

**UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION**

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| California Independent System Operator )<br>Corporation ) | Docket No. ER98-211-000                       |
| California Power Exchange Corporation )<br>)              | Docket Nos. ER98-210-000<br>and ER98-1729-000 |
| Southern California Edison Company )<br>)                 | Docket No. ER 98-462-000                      |
| Pacific Gas & Electric Company )<br>)                     | Docket Nos. ER98-556-000<br>and ER98-557-000  |

**OFFER OF SETTLEMENT OF THE  
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

Pursuant to Rule 602 of the Federal Energy Regulatory Commission's (FERC or Commission) Rules of Practice and Procedure, 18 C.F.R. § 385.602 (1997), the California Independent System Operator Corporation (ISO), hereby submits its Offer of Settlement as a full resolution of the issues in Docket Nos. ER98-211-000 and ER98-462-000 and a partial resolution of issues in Docket Nos. ER98-210-000, ER98-1729-000, ER98-556-000 and ER98-557-000. In support of this Offer of Settlement, the ISO states as follows.

**Background**

1. On October 17, 1997, the ISO filed with the FERC for approval of its Grid Management Charge (GMC), pursuant to Section 205 of the Federal Power Act and Section 35.13 of the Commission's regulations, 18 C.F.R. § 35.13 (1997) (October 17 rate filing). The October 17, 1997 rate filing was designated by the Commission as Docket No. ER98-211-000.

2. On December 17, 1997, the Commission set the ISO's October 17, 1997 rate filing for hearing. The Chief Administrative Law Judge held a prehearing conference and set a procedural schedule on January 9, 1998.

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3. On October 31, 1997, Southern California Edison Company (SoCal Edison) made a filing in Docket No. ER98-462-000 to pass through to its wholesale customers SoCal Edison's share of the ISO's GMC charge and the PX's full requirements volumetric Administrative Charge. SoCal Edison also filed a separate scheduling and dispatch charge. The Commission set SoCal Edison's filing for hearing on December 17, 1997.

4. On October 31, 1997, Pacific Gas and Electric Company (PG&E) filed a proposed formula rate in Docket No. ER98-556-000 to recover from certain existing customers a portion of the GMC. In Docket No. ER98-557-000, PG&E filed a proposed formula rate to recover a portion of the PX Administrative Charge from existing wholesale customers. On December 17, 1997, the Commission set both of these filings for hearing.

WHEREAS, the ISO files this Offer of Settlement for the purpose of resolving certain issues that were set for hearing as described below.

## **SETTLEMENT TERMS**

### ***GMC Revenue Requirement***

5. All issues as to the Grid Management Revenue Requirement Formula, as set forth in Schedule 1, Appendix M of the ISO Tariff are resolved, in accordance with Attachment A to this settlement, for 1998. All issues with respect to the remaining rate schedules are resolved in accordance with the modifications contained in Attachment A for 1998. However, Access Charges and Wheeling Access Charges originally filed in Rate Schedules 10 and 13 will be subject to the outcome of the proceedings in *Southern California Edison Company*, Docket No. ER97-2355-000, *Pacific Gas & Electric Company*, Docket No. ER97-2358-000, and *San Diego Gas and Electric Company*, Docket Nos. ER97-2364-000

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and ER98-1682-000, and any amendments to those filings that have been accepted by the Commission. Consequently, all parties acknowledge that they will not object to the overall revenue requirement filed by the ISO on October 17, 1997 in this docket and as modified by this settlement in Paragraph 10 to reallocate \$1,300,000 of annual operating costs under the Communications Infrastructure Systems and Services Agreement, between the ISO and MCI Telecommunications Corporations (MCI Contract) from the ISO to the California Power Exchange Corporation (PX). Nothing in this settlement applies to any ISO Tariff amendment filed with the Commission after December 31, 1997 and this settlement shall not affect the rights of any party to protest, litigate, or otherwise contest any issue raised by any such amendments. The ISO will treat any adjustment amounts that reflect 1998 underrecovery of ISO costs in the development of the 1999 GMC in a nondiscriminatory manner.

6. Schedule 2 describes where other charges described in these dockets and in this Offer of Settlement are found in the ISO Tariff and Protocols. Nothing in Schedule 2 or this Offer of Settlement precludes any challenge to any change in the Tariff or Protocols, including the applicability of the charges in Schedule 2 to any entity, that may be proposed by the ISO. Nothing in Schedule 2 or this Offer of Settlement affects in any way the rights and obligations set forth in the Responsible Participating Transmission Owner agreements on file with the FERC. Agreement to this Offer of Settlement by a party does not represent the agreement of the party to the ISO's Protocols, which are the subject of other proceedings pending before the FERC.

7. Notwithstanding the general provision in Paragraph 27 of this settlement establishing the lack of precedent for matters determined by this settlement, the parties agree to the use of a formula rate that recovers the ISO's prudently incurred costs, and the parties

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expressly stipulate to the justness and reasonableness of the following formula rate provisions for the duration of any ISO financing covenants that require such provisions, but in no event later than the tenth anniversary of the date of the ISO's initial debt financing:

- the ISO GMC rate formula shall contain an amount equal to 25 percent of its Senior Lien Debt Service as a Coverage Requirement;
- the ISO shall establish and maintain a Reserve Requirement equal to 15 percent of its annual Operating Expenses; and
- the amounts financed in the initial debt financing (to cover the Infrastructure Budget, cash working capital, and 1998 and 1999 Capital Expenditure Budgets) up to a maximum level of \$310,000,000, as authorized by a resolution of the ISO Board of Governors on February 24, 1998.

If the ISO seeks to change any of these stipulated provisions it shall bear the burden of establishing that the proposed change is just and reasonable.

8. The parties to Docket Nos. ER98-211-000, ER98-210-000 and ER98-1729-000 agree to withdraw any objections previously made and waive their right to make future objections to the ISO's collection of its 1998 Operating Costs.

9. The parties agree to a revised calculation of the Grid Management Charge, contained in Rate Schedule 1 of Attachment A, as follows:

$$\text{GMC} = \frac{\text{Revenue requirement of } \$152,710,000}{\text{Total Transmission volume of } 195,000,000/\text{MWh}} = \$0.7831/\text{MWh}$$

10. The ISO and the PX agree that \$1,300,000 of the annual costs of the MCI Contract should be reallocated from the ISO to the PX. The parties to this proceeding agree

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to withdraw all allegations regarding the improper allocation of costs between the ISO and the PX in Docket Nos. ER98-211-000, ER98-210-000 and ER98-1729-000.

11. Subject to the reservation of rights in Paragraph 5 above, the parties agree that the GMC formula contained in Schedule 1, Appendix M, of the ISO Tariff should be revised as shown in Attachment A to this settlement and request that the FERC waive all requirements necessary so that the revised formula may be incorporated into the ISO Tariff at the time that the Commission approves this settlement without the requirement of additional filing or review.

12. In the 1999 operating budget, the ISO agrees that it will not seek to include an operating contingency greater than 5%.

13. The ISO agrees that annually its management will document the use of all operating budget contingency funds included in its operating budget (if any) and the 15% Operating Reserve funds agreed to in Paragraph 7 and present the report to the ISO Board of Governors within 60 days after the completion of all expenditures called for in the budgets. When presented to the Board, the report will also be posted on the ISO's Website. For 1998, in addition to the annual reports, such reports will be prepared on a quarterly basis.

14. The ISO agrees that its management will state the criteria it uses to set projected volumes for the purpose of both an interim rate adjustment and for each annual forecast used to set the GMC unit rate for the following year. This criteria and the preliminary projection will be presented to the ISO Board of Governors on or before September 1, 1998. The final projection to be used for setting the GMC will be adopted no later than December 15, 1998.

15. The ISO Board has directed its management to develop benchmarks for the cost of the services provided by the ISO and a plan for reducing costs relative to those benchmarks and ISO current performance. The Board has further directed management to provide a report to the Board by its October meeting. The ISO management will post a copy of the report in draft on the ISO Website at least one week prior to the October Board meeting. ISO management will accept public comments until November 15, 1998 and provide a report on those comments to the Board at the November meeting.

16. Beginning in 1999, the ISO will make an informational filing each year on December 15, which shall contain cost data on the ISO as provided in Attachment B and in conformance with the FERC Uniform System of Accounts (USA). This filing shall contain all information presented in the ISO's monthly financial report as provided in Paragraph 17, and such additional information as is required to set the GMC unit rate for the following calendar year, including the criteria used to set the projected volumes. To the extent that any party objects to such unit rate to be established, such party must file a complaint with the FERC under Section 206 of the Federal Power Act. Except as provided in Paragraph 7, nothing in this agreement shall be construed as barring a party's rights to seek or obtain relief under Section 206 of the FPA.

17. The ISO agrees to create monthly financial reports as indicated by Attachment B to this settlement. The monthly financial reports will present financial data both in the form created for the ISO Board of Governors and in a manner that conforms with the FERC USA, and shall include an explanation of how the data is converted from one format to the other. The monthly financial reports and the conversion explanation will be posted on the ISO's Website monthly. The ISO also agrees to prepare its preliminary yearly budget forecast for

1999 by the first week in October 1998, including a summary explanation of the bases for its projections, and post it on the ISO's Website. The ISO further agrees that during the third week in October of 1998, the ISO will hold a budget workshop open to all stakeholders at which ISO management will present its most current budget forecast and answer questions propounded to ISO by participants at the workshop. In all succeeding years, the ISO will follow the procedures set forth in Attachment B. Although approval of the ISO budget is reserved for the Finance Committee and the Board of Governors, stakeholders have the right to discuss and comment on the proposed budget as presented. The ISO further agrees that at the November Board meeting, the ISO Board of Governors shall adopt in a session open to the public a budget for the following year.

18. The ISO agrees that special procedures shall be applicable to the informational filing used to establish the GMC unit rate for the year 2002, (*i.e.*, the informational filing to be submitted December 15, 2001) and each third year thereafter (triennial filings). The ISO agrees that it will submit all the information required under 18 C.F.R. § 35.13, with the exception of pre-filed testimony, with such triennial filings. The ISO further agrees that it will provide discovery on the triennial filings limited to requests for existing documents related to these filings: provided, however, that the ISO is not required to provide the parts of documents containing confidential information. The ISO will agree to accept requests for such documents through the following January 8 for a filing subject to this paragraph and will answer such requests by the following January 24. For a filing subject to this paragraph, parties may request a hearing by filing pleadings with the FERC by the following February 15 or by the date for filing such pleadings as set by the Commission. The ISO will inform the FERC of these procedures in its transmittal letter for the filing. If the FERC orders a hearing

pursuant to such pleadings then the ISO agrees that it will have the burden of proof on all questions set for hearing, except for the continued use of a 25 per cent Coverage Requirement, the continued use of a 15 per cent Reserve Requirement, or the justness and reasonableness of its initial debt financing (as provided in Paragraph 7). This paragraph shall not limit discovery rights otherwise available if a hearing is ordered. For purposes of this paragraph, “confidential information” shall mean (a) information deemed confidential by a third party that the ISO by contract is prohibited from disclosing, but only to the extent that the ISO is unable to obtain consent from such third party to release the information; (2) information that constitutes a trade secret of the ISO; (3) documents prepared as part of any investigation by the Market Surveillance unit; and (4) information that the ISO could withhold, were it a public agency subject to the California Public Records Act.

***Unbundling***

19. The ISO agrees that its management will act as facilitator for the performance of an unbundling study to identify what, if any, of the functions of the ISO should be separately priced, and will make that study available to the ISO Board of Governors on or before September 1, 1998 and will post the study results on the ISO’s Website. A subcommittee of the stakeholder steering committee has been created to assist in the selection of a consultant to conduct the study. The stakeholder steering committee will receive periodic progress reports on the study from the consultant, and will review the study, provide advice and submit comments to the ISO management on what should be presented as the results of the study. ISO management will treat all members of the stakeholder steering committee on an equal basis and not give preferential treatment to any particular steering committee member or viewpoint.



20. If approved by the ISO Governing Board, the ISO will file with the FERC under Section 205 to implement new GMC rates based on the results of the unbundling study, proposed to be effective January 1, 1999, and the parties to this settlement reserve the right to challenge the filing on any basis including the justness and reasonableness of the formula rate, except to the extent that certain provisions of the ISO formula rate, as indicated in Paragraph 7, are not subject to future challenge, in accordance with Paragraph 7. If the ISO Board does not approve an unbundled rate, the ISO will nevertheless make a new rate filing under Section 205, proposed to be effective January 1, 1999, which will be subject to challenge as stated in the previous sentence.

21. Regardless of whether the ISO files unbundled GMC rates proposed to be effective on January 1, 1999, parties agree that the ISO shall not be liable for refunds of the GMC rates paid in 1998. This agreement will not preclude a party from seeking an order from FERC to correct billing errors or misapplication of the ISO Tariff.

***GMC Assessment***

22. Scheduling Coordinators for entities receiving energy under Existing Contract rights as defined in the ISO Tariff as it exists on April 1, 1998 (such entities being hereinafter referred to as "Existing Contract Entities") will be assessed by the ISO the GMC rate in accordance with Schedule 1 of Attachment A.

23. During 1998, the ISO will bill the GMC rate for Existing Contract Entities on a "net" basis as provided in Schedule 1. In addition, the Load served by a Qualifying Facility (QF) shall also be exempt from the GMC, provided that the QF electricity is generated on or distributed by the QF generator through private property or over distribution facilities that are dedicated to the QF through either an arrangement with the UDC in whose service territory

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the QF is located, or another entity that provides distribution level service, solely for its own use or the use of its tenants or two other corporations located on the real property on which the electricity is generated or on immediately adjacent real property and not for sale or transmission to others (such load being referred to as “Qualified Load”). Any other volumes generated by the QF and transported on the ISO Controlled Grid are subject to the full GMC. Beginning on January 1, 1999 or such other effective date ordered by FERC, the GMC, as set forth on Schedule 1 of Attachment A, will no longer be effective and the GMC will be assessed on the basis expressed in the new rate filing proposed to be effective January 1, 1999 or as ordered by the Commission. Parties will have the right to litigate the January 1, 1999 assessment of the GMC, whether or not the ISO files unbundled rates. If the Board determines that it wishes to modify the net billing policy, it shall include any necessary Tariff amendment in such filing and the ISO shall bear the burden of demonstrating the justness and reasonableness of any succeeding methodology.

24. In 1998, the ISO will not assess any Grid Operations Charge, charge for Black Start, Voltage Support, or Unaccounted For Energy (the “Specified Charges”) or a GMC for any transmission service using existing arrangements for which the contract path does not use any part of the ISO Controlled Grid (such service being referred to as “Existing Control Agreement Service”). In 1998, the parties agree that with respect to any revenue unrecovered by the ISO for Specified Charges as the result of Existing Control Agreement Service, such revenue shall be included in the amounts provided for in SABP 3.1.1.

25. With respect to the PG&E pass-through cases, Docket Nos. ER98-556-000 and ER98-557-000, PG&E will be making a compliance filing with respect to the FERC's order issued March 31, 1998 in *California Independent System Operator Corporation, et al.*, 82

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FERC ¶ 61,348 (1998). To the extent allowed by FERC's Rules of Practice and Procedures, all parties reserve the right to comment on or otherwise respond to that compliance filing. To the extent allowed by FERC's Rules of Practice and Procedure, PG&E reserves the right to reply to any comments. All parties reserve the right to seek rehearing of the FERC's order on the compliance filing. In the event that the FERC determines that a hearing is necessary as to some or all of the Existing Contracts to which PG&E seeks to apply the GMC or PX Administration Charge, all parties agree that the litigation respecting such proposed application shall be deferred until 1999; provided however, parties reserve their rights to seek rehearing or appellate review. Parties to any Existing Contracts so set for hearing shall pay the GMC (calculated in 1998 as reflected in this Offer of Settlement) and PX Administration Charges applicable to such parties as ordered by FERC. Any party that has paid the GMC or PX Administration Charge and that prevails in a final FERC order establishing that the imposition of those charges in 1998 was inappropriate shall be entitled to receive refunds with interest calculated in accordance with the FERC's regulations from April 1, 1998, or such later effective date established by the FERC's order. Litigation before an ALJ of all other issues covered by this Offer of Settlement in all other dockets shall be deferred until after January 1, 1999. In the SoCal Edison pass-through case, Docket No. ER98-462-000, the parties agree, for 1998, to settle all issues based on the rate proposal that SoCal Edison filed with the Commission on October 31, 1997, including the Scheduling & Dispatch rate, effective from the ISO operations date through December 31, 1998. The proceeding in Docket No. ER98-462-000 will be terminated with this settlement. No party may argue or litigate at any time in any forum that the level of the GMC for 1998 is unjust or unreasonable or is not in the public interest. As to the PX Administration Charge, no party may argue or

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litigate in Docket Nos. ER98-556-000 or ER98-557-000 that the level of the PX Administration Charge is unjust or unreasonable or not in the public interest. Nothing in this Offer of Settlement limits the parties' rights to litigate the amount of the PX Administration Charge in Docket No. ER98-210-000, *et al.*, except as provided in Paragraph 10. Nothing in this Offer of Settlement shall limit PG&E's rights to seek or any other party's rights to oppose any appropriate rate treatment or recovery mechanism for the portion of the GMC or PX Administration Charges that PG&E is precluded from passing through to Existing Contract Entities.

26. After the Commission's order setting the ISO's GMC filing, as provided in Paragraph 20, for hearing (or, if a hearing is not set, after any order accepting the filing and permitting it to go into effect), there will be a prehearing conference before the Chief Judge to set new procedural schedules, including discovery procedures, for the pass-through cases in Docket Nos. ER98-556-000 and ER98-557-000. The parties will consider the appropriateness of consolidating issues in the pass-through cases with the GMC rate proceeding to avoid duplicative litigation.

***General Conditions***

27. Except as provided in Paragraph 7, agreeing to this Offer of Settlement shall not be deemed in any respect to constitute an admission by any party hereto that any allegation or contention made by any other party in these proceedings is true or valid. In reaching this settlement, it was specifically agreed among the parties that this settlement represents a negotiated agreement for the sole purpose of settling certain issues, as described herein, in the captioned dockets. No signatory, participant or affiliate of any of the settling parties shall be deemed to have approved, accepted, agreed to, or consented to any fact,

concept, theory, rate methodology, principle or method relating to jurisdiction, prudence, reasonable cost of service, cost classification, cost allocation, rate design, tariff provisions, or other matters underlying or purported to underlie any of the resolution of the issues provided herein. The Commission's approval of the Settlement shall not constitute approval of, or precedent regarding, any principle or issue in this proceeding and shall not relieve the Commission or any signatory, participant, or affiliate thereof, of the burden, under Section 205 or 206 of the Federal Power Act, to establish the justness and reasonableness of any aspect of any superseding rate. Nothing herein shall affect any party's rights under existing contracts.

28. This Offer of Settlement is submitted on the further condition that, in the event the Commission does not by order accept it in its entirety, this Offer of Settlement shall be deemed withdrawn and, upon such withdrawal, it shall not constitute any part of the record in this proceeding or be used for any other purpose. If, however, the ISO and one or more of the Parties specifically agree, in writing, to all modifications ordered by the Commission, then the Settlement shall become effective as to those parties accepting such modifications.

29. The discussions among the Parties that have produced this Offer of Settlement have been conducted on the explicit understanding, pursuant to Rule 602(e) of the Commission's Rules of Practice and Procedures, that all offers of settlement and any comments on these offers are privileged and not admissible as evidence against any participant who objects to their admission and that any discussion of the parties with respect to offers of settlement is not subject to discovery or admissible in evidence. No signatory, participant, or affiliate thereof shall cite, summarize, utilize, or rely upon this Settlement, or the terms thereof, in any case, proceeding or rulemaking before this Commission or any other

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commission, regulatory authority, court, arbitrator, or alternative resolution dispute officer, to assert or infer that this Settlement, or the terms thereof, has any precedential effect on the issues resolved herein or any other substantive matter. Except as provided in Paragraph 7, the parties are agreeing to a rate level without reference to any cost components that are included in the rate level.

30. This Offer of Settlement shall become effective when an order of the Commission approving the settlement, without modification, or with modifications that are agreed to as provided in Paragraph 28, becomes final and nonappealable under the terms of the Federal Power Act.

31. If any date specified in this agreement falls on a weekend or holiday, the next business day will be the applicable date.

**WHEREFORE**, the ISO respectfully requests that the Commission accept this Offer of Settlement.

Respectfully submitted,

**CALIFORNIA INDEPENDENT  
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