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October 10, 2012

SENT VIA ELECTRONIC FILING
Kimberly D. Bose, Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Room 1-A209
Washington, D.C. 20426

Re: Docket No. EL11-50-000 - Astoria Generating Company L.P. and TC Ravenswood, LLC v. New York Independent System Operator, Inc.

Dear Secretary Bose:

Attached, for filing, is the Request for Rehearing of the New York State Public Service Commission in the above-entitled proceeding. The parties have also been provided with a copy of this filing, as indicated in the attached Certificate of Service. Should you have any questions, please feel free to contact me at (518) 473-8178.

Very truly yours,

David G. Drexler
Assistant Counsel

Attachment
cc: Service List

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Astoria Generating Company L.P. and TC Ravenswood, LLC	)	
	)	
v.	)	Docket No. EL11-50-000
	)	
New York Independent System Operator, Inc.	)	

REQUEST FOR REHEARING
OF THE NEW YORK STATE
PUBLIC SERVICE COMMISSION

INTRODUCTION

On September 10, 2012, the Federal Energy Regulatory Commission (FERC or Commission) issued an order granting in part, and denying in part, a Complaint filed by Astoria Generating Company L.P. and TC Ravenswood, LLC (collectively, Complainants) against the New York Independent System Operator, Inc. (NYISO) (September 10 Order).[1] The Complainants alleged that the NYISO improperly exempted the new 575 MW generating facility owned by Astoria Energy II LLC (AE II), and potentially other new facilities, including the 512 MW generating facility owned by Bayonne Energy Center, LLC (BEC), from the mitigation

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[1] Docket No. EL11-50-000, Astoria Generating Company L.P. and TC Ravenswood, LLC v. New York Independent System Operator Inc., Order on Complaint, 140 FERC ¶61,189 (issued September 10, 2012).

measures applicable to new entrants in the New York City (NYC) Installed Capacity (ICAP) market.

The September 10 Order directed the NYISO to recalculate its exemption determinations for AE II and BEC using updated data on prices, revenues, and costs as of October 2010. The New York State Public Service Commission (NYPSC) hereby requests rehearing of the Commission's September 10 Order pursuant to Rule 713 of Commission's Rules of Practice and Procedure.[2]

SUMMARY

The NYPSC is concerned that the September 10 Order represents a fundamental and unexplained departure from prior Commission precedent that will: 1) significantly increase regulatory uncertainty and ultimately deter market entry in one of the most constrained markets in the nation; 2) hinder the State's ability to pursue public policy (e.g., environmental) objectives in a cost-effective manner; and 3) harm consumers.

Until the September 10 Order, the Commission indicated that "[i]t is reasonable for NYISO to provide an exemption test before a supplier begins construction of a new resource, *as*

[2] 18 C.F.R. §385.713. The September 10 Order accepted the NYPSC's Motion to Intervene, which was filed on August 3, 2011.

NYISO's tariff current[ly] provides, and to apply such a test to all new entrants."[3] As the Commission explained,

> [a]n entity whose resource is forecast to be economic at the time its construction begins is not attempting to artificially depress market prices through uneconomic entry. Thus, it would not be reasonable to impose an offer floor on such a resource that prevented it from clearing in the capacity auction if market conditions unexpectedly worsened by the time that construction is completed.[4]

The NYISO's decision to perform an exemption determination for AE II in October 2010, based on information available at the time the decision to proceed with construction was made in July 2008, was rational, reasonable, and consistent with the Commission's precedent.[5] The Commission's September 10 Order departs from this precedent by requiring the NYISO to perform an exemption determination based on information only available *after* the decision was made to proceed with construction in July 2008, and *after* AE II commenced construction in May 2009. Moreover, the Commission required that the NYISO use current information available as of 2010, when market conditions had unexpectedly worsened from 2008. The September 10 Order is at odds with the Commission's precedent, and should be reversed.

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[3] Docket No. ER10-3043-000, NYISO, Order on Proposed Revisions to In-City Buyer-Side Mitigation Measures (issued November 26, 2010) ¶71 (emphasis added).

[4] Id.

[5] Actual construction of AE II commenced in May 2009.

The Commission's error is compounded by the incorrect determinations it made with respect to individual cost components for AE II's Unit net CONE determination. In particular, the Commission concluded that the tariff provision referring to "embedded costs" required the inclusion of AE II's "sunk costs." This conclusion is contrary to the evidence provided to the Commission regarding the economic rationale underlying "buyer-side" mitigation measures.

Moreover, the Commission should not have ignored AE II's actual financing costs. The Commission's decision was based on the erroneous finding that AE II's power purchase agreement with the New York Power Authority (NYPA) in 2008 was the result of a "discriminatory" process. This conclusion was unsupported by the evidence and was based on an incorrect legal standard. The correct legal standard under the Federal Power Act is whether the action was "*unduly discriminatory or preferential*."[6] The Commission cannot conclude that the competitive Request-for-Proposals process and resulting agreement were unduly discriminatory or preferential where NYPA sought to satisfy additional capacity needs and opened its process to *all* new capacity, including existing suppliers with repowered projects that would result in a net increase in capacity.

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[6] 16 U.S.C. §824e(a) (emphasis added).

The Commission has previously indicated that prospective new entrants should be given greater regulatory certainty in going forward with their projects once an exemption has been granted. The Commission's decision in this case is inconsistent with its prior recognition of the need to provide greater certainty for developers. Moreover, because the exemptions were granted during the period when the buyer market power mitigation mechanism was being developed and revised for the first time, and because the NYISO's approach was consistent with the Commission's precedents, the Commission should uphold as rational the NYISO's decisions to exempt certain generators from the mandatory bid floors.

Finally, the NYPSC requests that FERC defer the implementation of any compliance filing made by NYISO, which would reverse the previously-granted exemptions, until FERC has heard and decided the petitions for rehearing of FERC's September 10, 2012 Order. A failure to defer implementation could cause irreparable injury by forcing ratepayers to pay hundreds of millions in unjust and unreasonable increased ICAP costs. Refunds would not likely be a viable option to

compensate ratepayers in the event the Commission addresses the reversible errors noted herein.[7]

STATEMENT OF ISSUES

1) Whether FERC's decision reversing the NYISO's Unit Exemption determination for AE II, and directing the NYISO to disregard information relied upon in 2008 when deciding whether to develop AE II as a capacity resource, was arbitrary, capricious, and inconsistent with reasoned decision-making.[8]

2) Whether FERC's decision directing that the Unit Exemption determination include sunk costs, while such costs are excluded by developers in deciding whether to develop a facility as a capacity resource, was arbitrary, capricious, and inconsistent with reasoned decision-making.[9]

3) Whether FERC's decision finding that the power purchase agreement between AE II and NYPA was "discriminatory" and "irregular or anomalous," and directing the use of a proxy

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[7] The September 10 Order clearly articulated that "it is preferable not to re-run. . .past auctions, in order to provide greater certainty for market participants, and to avoid the need to resolve these complex issues." September 10 Order, ¶141.

[8] In reviewing agency determinations, courts shall "hold unlawful and set aside agency action, findings, and conclusions found to be...arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;...in excess of statutory jurisdiction, authority, or limitations, or short of statutory right...; or, unsupported by substantial evidence." 5 U.S.C. §706; Federal Communications Commission v. FOX Televisions Stations Inc., 129 S. Ct. 1800, 1811 (2009)(finding that an agency is required to provide a reasoned explanation for "disregarding facts and circumstances that underlay or were engendered by [a] prior policy"); Greater Boston Television Corp. v. Federal Communications Commission, 444 F.2d 841, 852 (D.C. Cir. 1970)(determining that an agency must engage in reasoned decision-making when changing course from its prior precedents), cert. denied, 403 U.S. 923 (1971).

[9] Id.

cost of capital for AE II, was arbitrary, capricious, and inconsistent with reasoned decision-making.[10]

4) Whether FERC's decision requiring the NYISO to re-determine the exemption determinations, which developers have relied upon in entering the capacity market, conflicts with prior FERC precedent holding that "taking away a previously authorized exemption is not reasonable," and is otherwise arbitrary, capricious, and inconsistent with reasoned decision-making.[11]

DISCUSSION

I. The Commission erred in reversing the NYISO's Unit Exemption determination for AE II, and directing the NYISO to disregard information relied upon in 2008 when deciding whether to develop AE II as a capacity resource

Notwithstanding the NYISO tariff provision indicating that the applicability of an exemption shall be conveyed "as soon as practicable after completion of the relevant Project Cost Allocation," the Commission properly conceded that applying the tariff in this case is not reasonable since "it took an inordinately long time for NYISO to complete the final project cost allocation for the 2009 and 2010 class years."[12] The Commission has also indicated that "[i]t is reasonable for NYISO to provide an exemption test before a supplier begins construction of a new resource, *as NYISO's tariff current[ly]*

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[10] Id.

[11] Id.

[12] September 10 Order, ¶64.

provides, and to apply such a test to all new entrants."[13] Due to the disconnect between the developer's construction schedule and the NYISO's interconnection process, a unique factual element to this case, the Commission properly waived the tariff to allow the exemption determinations to occur prior to the announcement of the final project cost allocations, which were finally resolved on November 30, 2011.[14]

The Commission, however, erred in finding that the exemption determinations should have been made for AE II based on the information available as of October 2010, rather than on information that the investors presumptively relied on in 2008. The Commission offered no explanation, let alone a reasoned one, as to why an October 2010 projection should have been used. It appears that the Commission crafted a new policy requiring that an exemption determination should "at least be provided before the unit enters the capacity market, not after."[15]

Requiring an exemption determination for AE II based on information projected as of October 2010 is inconsistent with the purpose underlying the mitigation test and FERC's own precedent indicating that the determination should be based on

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[13] ER10-3043-000, NYISO, Order on Proposed Revisions to In-City Buyer-Side Mitigation Measures (issued November 26, 2010), ¶71 (emphasis added).

[14] NYISO, Class Year 2010 - Notice of Completion of the Decision/Settlement Process (November 30, 2011).

[15] Id.

the market conditions reasonably assumed by the investor at the time of the investment commitment.

The NYISO's decision to utilize 2008 information in performing the exemption determination, which was the time of the investment decision, was consistent with the Commission's rationale underlying the buyer-side mitigation measures. According to the Commission, "[a]n entity whose resource is forecast to be economic at the time its construction begins is not attempting to artificially depress market prices through uneconomic entry."[16] The NYISO's determination to apply 2008 data was not unreasonable because its inquiry properly focused on "whether a rational investor could reasonably expect a project to be economic based on information available at the time the investor committed to going forward."[17]

In the case of AE II, the commitment to "going forward," which was based on NYPA's approval of a 20-year contract with AE II, arose long before October 2010. The decision to proceed with construction occurred in July 2008, following NYPA's approval of a 20-year contract with AE II.

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[16] Docket No. ER10-3043, NYISO, Order on Proposed Revisions to In-City Buyer-Side Mitigation Measures (issued November 26, 2010), ¶71.

[17] September 10 Order, ¶72.

Actual construction began in May 2009.[18] The NYISO's reliance on 2008 information as the going-forward date for construction was rational, reasonable, and consistent with the purpose of the mitigation test and FERC precedent. The Commission's September 10 Order provides no basis for substituting a reference date of October 2010. Indeed, it is clear that conditions in October 2010 were not reflective of investment conditions at the time the decision was made to proceed with construction, over two years earlier. In addition, the October 2010 reference date is more than one year after construction began. Under these circumstances, the use of an October 2010 reference date is arbitrary, capricious, and inconsistent with reasoned decision-making.

The Commission should also recognize the overriding need to provide regulatory certainty to investors and to potential future entrants. FERC should not subject new entrants to the possibility of being evaluated against data that they could not have anticipated at the time they made their decision to invest. The NYISO provided exemption determinations to both AE II and BEC, based on a rational and logical interpretation of

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[18] FERC's September 10 Order does not dispute these facts but injects its own business judgment that the decision to proceed with the project should have been reversed. See, September 10 Order, fn 87. Injecting prudence issues into the mitigation test is fraught with difficulties and introduces the kind of contentious issues that FERC urged the NYISO to eschew in other portions of the order. See, September 10 Order, ¶84.

the Commission's guidance on this fundamental point. As the Commission correctly observed, "taking away a previously-authorized exemption[] is not reasonable."[19] However, that is precisely the outcome the Commission will likely produce by requiring the NYISO to re-apply the exemption test with information available as of October 2010.

II. The Commission erred in directing that the Unit Exemption determination include "sunk" costs because such costs are excluded by developers in deciding whether to develop a facility as a capacity resource

While the NYISO determined that the costs associated with AE II paying for a portion of the facilities it shares with AE I were "sunk," and therefore would be excluded by rational investors in evaluating whether a proposed project will be profitable, the Commission concluded that it was improper for NYISO to exclude these costs from the calculation of AE II's Unit net CONE.[20] The Commission based its conclusion on the definition of Unit net CONE as the "localized levelized embedded costs of a specific [ICAP] supplier, including interconnection costs...."[21] As the Commission rationalized its decision, "the common meaning of the term 'embedded costs' includes all costs

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[19] Docket Nos. ER10-3043-002 et al., NYISO, Order on rehearing and Clarification (issued August 2, 2011), ¶27.

[20] September 10 Order, ¶121. Pursuant to an agreement, the developers of AE II paid the developers of Astoria I for a portion of the costs of the shared facilities.

[21] Id.

that have been incurred in the past, whether or not the associated assets have any opportunity costs or market value" (i.e., whether or not they are sunk costs).[22]

The September 10 Order appears to ignore the intent and purpose behind applying a mitigation analysis to a new entrant, which is to prevent uneconomic entry. Accordingly, such analysis should evaluate whether a new entrant's project is profitable or not. The NYISO, as supported by its external Market Monitor, undertook this type of rational, reasoned, and supported economic approach in determining that a rational investor would exclude sunk costs, including shared facility costs paid by AE II, in analyzing the profitability of a proposed project.

The Commission inappropriately relied on a narrow interpretation of standard definitions of "embedded costs" without considering the purpose of the tariff. Even the definition referred to in footnote 153 of the September 10 Order indicates that recorded costs are used by managers, investors, regulators and economists in carrying out their respective jobs. The NYISO used the recorded costs in a rational and reasonable manner consistent with economic theory. FERC's unquestioning insistence that all recorded costs be included in the test ignores the purpose of the mitigation analysis. AE II's payment

[22] Id.

to its affiliated generator had no bearing on its decision to go forward in the capacity market. Therefore, the Commission erred in overturning the NYISO and determining that shared facilities costs of AE II were embedded costs that should be included in the mitigation determination.

Alternatively, even if these facility costs have to be included as "embedded costs" that must be included as part of Unit net CONE, the Commission erred in not waiving the tariff to exclude such costs in this instance. As a result, the Commission's September 10 Order will inappropriately act as a deterrent to new investment and entry into the NYC ICAP market that may otherwise be economic/profitable, such as AE II and BEC.

III. The Commission erred in finding that the power purchase agreement between AE II and NYPA was "discriminatory" and "irregular or anomalous," and directing the use of a proxy cost of capital for AE II

The primary purpose for NYPA's RFP, which culminated in a power purchase agreement with AE II, was to procure additional needed ICAP resources within NYCA Zone J. Nevertheless, the Commission concluded that the contracting process was "discriminatory" because it was limited to new resources.[23] Based on this conclusion, the Commission

[23] September 10 Order, ¶135. The NYISO's 2007 CRP identified a need for an additional 1000 MW in NYC and to defer the closing of NYPA's old Poletti until 2010. The NYISO's 2007 RNA found reliability violations starting in 2012.

characterized the power purchase agreement as "irregular or anomalous" and directed the NYISO to use the proxy cost of capital in redoing an exemption determination for AE II.

In reaching its conclusion, the Commission applied an erroneous legal standard and thus, committed an error of law. The Federal Power Act precludes "*unduly* discriminatory or preferential" contracts, not those that are merely "discriminatory."[24] Here the distinction between new and existing resources was not "unduly discriminatory" but perfectly proper. Faced with a net capacity loss in Zone J due to the retirement of its old Poletti generating station, NYPA looked to replace the lost capacity through new resources. By definition, existing resources could not address the need for capacity to replace the capacity retired in Zone J. Moreover, existing generation was allowed to participate in the RFP process in so far as it could offer a net increase in its capacity. Therefore, it is incorrect to conclude that under the circumstances this process was either discriminatory or unduly discriminatory. For the same reasons, it is incorrect to characterize the "lower financing costs associated with the power purchase agreement... [as] 'irregular or anomalous' cost advantages that are 'not in the ordinary course of business.'"[25]

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[24] 16 U.S.C. §824e(a) (emphasis added).

[25] September 10 Order, ¶135.

In characterizing the use of a Power Purchase Agreement in connection with what is in effect a repowering project, the Commission introduces significant regulatory uncertainty into the process for bringing important resources into the electric markets. For example, because market price signals do not adequately reflect environmental externalities, the goal of improving NYC's air quality could not effectively be accomplished by relying solely on existing, dirtier plants competing through the market. Under the Commission's decision, the use of Power Purchase Agreements to accomplish these laudable public policies would be considered to be "discriminatory" and "irregular or anomalous." The Commission's decision thus would have far reaching adverse consequences for the ability of the State to address resource adequacy requirements while pursuing legitimate public policies in a cost-effective manner. The successful achievement of public policies may depend on the use of targeted procurements, and the Commission should not, without any evidence, characterize such efforts as discriminatory, irregular, or anomalous.

The ancillary benefits of improving air quality via reduced generator emissions was a key factor in the retirement of the 885 MW Poletti generating facility and the procurement of AE II as a replacement. To the extent new generation resources are pursued by the State for public policy purposes, we continue

to believe that ratepayers should be allowed to count the capacity associated with those resources toward their Load-Serving Entities' ICAP requirements. By preventing these new resources from contributing toward ICAP requirements, which is the result of applying "buyer-side" mitigation measures and prohibiting Load-Serving Entities from "self-supplying," ratepayers will be required to go through the market to procure the same amount of capacity from an incumbent generator. This is an unreasonable outcome that requires the Commission's attention. If the Commission's objective is to favor incumbent generators' financial solvency at the expense of ratepayers and environmental goals, then the Commission should clearly articulate that goal. If the Commission's goal, however, is to prevent new entry from improperly suppressing market prices for any capacity required to be procured from the market beyond that which a Load-Serving Entity has already procured through self-supply or other means, then we support and ask that the Commission address the reforms needed to accomplish that goal.[26]

[26] We note that PJM includes a "Fixed Resource Requirement" alternative for Load-Serving entities to satisfy their capacity obligations outside of the market, and that a variant of that approach may be suitable for the NYISO.

IV. The Commission erred in requiring the NYISO to re-determine the exemption determinations, thereby creating a significant barrier to entry

Under the unique circumstances presented in this case, the Commission should uphold as rational the NYISO's decision to exempt AE II from the bid floor. The Commission has previously indicated that "[i]t is reasonable to permit a reevaluation of an offer floor exemption determination when the originally-projected economics of the project change upon entry into the capacity market and the project is then expected to be economic upon such entry." Most importantly, however, the Commission concluded that "[t]he reverse, i.e., the scenario addressed by both orders of a re-determination resulting in taking away a previously-authorized exemption, is not reasonable." In affording a developer the certainty that a NYISO-determined exemption will not be taken away at a later date, the Commission provided market certainty that developers can rely upon the NYISO's determination in going forward with their projects.

The Commission's decision in this case is inconsistent with its prior recognition of the need to provide certainty for developers. In the cases of AE II and BEC, the NYISO reasonably interpreted its tariff and the Commission's guidance on the proper implementation of the market mitigation rules and determined that these suppliers should be exempt. The

Commission has provided no basis for concluding, against it own prior findings, that this exemption should be overturned.

Further, the two suppliers at issue in this case had the unfortunate circumstance of making their investment decisions at the same time the FERC and NYISO were, for the very first time, developing and revising the buyer market power mitigation mechanism. To now reverse the NYISO, change the rules of the road and penalize these new suppliers for a regulatory problem that was in no way their own doing is unjust and unreasonable. Because the exemptions were granted during this shakeout period, and because the NYISO's approach was consistent with the Commission's precedents, the Commission should uphold as rational the NYISO's decisions to exempt certain generators from the mandatory bid floors.

To rule otherwise undermines the goal of developing and fostering competitive markets in New York City. Stated another way, the competitiveness of markets depends heavily on the extent to which entry barriers are small and can be kept small over time. New York City is a very difficult market for new suppliers to enter, even without additional new entry barriers. Proper policy in the pursuit of competitive markets must involve the explicit recognition by the regulator of the unintended consequences of regulatory rules. In implementing its buyer market mitigation rules as the Commission has done in

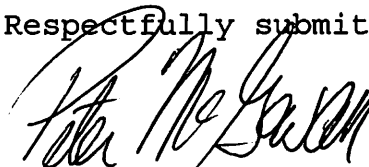
its September 10 Order, the FERC has created a new, very large entry barrier, namely regulatory uncertainty.

Turning to the specifics of this case, the Commission has signaled to future potential new entrants that a favorable decision encouraging entry from the NYISO may be reversed more than a year later, when this Commission substitutes its own judgments and calculations for the reasonable judgments and interpretations made by the market administrator - according to the Commission's own guidance. The FERC must rebalance the intended and unintended effects of its buyer market power mitigation rules, and, in doing so, explicitly give the largest weight to the imperative of keeping the barriers to new entry as low as possible. This imperative requires the Commission to reverse its order and to uphold the NYISO's determinations.

CONCLUSION

The NYPSC respectfully requests that the Commission grant the foregoing Request for Rehearing, defer implementation of the NYISO's compliance filing, and correct the identified errors in the September 10 Order noted herein.

Respectfully submitted,



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By: David G. Drexler
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Dated: October 10, 2012
Albany, New York

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated: Albany, New York
October 10, 2012

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