resources. While the ability to elect a multi-year price guarantee shields new capacity resources from the price suppression resulting from new entry, there are no comparable protections for existing resources, which are doubly impacted, first by the increase in supply from the new entrant and further by the price suppression that results from the new capacity being offered at $0. As a result, there is no assurance that capacity prices for incumbents will ever approach new entry price levels, even when new entry is required.[57] This is the case because even if retirements or load growth create a continuing need for new entry, existing generation does not receive the capacity clearing price paid to new entrants but is instead relegated to prices set under flawed tariff rules that by design institutionalize a two-tier

[57] Schnitzer Testimony at p. 22.

market price structure under which prices paid to existing resources do not begin to approach competitive levels or the prices actually paid to new entrants.

2. The Commission mistakenly concluded that price suppression resulting from zero-price bids is only a concern in capacity markets that utilize a sloped demand curve.

The Commission has previously recognized the price suppressive effects of zero-price bids and has acted in a variety of settings to require sellers to submit bids that reflect the actual cost of the resource. In its Complaint, NEPGA cited this precedent to support its showing that the zero-price bids suppressed market prices and led to undue discrimination between the prices paid to existing resources and the prices paid to new entrants.[58] In the Complaint Order, however, the Commission dismisses NEPGA's arguments on grounds that precedent concerning the PJM market is distinguishable because PJM's market differs from ISO-NE's most notably in its use of a sloped demand curve in its forward capacity market.[59] In this regard, the Commission mistakenly links the well-established price distortion associated with below-market or zero-price bids to a specific market design feature of the PJM market, when the price distortion and price suppression associated with such bids has been recognized in ISO-NE and other markets beyond PJM. Accordingly, the Commission should grant rehearing and should require ISO-NE to eliminate the zero-bid requirement and implement the bidding protocols requested by NEPGA in its Complaint.

First, the suggestion that the price suppression associated with zero-price bids – and the need for the remedy sought by NEPGA – is restricted to markets with sloped demand curves is simply wrong. The Complaint Order fails to explain how these differences prevent zero-price

[58] Complaint at pp. 19-34, Schnitzer Testimony at pp. 15-30.

[59] Complaint Order at P 58.

bids from suppressing market prices in New England or why these differences render the experience and precedent from PJM and other markets irrelevant to the same issues with regard to FCM. As Commissioner Clark noted in his partial dissent to the Complaint Order, "the Commission has determined in multiple markets that [zero-price] bidding practices undermine the design and function of the capacity market."[60]

A review of these orders demonstrates the wide range of circumstances in which zero-price bids have been held to be unjust and unreasonable because of their distorting effects on market prices. One need look no further than prior decisions concerning ISO-NE's FCM to find clear guidance regarding the price suppression associated with artificially low or zero-price capacity bids. In 2011, the Commission reviewed and rejected ISO-NE's Alternative Capacity Price Rule, an aspect of which was subsequently reinstated as the Capacity Carry-Forward Rule, concluding that the ISO-NE Tariff provisions at issue were unjust and unreasonable because they did not result in competitive market proxy prices that reflected the outcome of a fully competitive market environment.[61] In that instance, the Commission directed ISO-NE to address the price suppression resulting from low capacity offer prices attributable to uneconomic entry by establishing benchmark prices that reflect the cost of new entry and using such benchmarks to set offer floors for FCAs.[62]

Further, in *PJM Interconnection, L.L.C.*, the Commission similarly recognized that zero price capacity supply offers suppress market prices and create undue price discrimination

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60 Complaint Order at Clark dissent.

61 *ISO New England, Inc.*, 135 FERC ¶ 61,029 at PP 60, 62.

62 *Id.* at P 169.

between new and existing resources. [63] In this instance, the Commission considered arguments that PJM capacity suppliers that had elected new entry pricing should be required to offer their capacity into subsequent auctions at a $0 bid in order to guarantee that the capacity would clear. The Commission found that such bidding practices would suppress capacity prices and would create unjustified price discrimination between new and existing resources. [64]

Moreover, the finding that $0 supply offers suppress market prices is not restricted to capacity markets. In a series of related cases, the Commission addressed circumstances in which a market participant's market-based rate tariff was suspended and it was required to submit proxy bids. The market participant was initially required to submit energy offers at a $0 price, but CAISO, other parties, and market monitors each argued that $0 energy bids would displace economic capacity and would suppress market prices and thereby adversely affect other market participants.[65] The Commission agreed with these concerns and directed that the suppliers' bids be cost-based.[66]

What these decisions show is that the price distortion resulting from zero-price bids is a function of the zero-price bid rather than other design features of the relevant market. Regardless of whether the applicable market reflects a vertical demand curve, a sloped demand

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63 *PJM Interconnection, L.L.C.*, 128 FERC ¶ 61,157 (2009).

64 *Id.* at P 112. In that order, the Commission explained:

> The original purpose of including the bidding limitations was to ensure that a new entrant in a small LDA will not reduce prices to the existing resources by submitting a $0 bid in Years 2 and 3, knowing that it is guaranteed to be paid its first year bid price no matter what it bids. We continue to find that PJM and NRG have not explained why a bid floor is not necessary to protect against such bidding behavior and the resulting discriminatory pricing. That is, the new resource would receive its first-year price for all of the years in which it receives NEPA treatment, while existing resources in the LDA would receive a lower price (reflecting the LDA's surplus of capacity).

65 *California Independent System Operator Corp.*, 142 FERC ¶ 61,191 at PP 15, 28 (2013); *J.P. Morgan Ventures Energy Corp*., 143 FERC ¶ 61,118 at PP 25, 28 (2013).

66 *California Independent System Operator Corp.*, 142 FERC ¶ 61,191 at P 28.

curve, or any other aspect of market design, the simple, inescapable fact is that when energy or capacity is offered into a bid-based market at $0 that offer will displace other bids and will likely suppress the resulting market-clearing price. As a result, market participants, market monitors, and the Commission itself have concluded that zero-price bids suppress prices and the Commission has required such bidding practices to be revised. Moreover, even if the Commission was correct that price suppression associated with zero-price bids is indeed restricted to markets with sloped demand curves, the Commission erred by failing to require that ISO-NE eliminate the current zero-price bid requirement at the same time that it implements a sloped demand curve. If markets with a sloped demand curve do not allow zero-price bids, then the Commission should not allow deviation from that market design requirement when it directs the adoption of a sloped demand curve in ISO-NE. The Commission should grant rehearing and should require ISO-NE to eliminate the use of zero-price bids for capacity subject to multi-year price protection.

IV. CONCLUSION

WHEREFORE, for the reasons stated herein, NEPGA respectfully requests that the Commission grant rehearing of the Complaint Order and the Tariff Order as set out more fully in the body of this request.

Respectfully submitted,

Bruce F. Anderson
Bruce F. Anderson
Director of Market & Regulatory Affairs
New England Power Generators
Association, Inc.
141 Tremont St.
Boston, MA 02111
(617) 902-2354
banderson@nepga.org

Dan Dolan
President
New England Power Generators
Association, Inc.
141 Tremont St.
Boston, MA 02111
(617) 516-5355
ddolan@nepga.org

James C. Beh
Jonathan F. Christian
Marvin A. Liang
JONES DAY
51 Louisiana Avenue, N.W.
Washington, D.C. 20001
(202) 879-3939
jcbeh@jonesday.com
jchristian@jonesday.com

Counsel for the New England Power Generators Association, Inc.

February 24, 2014

CERTIFICATE OF SERVICE

I hereby certify that I have this the 24th day of February, 2014, caused a copy of the foregoing document to be served on all parties to these proceedings, as listed on the official service list compiled by the Commission Secretary for these proceedings.

Jonathan F. Christian
Jonathan F. Christian

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