

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Joint Petition of Iberdrola, S.A., Energy East Corporation, RGS Energy Group, Inc., Green Acquisition Capital, Inc., New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation for Approval of the Acquisition of Energy East Corporation by Iberdrola, S.A.

Case 07-M-0906

**BRIEF ON EXCEPTIONS OF
INDEPENDENT POWER PRODUCERS OF NEW YORK, INC.**

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INTRODUCTION

In accordance with the Notice of Schedule for Filing Exceptions issued by the New York State Public Service Commission (“Commission”) on June 16, 2008 in the above-captioned proceeding, Independent Power Producers of New York, Inc. (“IPPNY”), hereby submits its Brief on Exceptions to the Commission on Administrative Law Judge (“ALJ”) Rafael Epstein’s Recommended Decision issued in this proceeding on June 16, 2008 (“RD”).¹ IPPNY is a not-for-profit trade association representing the independent power industry in New York State. Its members include more than 100 companies involved in the development, operation and ownership of electric generators and the marketing and sale of electric power in New York’s wholesale and retail markets, including the markets in the service territories of Joint Petitioners New York State Electric & Gas Corporation (“NYSEG”) and Rochester Gas and Electric Corporation (“RG&E”).

¹ Parenthetical references to the recommended Decision are preceded by the notation “RD”; parenthetical references to the transcript in this proceeding are preceded by the notation “Tr.”; references to the exhibits admitted into evidence during the hearings are preceded by the notation “Exh.”.

IPPNY accepts the RD's Overview and Summary as its statement of the case. IPPNY strongly supports the ALJ's recommendation that, if the Commission approves the acquisition of Energy East Corporation by Iberdrola, S.A. (the "Transaction"), Iberdrola must not be permitted to own any generation in its own service territories, and thus, NYSEG and RG&E must be required to divest all of their electric generating facilities to adequately address the vertical market power issues (RD at 1). However, IPPNY respectfully asserts that the ALJ has erred in proposing that the timing of the divestiture be established by a collaborative process at the conclusion of this proceeding (RD at 77). As discussed below, if the Commission approves the Transaction, it should require the Joint Petitioners to auction all of NYSEG's and RG&E's electric generating facilities to an unaffiliated third party within nine months of the Commission's ruling on the Transaction to ensure that such divestiture occurs without undue delay.

The ALJ also has erred in not rejecting Strategic Power Management's ("SPM") three alternative proposals for the divestiture of wind generation on procedural grounds (RD at 74). As discussed below, SPM's unsubstantiated proposals should be dismissed because they were raised for the first time in its reply brief and were, therefore, offered far too late to be considered as part of the record.

I. THE COMMISSION SHOULD REQUIRE THAT, AS A CONDITION OF TRANSACTION APPROVAL, NYSEG AND RG&E COMPLETE THE DIVESTITURE OF THEIR GENERATING FACILITIES TO UNAFFILIATED THIRD PARTIES WITHIN NINE MONTHS OF THE COMMISSION'S ORDER.

In the testimony of IPPNY's expert witness, Mr. Mark Younger, and in IPPNY's Initial Brief, IPPNY explained that a firm deadline was necessary with respect to the auction of NYSEG's and RG&E's generating facilities to ensure that these facilities would be divested

without delay.² IPPNY advocated that the Commission order the divestiture be consummated within nine months of its order on the Transaction.³ As summarized in the RD, the Consumer Protection Board (“CPB”) advocated that the Commission “allow enough time for design of the auction protocol to ensure that the sales generate the maximum potential proceeds and that artificial time limits do not give undue leverage to potential buyers” (RD at 77). In response to CPB’s and IPPNY’s different positions and Joint Petitioners’ proposal that a post-auction collaborative process be used to determine how the divestiture proceeds should be flowed through to customers, the ALJ stated:

The best solution may be to initiate the collaborative at the conclusion of this case, rather than after the auction as petitioners propose, so the parties will have an opportunity to return to the Commission with a proposed protocol and timetable that the parties have thoroughly considered instead of litigating the matter at the exceptions stage in this case (RD at 77).

IPPNY does not object to interested parties establishing the auction protocols through a collaborative process. The ALJ, however, has not offered any sound basis for why the Commission should not impose a firm deadline to complete such collaborative process and consummate the divestiture.

The RD does not address IPPNY’s concerns that, without a firm deadline established by the Commission in its order, Joint Petitioners may unduly delay the ultimate divestiture of NYSEG’s and RG&E’s generation. This is particularly true given RG&E’s very recent behavior with respect to one of these assets, its 257 MW coal-fired Russell Station. Notwithstanding the fact that RG&E committed to divest this plant in order to secure authority to go forward with its Rochester Transmission Project (“RTP”) -- a quid pro quo that the Commission approved -- RG&E subsequently unilaterally attempted to dodge its commitment by seeking to repower this

² Case 07-M-0906, *Initial Brief of Independent Power Producers of New York, Inc.*, p. 9-12.

³ *Id.* at 9.

facility. Thus, it is essential that the Commission impose a firm deadline on Joint Petitioners to divest NYSEG's and RG&E's generation so the company cannot again attempt to evade its commitments.

In contrast, as recognized by the Petitioners, there is no critical time frame for ascertaining how the proceeds of the auction should be allocated. In fact, it may be beneficial to first receive the auction results before determining how such proceeds should be allocated. Thus, the allocation process easily could proceed on a separate track. As Mr. Younger explained in his testimony, RG&E committed to divest its retired Russell Station after it completed the RTP.⁴ Notwithstanding this obligation, RG&E informed the Commission that it planned to repower the facility.⁵ While the requirement to divest Russell Station was clear, RG&E's actions in the face of this unambiguous directive demonstrate the need to impose explicit conditions on the Joint Petitioners to divest this and the other generating facilities in the NYSEG and RG&E service territories by a date certain.

As specifically noted in the Commission's order approving the construction of the RTP, RG&E expressly committed in an information request response to "follow an appropriate competitive auction process with a goal of the sale of the Russell Station site to a non-affiliated entity."⁶ This commitment is embodied in the Joint Proposal approved by the Commission in the

⁴ As established in the RTP Article VII Proceeding, RG&E is constructing the RTP to ensure adequate and reliable service to the Rochester area following the closing of Russell Station. Russell Station was scheduled to be retired in the second quarter of 2008 upon the completion of the RTP. Case 03-T-1385, *Rochester Gas and Electric Corporation*, Order Granting Certificate of Environmental Compatibility and Public Need (December 16, 2004) (hereinafter "Russell-RTP Order").

⁵ Cases 03-E-0765 *et al.*, *Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Rochester Gas and Electric Corporation for Electric Service*, RG&E Filing (February 1, 2008), p. 3.

⁶ Russell-RTP Order, p. 5.

Russell-RTP Order, with the only condition that the actual transfer of ownership was set to occur upon the completion of the RTP.⁷

On March 19, 2007, RG&E's parent, Energy East, announced it planned to invest \$500 million to repower Russell Station using clean coal technologies, and on May 2, 2007, Energy East announced that RG&E had informed the NYISO that it planned to build a new 300 MW plant at the Russell Station site.⁸ Both proposals were to be funded by ratepayers via rate-based, cost-of-service regulation. Further, when the proposed Transaction was announced on June 25, 2007, RG&E pointed to Iberdrola's construction expertise as a benefit of the proposed merger, expertise that could help in the repowering of Russell Station.⁹

In April, 2007, IPPNY requested that the Commission initiate a proceeding to investigate the planned redevelopment of Russell Station.¹⁰ In his response to IPPNY's request for an investigation, Mr. James P. Laurito, President and CEO of NYSEG and RG&E, stated:

Redeveloping the Russell Station site will, without question, address an identified reliability concern of the NYISO in their most recent Reliability Needs Assessment (RNA), and position this plant as an important part of New York's long-term energy future (Exh. 61).

As Mr. Younger testified, the NYISO did not choose RG&E's proposed repowering of Russell Station because other market-based solutions were available to meet the reliability need (Tr. 912). That fact did not deter RG&E from continuing to seek to repower Russell Station as a rate-based project, however.

⁷ *Id.*, Appendix B, Joint Proposal, p. 30.

⁸ *Id.*

⁹ Energy East press release, *June 25, 2007*, "IBERDROLA Reaches an Agreement to Acquire Energy East for \$4.5 Billion (3.4 Billion Euros)," *available at*, <http://phx.corporate-ir.net/phoenix.zhtml?c=104038&p=irol-newsArticle&ID=1019243&highlight=> (last visited June 26, 2008).

¹⁰ Case 07-E-0435, *Complaint of Independent Power Producers of New York, Inc., Concerning Plans of Energy East Corporation to Repower Coal and Hydroelectric Facilities*.

Nearly nine months later, with its RTP well underway, RG&E presumably should have been publicly releasing auction protocols to ensure that the Russell Station would be sold upon the RTP's completion. Yet, to the contrary, RG&E chose this time to offer a new excuse for why repowering of the facility was allegedly necessary. In response to an IPPNY information request in this proceeding, RG&E disclosed for the first time that the RTP will not meet the reliability needs of the Rochester area after Russell Station is retired (Exh. 60). RG&E attached to its information response its 2006 "Rochester Area 1900 MW Source Study" to demonstrate that the bulk transmission transformers that supply the Rochester region are forecasted to be above their rating in three years and that "another source to the region is required" (*id.*).¹¹

Despite completing the Source Study in the Spring of 2006, RG&E did not state in its May 2, 2007 press release nor disclose to the NYISO that the Russell Station repowering was allegedly needed to meet a local reliability need.¹² Clearly, RG&E's justifications for why a repowering of Russell Station is needed are continuously evolving.

In light of Energy East's conduct related to Russell Station, the Commission should apply a high level of scrutiny to RG&E's and NYSEG's generation divestiture to ensure that Energy East cannot again attempt to evade its commitments. As the ALJ concluded in his RD, divestiture of all of NYSEG's and RG&E's generation is essential to address Joint Petitioners'

¹¹ RG&E's claim that increasing load in the Rochester region will soon cause local reliability problems is belied by the NYISO's recently published 2008 Load and Capacity Data Book ("the Gold Book"). The updated forecast contained in the 2008 Gold Book for the Rochester region (NYISO Zone B) has declined significantly from the forecast provided in the 2007 Gold Book. The Rochester region load that was previously forecasted for 2010 is now not forecasted to occur until some time after 2018. This is likely to be delayed even further given the aggressive conservation plans that the Commission recently adopted in its Energy Efficiency Portfolio Standard proceeding. Case 07-M-0548, Order Establishing Energy Efficiency Portfolio Standard and Approving Programs (June 23, 2003). It should be noted that the NYISO works in close coordination with the respective Transmission Owners to set the load forecasts for each area so presumably RG&E was well aware of this marked reduction in the load forecast for the Rochester area. Moreover, even if generation were required at the site, there is no reason that RG&E must be its owner or operator. New York utilities, including RG&E's sister company, NYSEG, have entered into load pocket agreements to address such circumstances.

¹² Case 07-M-0906, Joint Petitioners' Responses to On the Record Requests and Items Subject to Check, p. 12.

ability to exercise vertical market power through their ownership of generation assets connected to NYSEG and RG&E's transmission and distribution systems.

To ensure compliance with the Commission's divestiture requirement, a firm deadline on the consummation of the divestiture must be imposed. IPPNY's proposed nine-month deadline is a fair condition to place on the Joint Petitioners.¹³ Indeed, on cross-examination, the Joint Petitioners' Benefits and Public Interest Panel admitted that a nine-month time period is not an "unreasonable goal" (Tr. 693).¹⁴ For these reasons, the Commission should, if it approves the Transaction, set forth the express condition that Joint Petitioners must complete the divestiture of all of NYSEG's and RG&E's electric generating facilities to an unaffiliated third party within nine months of the Commission's ruling on the Transaction.

II THE COMMISSION SHOULD DISMISS SPM'S THREE ALTERNATIVE PROPOSALS FOR THE OWNERSHIP OF WIND GENERATION.

Notwithstanding the fact that this proceeding began last year and involved settlement discussions, extensive discovery and a full litigated process, SPM chose to wait until its reply brief in this proceeding to raise three alternative proposals to allegedly address vertical market power issues associated with Petitioners' ownership of wind assets. The RD took note of these three alternatives, summarizing them as follows:

(1) The Iberdrola affiliate (Renewables) could enter a long-term contract with NYSEG or RG&E for each wind project at a fixed per-kWh rate (subject to operating and maintenance expense adjustments) calculated to compensate investors for the special risks of wind investment; the rate would be negotiated or

¹³ NYSEG previously divested substantial generating assets using auction protocols that were approved by the Commission. Thus, it will not be necessary to start from "Square 1" to devise auction protocols for the divestiture of these units.

¹⁴ It should be noted that National Grid just completed the auction process for a much larger facility in approximately a six-month period. While the regulatory approvals must be obtained, National Grid was able to proceed this far in its divestiture process without any advanced work on an auction process. RG&E has been on notice that it had this obligation since December 16, 2004 when the Russell-RTP Order was issued. With the completion of the RTP expected imminently, RG&E presumably is well along with its auction process design.

determined by the Commission for individual projects in the permit process; the rate would be offered to other developers unaffiliated with Iberdrola, unless they opted for a market based rate; and the non-Iberdrola developers could interconnect with petitioners' T&D grids under the supervision of a "special monitor" or the NYISO; (2) Renewables could enter such a contract with a third party rather than the T&D companies; and (3) petitioners could be required to divest the RG&E and NYSEG transmission assets (RD at 74.).

The ALJ did not, and, in fact, because these proposed alternatives were submitted so late in this process, could not assess the merits of any of these alternatives or offer a recommendation. Rather, the RD simply concludes that "[p]arties have an opportunity to respond to these proposals on exceptions, as they did not appear initially until SPM's reply brief" (RD at 74).

SPM's proposals were not offered in testimony, and thus, could not have been addressed on rebuttal testimony. Nor were they otherwise offered on the record so they could be subject to discovery and cross-examination. Indeed, they were not even mentioned in SPM's Initial Brief. Moreover, no other party offered proposals to mitigate vertical market power on the record even remotely similar to SPM's proposals.

As the ALJ correctly recognized in the RD, the vertical market power issues were one of the most significant issues in this proceeding (RD at 59). The parties to this proceeding, with the exception of SPM, put forth their positions in testimony, responded to information requests, made witnesses available for cross-examination and fully briefed their positions. It would be manifestly unjust to allow consideration of unsupported and ill-defined alternatives previously not offered to the parties for review much less subject to discovery and cross-examination at this late date. Thus, the RD should have dismissed SPM's proposals as untimely and without record support. Further, raising new proposals in reply briefs runs contrary to the customary practice

that reply briefs should be limited to addressing arguments raised by other parties.¹⁵ The Commission should dismiss SPM's proposals on procedural grounds.

CONCLUSION

For the above reasons, IPPNY respectfully requests that the Commission adopt IPPNY's limited exceptions to the Recommended Decision issued in this proceeding.

Respectfully submitted,

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¹⁵ Section 4.10(c)(3) of the Commission's rules restricts briefs opposing exceptions to exceptions raised by other parties and prohibits raising issues not put forth on exceptions. 16 NYCRR § 4.10(c)(3).