UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	)	Docket No. EL02-45

Pursuant to the Commission's Order of January 25, 2002, in the above-identified proceeding, the California Independent System Operator Corporation ("ISO") respectfully submits its Reply Brief. The ISO seeks reversal of the Arbitrator's Final Order and Award in *Pacific Gas and Electric Co.,* American Arbitration Association Case No. 71 198 00711 00 ("Award").

INTRODUCTION AND SUMMARY

This proceeding is an appeal from an arbitration concerning charges that the ISO has assessed or contends are due from Pacific Gas and Electric Company ("PG&E") for Ancillary Services that the ISO procured in connection with schedules on the California Oregon Transmission Project ("COTP"). PG&E submits those schedules to the ISO.

The fundamental issue is the ISO's ability to procure Ancillary Services necessary to comply with its obligation under the ISO Tariff to maintain the reliability of the ISO Controlled Grid and to fulfill its responsibilities as Control Area operator. On February 25, the ISO submitted its Initial Brief, in which it explained that Section 2.5.1 of the ISO Tariff directs the ISO to procure sufficient Ancillary

Services to maintain the reliability of the ISO Controlled Grid in compliance with reliability criteria of the Western Systems Coordinating Council ("WSCC") and the North American Electricity Reliability Council ("NERC") and to bill Scheduling Coordinators for those Ancillary Services. Section 2.5.1 directs the ISO to ensure adequate Ancillary Services – and to recover the cost thereof – not simply *for* the ISO Controlled Grid, but *to maintain the reliability of* the ISO Controlled Grid. Thus, the ISO's authority to recover the cost of Ancillary Services is not determined by whether the transaction is on the ISO Controlled Grid, but rather by whether a lack of Ancillary Services for the transaction would endanger the reliability of the ISO Controlled Grid in violation of WSCC standards.

As the ISO set forth, the ISO's authority to procure Ancillary Services must, therefore, extend to all transactions within the ISO Control Area on facilities that are directly or indirectly connected to the ISO Controlled Grid. If a Generator serving Load over such facilities fails, it will cause an imbalance between Generation and Load in the Control Area, which includes the ISO Controlled Grid. If the ISO lacks the Ancillary Services resources necessary to correct that imbalance, the reliability of the entire Control Area, including of the ISO Controlled Grid, will be put at risk. The amount of resources necessary is determined by WSCC criteria, and is based on *all* Load in the Control Area. Accordingly, in order to fulfill its responsibilities under section 2.5.1, the ISO must procure Ancillary Services for all transactions in the Control Area, regardless of whether they involve the ISO Controlled Grid.

On March 27, Reply Briefs were filed by PG&E, by San Diego Gas & Electric Company,[1] by the Sacramento Municipal Utility District ("SMUD"), and jointly by SMUD, the North California Power Agency, the Transmission Agency of California, the City of Redding, Silicon Valley Power, the Modesto Irrigation District, the M-S-R Public Power Agency, and the Turlock Irrigation District (together, "Intervenors"). The notable fact about these reply briefs is that none addresses substantively the authority provided by the language of section 2.5.1. Rather they focus primarily on whether PG&E is the Scheduling Coordinator for the COTP schedules, whether the Intervenors, on whose behalf PG&E provides the schedules, self-provide Ancillary Services, and whether the ISO's charges violate contractual obligations.

As the ISO shows below, PG&E is a Scheduling Coordinator under the ISO Tariff and submits the schedules for the COTP transactions. This suffices to make it the Scheduling Coordinator for those transactions. The other primary arguments are of little moment to this proceeding. The self-provision of services by the Intervenors cannot be used to fulfill the ISO's obligations to maintain the reliability of the ISO Controlled Grid unless the services provided meet the necessary criteria for Ancillary Services and are made known to the ISO. To the extent services were provided, they did not meet these requirements. The various contractual provisions cited by Intervenors are simply not implicated by the ISO's charges to PG&E for COTP related Ancillary Services.

[1] Because San Diego Gas & Electric Company makes no substantive arguments regarding the Arbitration Award, the ISO does not discuss its brief in this Reply.

Nothing argued by PG&E, Intervenors, or SMUD contradicts the ISO authority and obligation, under the unambiguous terms of section 2.5.1, for having procured the Ancillary Services that are the subject of these proceeding in order to protect the reliability of the ISO Controlled Grid in accordance with applicable standards. Accordingly, the Commission should reverse the Arbitrator's Award.

ARGUMENT

I. The ISO Tariff Authorizes to the ISO to Charge for Ancillary Services Procured in Support of Transactions Within the ISO Control Area but Not on the ISO Controlled Grid.

A. No Party Has Shown How the ISO Can Fulfill Its Tariff Obligations Without Procuring Ancillary Services for COTP Transactions.

The ISO's Initial Brief demonstrated that section 2.5.1 of the ISO Tariff authorizes and obligates the ISO to charge Scheduling Coordinators for Ancillary Services necessary to ensure the reliability of the ISO Controlled Grid in accordance with Western Systems Coordinating Council ("WSSC") Minimum Operating Reliability Criteria ("MORC"). ISO Br. at 21. That obligation requires the ISO to procure those Ancillary Services not only for transactions on the ISO Controlled Grid, but also – absent notification by a Scheduling Coordinator that Ancillary Services are being self-provided – for transactions within the ISO Control Area on facilities that are directly or indirectly connected to the ISO Controlled Grid and that therefore can affect the reliability of the ISO Controlled Grid. The ISO's failure to ensure the availability of Ancillary Services in this manner would place the reliability of the ISO Controlled Grid, and indeed the Control Area for

which the ISO is responsible under the MORC, in jeopardy. No party refutes this proposition or even addresses its substance in its reply brief.

PG&E merely repeats its arguments before the Arbitrator that the ISO's obligations under WSCC criteria are not the same as the ISO's rights under its Tariff, noting that the Tariff speaks to the reliability of the ISO Controlled Grid, not the Control Area. PR&E Br. at 4. PG&E completely ignores the fact that section 2.5.1 directs the ISO to ensure adequate Ancillary Services – and to recover the cost thereof – not simply *for* transactions that use the ISO Controlled Grid, but *to maintain the reliability of* the ISO Controlled Grid. PG&E does not explain how the ISO can maintain the reliability of the ISO Controlled Grid without ensuring adequate Ancillary Services in the ISO's Control Area. For this simple reason, PG&E's argument must fail.

Lacking a substantive response, Intervenors' first line of attack is an assertion that the ISO's position is a new argument and therefore impermissible.[2] Int. Br. at 56-57. They are in error. Throughout the proceeding below, the ISO argued that section 2.5.1, as well as other sections of the ISO Tariff, require the ISO to procure Ancillary Services for all transactions in the Control Area in compliance with the MORC. *See e.g.*, ISO Tariff §§ 2.3.1.1, 2.3.1.3.2, 2.5.2.1, 2.5.2.2, and 2.5.3. The ISO's Initial Brief merely elaborates on those arguments.[3] The arguments presented in the brief are "part and parcel" of the argu-

[2] Intervenors support for the proposition that the ISO cannot raise new arguments is inapt. *Northwest Pipeline Co.*, 81 FERC ¶ 61,036 (1997) involved an attempt to raise a new *issue* on rehearing. Indeed, the Commission prefers new arguments in rehearing requests. It frequently denies rehearing for the simple reason that the petitioner has not raised a new argument.

[3] Even the Intervenors at one point refer to the ISO's arguments as just a "new spin" on its old reliability argument.

ments before the arbitrator, and are therefore appropriate for Commission consideration. *Cf. Information Systems and Networks Corp. v. City of Atlanta,* 281 F.3d 1220, 1227 n.7 (11th Cir. 2002) (on appeal, party may offer further support for an argument made below; such support is "part and parcel" of original argument); *Caribbean Mushroom Co., Inc. v. Government Dev. Bank for Puerto Rico*, 102 F.3d 1307, 1310 (1st Cir. 1996) (alternative statutory interpretation presented first time on appeal is not a new argument because party consistently stated case is outside statute's range).

Moreover, even if the arguments were new, they would appropriately be before the Commission. As the ISO discusses in section III., infra, the interpretation of the ISO Tariff on its face is a question of law. Appellate Courts often entertain new arguments regarding questions of laws. *See, e.g., Frederick Steel Co. v. Commissioner of Int. Rev.*, 375 F.2d 351, 355 (6th Cir. 1967*); see also Marx v. Loral Corp.*, 87 F.3d 1049, 1055 (9th Cir. 1996). Given the need for uniform interpretation of tariffs within the Commission's jurisdiction, it would be incumbent upon the Commission to consider the ISO's argument even if it were new.

Intervenors' only "substantive" response to the ISO's argument is to state that the Arbitrator construed the ISO Tariff as not authorizing the ISO's procurement of Ancillary Services in connection with COTP transactions.[4] Int. Br. at 7.

[4] Intervenors do state "the ISO's argument that references to "ISO Controlled Grid" in the definition of Ancillary Services and in Section 2.5.1 are not restrictive, and can be read more expansively does not change the fact that the language of the tariff is, in fact, limited to the ISO Controlled Grid." Int. Br. at 17. This statement fundamentally misunderstands the ISO's argument. The ISO does not contend that ISO Controlled Grid means anything more expansive than its plain terms. The determinative phrase, however, is "reliability of the ISO Controlled Grid," which entails responsibilities extending beyond the ISO Controlled Grid.

The ISO does not, of course, dispute that the Arbitrator so concluded. The validity of that tariff construction, however, is the very subject of this proceeding, and, as the ISO has shown in its Initial Brief, that construction is fundamentally unsound. Indeed, it would actually *preclude* the ISO from procuring the Ancillary Services necessary to "maintain the reliability of the ISO Controlled Grid consistent with WSCC and NERC criteria," as explicitly required by section 2.5.1. The Arbitrator's misguided conclusion on this issue of tariff construction carries no weight.

Intervenors also incorrectly suggest that the ISO is presuming that it has sole responsibility for procuring the necessary Ancillary Services for the Control Area, in violation of Existing Contracts.[5] Int. Br. at 43. Suffice it to say that the ISO does not claim sole responsibility; it does, however, claim ultimate responsibility under section 2.5.1 and the MORC. If (and only if) load serving entities are incapable of procuring or self-providing the necessary Ancillary Services, or do not through a Scheduling Coordinator inform the ISO of such procurement or self-provision, then the ISO must procure those Ancillary Services in order to ensure the reliability of the ISO Controlled Grid in compliance with the WSCC MORC (which imposes the ultimate obligation on the Control Area Operator.) ISO Exh. 8. (R.04668).

Finally, Intervenors' contention that COTP loads are not part of the ISO's load responsibility because they are "non-ISO Controlled Grid loads" suggests a basic unfamiliarity with the MORC, which are part of the record and pivotal to in this proceeding. Int. Br. at 58. The MORC – which are a part of the Applicable

Reliability Criteria with which the ISO must comply under its Tariff and which provide the basis for the ISO's Ancillary Services standards – define a Control Area operator's "load responsibility" as "[a] control area's firm load demand plus those firm sales minus those firm purchases for which reserve capacity is provided by the supplier." ISO Exh. 8. (R.04699). No one denies that the COTP loads are in the ISO Control Area. They are therefore undeniably part of the ISO's load responsibility under the MORC.

B. PG&E's Responsibility for the Charges at Issue Is Not Affected by the Purported Self-Provision of Ancillary Services.

Intervenors assert that the ISO's authority under section 2.5.1 is limited to Ancillary Services that are not self-provided. They state:

> Rather than accept the fact that the Intervenors provided Ancillary Services for the off-Grid transactions here . . . the ISO went out and imprudently purchased additional Ancillary Services for those transactions.

Int. Br. at 18. The ISO agrees that any Scheduling Coordinator may self-provide Ancillary Services, but this argument does not advance Intervenors' position.

The ISO explained in its Initial Brief that the Intervenors, with the exception of SMUD, do not self-provide Regulation, which is the source of the vast majority of the charges at issue. ISO Br. at 40. The ISO noted that only Generating Units that are certified by the ISO to provide Regulation and have equipment in place that allows the ISO to control the Generating Unit electronically may self-provide this particular Ancillary Service, and that the Intervenors have no such units. *Id*. The Intervenors response is that the certification requirement applies to Regulation as defined by the ISO Tariff, that they do self-provide regulation

[5] Intervenors' arguments regarding Existing Contracts are discussed in section C, *infra*.

(with a "small r") pursuant to their Interconnection Agreements, and that the ISO is obligated to honor ancillary services standards established in the Interconnection Agreements. Int. Br. at 47. Although Intervenors never really identify what they intend by "small r" regulation, that distinction is of no moment. For Regulation, whether capitalized or not, to fulfill its intended purpose under the MORC, it must be under Automatic Generation Control ("AGC") capable of responding to the ISO's digital signals to increase or decrease Generation in real time. These requirements apply regardless of whether the Regulation is supplied in connection with a transaction on the ISO Controlled Grid. They derive from the basic nature and purpose of Regulation, as reflected in Commission and WSCC rules. This type of service is called Regulation Service (with capitals) in Order No. 888.[6] It is the same as Regulating Reserve, which the MORC define as Spinning Reserve under AGC. ISO Exh. 8 at 2. (R.04669).

Intervenors admit that the MORC require some AGC. Int. Br. at 49. Intervenors assert, however, that there is no support for the ISO's position that all generation units within the Control Area must be subject to AGC. *Id.* The ISO, of course, has stated no such position. Rather, the ISO's position is that all units *providing Regulation* must be on AGC. This is consistent with the Commission's and MORC's definition, as noted above. Intervenors also assert that there is no record of support for the proposition that ISO's generation units subject to AGC

[6] *Promoting Wholesale Competition Through Open Access Non-discriminatory transmission services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 Fed. Reg. 21,540 (1996), FERC Stats. & Regs. ¶ 31,036 (1996), *order on reh'g*, Order No. 888-A, 62 Fed. Reg. 12,274 (1997), FERC Stats. & Regs. ¶ 31,048 (1997), *order on reg'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part, remanded in part on other grounds sub nom*, Transmission

must be under the exclusive dispatch of the ISO as Control Area operator.[7] Int. Br. at 49. To the extent that those units are to fulfill the MORC requirements for Regulating Service, however, Intervenors are simply *wrong*. The MORC define "Automatic Generation Control" as "[e]quipment that automatically adjusts a control area's generation from a central location to maintain its interchange schedule plus frequency bias." ISO Exh. 8 at 4 (R. 46712). The MORC also require that the Control Area operator direct the generation under AGC. *Id.*

Intervenors next assert that they can self-provide, purchase, or make contractual arrangements for regulation service. Int. Br. at 49. The ISO does not disagree. The ISO does vehemently disagree, however, with Intervenors' conclusion:

> In each case, the ultimate provider of regulation service is responsible for AGC. That practice satisfies MORC and poses no threat to Control Area reliability. There is absolutely nothing in the record to the contrary.

Id. The Intervenors appear in this conclusion to contend that each Generation owner in the Control Area can send its own signal to control AGC-equipped Generating Units and individually determine how that Generating Unit will operate. As the ISO has shown above, the record most certainly contains evidence *directly* to the contrary: the MORC. Generation under AGC providing regulation in compliance with the MORC must be centrally controlled by the Control Area operator. If it were otherwise, there would be no way for the Control Area operator to fulfill its fundamental responsibility to balance Generation and Load in real-

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Access Policy Study Group, et al. v. FERC, 225 F.3d. 667, Nos. 97-1715, et al. (D.C.Cir), *cert. granted in part*, New York v. FERC, 121 S.Ct. 1185 (2001).

[7] Curiously, Intervenors cite record evidence (testimony) for the ISO's statement that they assert is unsupported by record evidence. Int. Br. at 49.

time. ISO Exh. 8 (R. 04668). Accordingly, Intervenors cannot self-provide regulation from their Units or buy from Units of other entities such as PG&E, unless those Units' AGC is committed to the ISO.[8] Because Intervenors, by their own admission, have not provided the ISO with AGC for their Generating Units, they cannot rely upon capacity from those Units to meet their shares of Control Area requirements for Regulation. There is also no evidence in the record that PG&E, or any other entity, has provided Regulation on their behalf. Moreover, such Regulation could not be under the ISO's control unless PG&E informed the ISO of the self-provision. It has not done so.

For the same reasons, SMUD's purported "self-provision" of regulation prior to December 1, 2000, see SMUD Br. at 6-7, does not substitute for the ISO's procurement of Regulation for SMUD loads served over the COTP during that period. SMUD contends that the ISO conceded that SMUD had self-provided regulation during that period, *id.* n. 23, and the ISO does not deny that SMUD had units under AGC that could respond to SMUD's control signals. A reference to SMUD's "regulation" of its Generating Units by AGC, however, is not a concession that such regulation satisfied reliability requirements.

Although Intervenors can self-provide Spinning and Non-spinning Reserves, that self-provision cannot fulfill Reserve requirements under the MORC (and allow the ISO to fulfill its Tariff responsibility), unless the ISO is aware of such self-provision. The MORC provide, "Operating Reserves will be calculated such that the amount available which can be fully activated in the next ten min-

[8] To the extent that Intervenors' assert that the ISO's obligations to honor existing contracts require it to accept the Ancillary Services self-provided under the IA's as Regulation, regardless of

utes will be known at all times" ISO Exh. 8 at 3 (R. 04670). There is no dispute that PG&E did not inform the ISO of the quantities of Ancillary Services that Intervenors might be self-providing. Any such Ancillary Services could not, therefore, substitute for the ISO's procurement of Ancillary Services.

Intervenors nonetheless argue that, in light of their right to self-provide under their Existing Contracts, it was incumbent upon the ISO to inquire whether Ancillary Services were being provided. Int. Br. at 46-47. The ISO, in its Initial Brief, has already explained the utter impracticality of such a shift of responsibility. ISO Br. at 39. It is also worth noting, however, that the Responsible Participating Transmission Owner Agreement ("RPTOA"), which Intervenors cite as requiring the ISO to honor their self-provision, see section I.C., infra, also in section 2.3 requires PG&E to be the Scheduling Coordinator for the Existing Rightsholders. Int. Br. at 40. Int. Exh. 5 at 5 (R. 05193). Section 2B of the Scheduling Coordinator Agreement requires the Scheduling Coordinator to perform all of the obligations of Scheduling Coordinators under the ISO Tariff. ISO Tariff, Appendix B. The ISO Tariff requires Scheduling Coordinators to inform the ISO of self-provision. ISO Tariff § 2.5.20.5. There is accordingly no basis to excuse PG&E from that responsibility.

C. The ISO's Charges to PG&E for the Procurement of Ancillary Services in Connection with Transactions on the COTP Are Consistent with the ISO's Obligation to Honor Existing Contracts.

Intervenors and SMUD assert that the ISO's contractual obligations bar the ISO from assessing charges for Ancillary Services in connection with the

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its nature, that argument is address in section C. *infra*.

COTP transactions. Int. Br. at 40. In particular, they cite their Interconnection Agreements (as Existing Agreements that must be honored by the ISO); the RPTOA; and the Interim Agreement and Restated Interim Agreement between the ISO and SMUD. *Id.*

The ISO does not disagree that the ISO Tariff and the RPTOA obligate it to honor Existing Contracts. The ISO cannot agree, however, that the ISO's charges to PG&E for Ancillary Services in connection with COTP transactions would violate that requirement or contravene any provision in any of the Intervenors' Existing Contracts.

The ISO's obligation to honor Existing Contracts requires it to respect the terms of the Agreement *between the parties to the Agreement. See* Section 2.4.4.1.1 of the ISO Tariff, Section 2.1 of the RPTOA Int. Exh. 5 (R. 05191). That obligation does not affect the respective rights and obligations of the ISO and PG&E under the ISO Tariff Scheduling Coordinator Agreement except to the extent that they would interfere with the respective rights and obligations of the parties to the Existing Contracts. As is apparent from the whole of the ISO Tariff and the RPTOA (which give rise to the obligation to honor Existing Contracts), the ISO's right charges to PG&E for Ancillary Services is wholly distinct from the ability of Intervenors to self-provide, or pay PG&E for Ancillary Services under their Existing Contracts. Sections 2.7[9] and 4.1[10] of the RPTOA and section

[9] "**Accounting for Ancillary Services & Transmission Losses.** The Parties recognize that the Responsible PTO will need to apply to the FERC for the recovery in Transmission rates, as of the ISO Operations Date, its debits and credits to the Transmission Revenue Balancing Account (TRBA) with respect to any shortfalls or surpluses referenced in Sections 3.3 and 4.1 of this Agreement. The ISO agrees to provide supporting documentation for such an application by the Responsible PTO. The Parties agree that, if such recovery or application is denied by the FERC, or if the FERC subsequently disallows all or any part of this recovery, and if the Parties thereafter

2.4.4.4.5 of the ISO Tariff specifically contemplate that the Responsible Participating Transmission Owner will pay the Ancillary Services charges under the ISO Tariff even if they differ from the payments its receives under the Existing Contracts. They provide that the ISO will provide an accounting of the details of Transmission Losses and Ancillary Services calculations so that the Participating Owner can settle the difference bilaterally or through its Transmission Owner Tariff. The ISO calculates Ancillary Services obligations based on a Scheduling Coordinator's metered Load, regardless of any Existing Contracts. These provisions of the Tariff and the RPTOA are simply inconsistent with any claim that the same Tariff, by requiring that the ISO honor Existing Contracts, precludes the ISO from charging PG&E in connection with Ancillary Services for transactions under those contracts.[11]

Intervenors also cite section 4.2 of the RPTOA, which provides that self-provision pursuant to Existing Contracts shall be deemed to satisfy the ISO's Ancillary Services standards under sections 2.5.2.1 and 2.5.20 of the ISO Tariff. They argue that this provision "contemplates self-provision of and forms of Ancil-

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disagree as to the nature and extent of any amendments thereby required to Section 3.3 and Article IV of this Agreement, or the responsibility of either Party for all or any part of the amount of the recovery that is disallowed, then the dispute shall be resolved pursuant to Section 11.1 of this Agreement. In resolving such disputes, the disputing Parties and any mediator or arbitrator shall endeavor to achieve a resolution consistent with the principles expressed in Section 2.4.3.1 of the ISO Tariff."

[10] "**Rights of Responsible PTO relating to Ancillary Services.** The Responsible PTO may self-provide or purchase, from the ISO, its share of Ancillary Services. In accordance with ISO Tariff Section 2.4.4.4.4.5, the ISO will provide the Responsible PTO with details of its Ancillary Services calculations so that the Responsible PTO may, in its judgment, determine whether the Ancillary Services result in any shortfalls or surpluses in requirements under the Existing Contracts."

[11] Intervenors may argue that these payment provisions of the RPTOA are intended to apply to transactions on the ISO Controlled Grid under existing transmission contracts. It is unclear, however, why the Interconnection Agreements would be interpreted differently in this regard for schedules on the ISO Controlled Grid than for COTP schedules.

lary Services other than as prescribed in the ISO Tariff" and presumes such alternative self-provision would comply with WSCC standards. Int. Br. at 48. This assertion, however, does not follow from the language of sections 4.2. Under section 1.1 of the RPTOA, terms are used as defined in the ISO Tariff. Int. Exh. 5 at 2 (R. 05190). The ISO Tariff defines Ancillary Services by specific type, and identifies the technical requirements for provision of such services. The "Self-provision of Ancillary Services" referred to in section 4.2 of the RPTOA thus by definition refer to Ancillary Services of the type specified in the ISO Tariff. There is simply no logical basis to conclude that, by virtue of section 4.2, the Intervenors' self-provision of Ancillary Services that do not satisfy the Tariff requirements for Regulation can substitute for the self-provision (or purchase) of Regulation services that the ISO can use to comply with MORC Regulation criteria, or that Intervenors' self-provision of a lesser quantity of Ancillary Services can substitute for the quantity required by the ISO Tariff and the MORC.

The ISO does not question Intervenors', including SMUD's, right to self-provide Ancillary Services under their Existing Contracts. *See* Int. Br. at 43, SMUD Br. at 5-10. Whether they have fulfilled their contractual obligations is a matter between the Intervenors and PG&E. To the extent that Intervenors do self-provide Ancillary Services, and PG&E notifies the ISO accordingly, the ISO will not need to procure the necessary Ancillary Services. Where the Ancillary Services are not provided, or the ISO is not notified of self-provision, however, the ISO's obligation to honor the respective rights and obligations of parties un-

der Existing Contracts does not alter the ISO's obligation to procure that which was not provided and to charge the responsible Scheduling Coordinator.

SMUD discusses the Interim Agreement at length. A large part of that discussion is to establish that the COTP transactions do not occur over the ISO Controlled Grid and to demonstrate compliance with the information provision requirements of the Interim Agreement. *See* SMUD Br. at 11-13. The ISO does not assert, and has never asserted, that COTP transactions occur over the ISO Controlled Grid and the ultimate issue does not turn on compliance with the information requirements of the Interim Agreement. Rather, it turns on the requirements of the ISO Tariff. The relevance of either of these arguments to the question of whether the ISO has violated the Interim Agreement is not readily apparent.

SMUD also points out that "Western bubble" transactions (i.e., SMUD load being served directly from Western Area Power Administration to SMUD) and "SMUD bubble" transactions (SMUD load being served internally to SMUD), which do not use the ISO Controlled Grid, are deemed delivered, not scheduled, and accordingly are not charged for Ancillary Services. *Id.* at 13-14. After establishing that PG&E was issued a proxy scheduling coordinator ID for the COTP, and that COTP schedules are "deemed delivered to or from Western and then to or from SMUD", SMUD concludes that the parties to the Restated Interim Agreement must have intended the COTP schedules to be exempt from Ancillary Services charges and that the ISO's charges thus violate the Restated Interim Agreement. *Id.* at 14-15. There is a gaping hole in SMUD's logic, however. In

the bubble transactions, energy is deemed delivered directly to SMUD. It is not scheduled. In the COTP transactions, Energy is deemed delivered to and from the COTP. It is *scheduled* over the COTP. The Ancillary Services are assessed in accordance with the deliveries over the COTP.

SMUD further argues that section 7 of the Restated Interim Agreement provides for settlement between the ISO and "SMUD's Scheduling Coordinator" to be based on SMUD's net import or export after exclusion of Bubble and COTP transactions. SMUD concludes that there is no question that the settlement provisions of the Interim Agreement also contemplated the exemption of Bubble and COTP transactions from ISO Tariff charges. SMUD Br. at 14. SMUD's logic again fails. Section 7 refers to settlement with the "Lake SC." The Lake SC ID was established to schedule SMUD's new firm uses on the ISO Controlled Grid. *See* ISO Exh. 6 at 2 (R. 04567). Because the COTP schedules do not reflect new firm use of the ISO Controlled Grid, it is only natural that they be exempted from charges to the Lake SC. The ISO has never billed the Lake SC for Ancillary Services in connection with the COTP schedules. Those charges are assessed to PG&E as the Scheduling Coordinator for the COTP schedules.

SMUD's argument that the ISO's charges to PG&E for Ancillary Services in connection with COTP transaction violates the Interim Agreement must fail for a simple reason. Nothing in these Agreements prohibits those charges. Indeed, it is noteworthy that SMUD's discussion of PG&E's agreement to schedule the COTP transactions omits one important fact. The Preamble to the Restated Interim Agreement states that "PG&E agrees to schedule all of the COTP sched-

ules as a 'proxy scheduling coordinator' provided that PG&E will not be liable for any Gird Management Charge associated with those schedules." ISO Exh. 6 at 1 (R. 04566). Significantly, that is the only specified exemption. It makes no sense to conclude that the drafters intended other exemptions, but chose to mention explicitly only one.

D. PG&E's and Intervenors' Reliance on Amendment No. 2 Is Unavailing.

In various places throughout their Briefs, PG&E and Intervenors revert to the argument that the Commission's Order on Amendment No. 2 to the ISO Tariff, *California Ind. Sys. Oper. Corp.,* 82 FERC ¶ 61,213 (1998), precluded the ISO from charging Scheduling Coordinators for costs associated with procuring Ancillary Services for transactions on the COTP. ISO Br. at 20, 21, and 26; PG&E Br. at 6. As the ISO noted in its Initial Brief, the Amendment No. 2 order is not inconsistent with the ISO's ability to assess such charges, and Amendment No. 2 was not necessary for that purpose. ISO Br. at 30. Rather, Amendment No. 2 addressed a need to clarify that a Scheduling Coordinator was required for *all* transactions within the Control Area whether or not it was on the Controlled Grid. As the ISO explained, while the disposition of that Amendment might be of some relevance were the transactions at issue "unscheduled," that is pointedly not the case. ISO Br. at 30-31. All of the transactions were scheduled with the ISO, with PG&E serving as the Scheduling Coordinator. Amendment No. 2 simply is not implicated by this dispute. Both before and after the Commission's order on Amendment No. 2, section 2.5.1 provided the ISO with the authority to charge

Scheduling Coordinators for Ancillary Services necessary to preserve the reliability of the ISO Controlled Grid.

Although PG&E attempts to undercut the ISO's description of Amendment No. 2 by citing various portions of the ISO's filing letter and the Commission's orders, PG&E Br. at 7-8, none of these citations is inconsistent with the intent of the ISO to ensure the scheduling of all transactions and the absence in the Commission's decision of any prohibition on charges in connection with scheduled transactions.[12] The ISO was indeed concerned about its ability to assess charges "on Off Grid transactions, " PG&E Br. at 11, because the ISO Tariff did not call for the scheduling of such transactions. PG&E Exh. 1 (R. 04264). Nothing suggests this concern extended to scheduled transactions, such as the COTP transactions in question.

The language in the filing letter regarding the need for authority to assess charges specifically on the COTP schedules, cited by PG&E, PG&E Br. at 12, is also not to the contrary. The filing letter was submitted on February 25, 1998. No one disputes that, at that time, there was a question regarding whether PG&E would agree to continue to schedule the COTP transactions. Also, however, no one disputes that PG&E was, indeed, scheduling the transactions at the time that the charges in question were assessed. The concern about the COTP schedules expressed in the filing letter was mooted by the fact that PG&E subsequently scheduled the transactions. PG&E Exh. 1 (R. 04264).

[12] PG&E cites the Commission's statement that Amendment No. 2 would inappropriately expand the ISO's control over non-jurisdictional facilities not being transferred to the ISO's control. PG&E

Intervenors nonetheless argue that the rejection of Amendment No. 2 is relevant because PG&E did not agree to be the Scheduling Coordinator for COTP transactions, Int. Br. at 26, and that neither they nor PG&E signed a Scheduling Coordinator Agreement for the COTP transactions, Int. Br. at 32. Whether PG&E was indeed the Scheduling Coordinator is discussed in section II., *infra*. The lack of a Scheduling Coordinator Agreement "for the COTP transactions" is irrelevant. The ISO's Scheduling Coordinator Agreement does not specify particular parties or transactions. ISO Tariff, Appendix A. By executing the Scheduling Coordinator Agreement, PG&E accepted responsibility for charges in connection with all transactions it schedules. *Id. See also California Independent System Operator Corp.*, 97 FERC ¶ 61,151 (2001).

In sum, neither PG&E nor Intervenors have shown that Amendment No. 2 was intended, or necessary, to provide the ISO with the authority to assess the charges in question. Section 2.5.1 provides that authority. Nothing in the Commission's order on Amendment No. 2 undermines that authority.

E. Intervenors' Argument on Cost Causation Is Misplaced.

In its Initial Brief, the ISO argued that the assessment to PG&E of charges for Ancillary Services in connection with COTP transactions is consistent with principles of cost causation. ISO Br. at 27-28. Intervenors both mischaracterize that argument and fail to rebut it.

Intervenors first refer to the ISO's argument as a "fall-back" position, and state that cost causation cannot create an exception to the filed rate doctrine.

Br. at 13. The ISO's ability to procure and charge for Ancillary Services, however, has nothing to do with control over such facilities.

Int. Br. at 59-60. The ISO never suggested such an exception. Rather, the ISO stated that its interpretation of the Tariff was consistent with cost-causation principles, ISO Br. at 27, and argued that if the Commission found the ISO Tariff ambiguous with regard to the ISO's ability to charge PG&E for COTP-related Ancillary Services – which the ISO believes it is not – then the Commission should consider cost causation in resolving the ambiguity. ISO at 28. Intervenors fail to show that such considerations would be in any respects improper.

Second, Intervenors state that cost causation principles do not support assessing the charges to PG&E because PG&E continued to honor the self-provision commitments of its Interconnection Agreements (such that the ISO did not have to procure additional Ancillary Services) and was not the Scheduling Coordinator for COTP transactions. Int. Br. at 59. The ISO has shown above that it could not rely on such self-provided Ancillary Services if they occurred because the Intervenors were incapable of providing some and the ISO was notified of none. The ISO explains below that PG&E was the Scheduling Coordinator.

II. PG&E Is Responsible for the Cost of Ancillary Services in Connection with COTP Transactions as Scheduling Coordinator for Those Transactions.

A. PG&E'S Agreements and Its Scheduling of the COTP Transactions make it the Scheduling Coordinator for Those Transactions.

In its Initial Brief, the ISO explained that PG&E is responsible for the costs of Ancillary Services procured in connection with the COTP schedules because it is the Scheduling Coordinator for those schedules. ISO Br. at 38. PG&E and Intervenors challenge that proposition on the basis that PG&E never agreed to

be the Scheduling Coordinator for the COTP transactions. Int. Br. at 34; PG&E Br. at 7.

As ISO explained in its Initial Brief, a Scheduling Coordinator is "[a]ny entity certified by the ISO for the purposes of undertaking the functions specified in section 2.2.6 of the ISO Tariff," Tariff, Appendix A, and PG&E has executed a Scheduling Coordinator Agreement and has been certified as a Scheduling Coordinator. ISO Br. at 33; Exh. PG&E-6 (R. 04379); *see also* Tr. 58:25 - 59:2 (R. 02107-02108); Tr. 512:17-20 R. 02561). A certified Scheduling Coordinator executes only one Scheduling Coordinator Agreement even though it may be issued several Scheduling Coordinator IDs. ISO Exh. 18, ¶¶ 3 & 9 (R. 04846, 04848); Tr. 895:1-2, (R. 02945).[13] The Scheduling Coordinator Agreement does not specify particular parties or transactions for which the party will act as Scheduling Coordinator. ISO Tariff, Appendix A.

The ISO has challenged the arbitrator's finding that PG&E did not agree to act as Scheduling Coordinator for the COTP transactions. Regardless of the validity of the Arbitrator's factual findings, however, PG&E is the Scheduling Coordinator for those transactions by virtue of its Scheduling Coordinator Agreement, the RPTOA, and the fact that it does indeed schedule those transactions pursuant to its responsibilities under the Coordinated Operations Agreement.

In its Initial Brief, the ISO pointed out that the Commission rejected PG&E's effort to amend the Coordinated Operations Agreement to remove itself from its Scheduling Coordinator responsibility for the COTP transactions in *Pacific Gas and Electric Co.*, 93 FERC. ¶ 61,322 (2000). ISO Br. at 35-36. Interve-

nors argue that the ISO tortures the language of the Commission's orders and that those orders actually support PG&E's position that it never agreed to act as Scheduling Coordinator or to accept charges for Ancillary Services in connection with the COTP transactions. Int. Br. at 35. To the contrary, it is Intervenors who torture the Commission's language. The provisions cited by Intervenors are merely the Commission's recitation of PG&E's assertions. The Commission *never* concluded that PG&E had not agreed to be the Scheduling Coordinator or to accept charges in connection with the COTP transactions.

PG&E, to its credit, acknowledges that the Commission was reciting PG&E's assertions. PG&E Br. at 14. PG&E instead focuses on the fact that the Commission capitalized "Scheduling Coordinator" when referring to PG&E disavowal of responsibility, and did not capitalize the "scheduling functions" from which it refused to release PG&E. *Id.* PG&E calls this "careful capitalization." There is no indication, however, that the Commission was doing anything more that echoing PG&E's assertions in the same manner that PG&E styled them. The substance of the Commission's decision does not rely upon capitalization.[14] The Commission stated that PG&E was obligated under the COA to schedule the COTP transactions. Under the ISO Tariff, the ISO can accept schedules *only* from Scheduling Coordinators. Because PG&E provides schedules for the

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[13] ISO Exh. 18 ¶ 3 (R. 04846). Tr. 810:19-811:13, (R. 02858-59).

[14] The ISO noted in its Initial Brief that the term Scheduling Coordinator (whether capitalized or not) was not used as a term of art prior to the filing of the ISO Tariff. (Tr. 158:25-159:2 (R. 02207-02208).) It "was a new term that became defined in the ISO Tariff. It was not a term that PG&E utilized to describe its responsibilities in performing its Control Area and scheduling functions with regard to the COTP prior to ISO Start-up." (Tr. 89:16-90:1 (R. 02138-02139).) In light of these factors, the ISO argued that the Commission recognized PG&E's responsibilities when it stated that "PG&E was attempting to 'assign' to a third party scheduling coordinator duties and obligations under the COA." PG&E does not address this argument.

COTP transactions, it is *de facto* the Scheduling Coordinator for those transactions.

As the ISO argued in its Initial Brief, this conclusion is consistent with, indeed compelled by, the Commission's order in *California Independent System Operator Corp.*, 97 FERC ¶ 61,151 (2001), in which the Commission concluded that it is the submission of schedules, not the subjective intent of the Scheduling Coordinator submitting the schedules, that determines whether a Scheduling Coordinator is the Scheduling Coordinator for a particular transaction. ISO Br. at 37. Intervenors make no attempt to address this ruling. PG&E contends that the ruling is irrelevant because the transactions in question occurred on the ISO Controlled Grid. PG&E Br. at 15. Implicit in this argument is PG&E's assertion in an earlier argument that "Scheduling Coordinators are limited to scheduling transactions that occur on the ISO Controlled Grid," PG&E Br. at 5. The ISO pointed out in its Initial Brief, however, that the provisions of the Scheduling Coordinator Agreement are not limited to transactions on the ISO Controlled Grid. ISO Br. at 34-35. At least three other utilities that schedule Grid and non-Grid transactions with the ISO have executed Scheduling Coordinator Agreements identical to that executed by PG&E. (ISO Exh. 11 (Riverside SCA) (R. 04716); ISO Exh. 12 (Anaheim SCA) (R. 04724); ISO Exh. 13 (Pasadena SCA) (R. 04730); Tr. 898:25 - 899:24; Tr. 904:20 - 905:6 (R. 02948-02949); Tr. 907:16 - 908:3 (R. 02954-02955, 02957-02958).) Under their Scheduling Coordinator Agreements they fulfill their Ancillary Service obligations regardless of whether the particular schedule is on or off the grid. *Id.* Indeed, because the ISO can

only accept schedules from Scheduling Coordinators, the ISO could not schedule such non-Grid transactions if Scheduling Coordinator Agreements were so limiting.

The Commission's order in *Pacific Gas and Electric Co.*, *supra*, recognized that it was necessary for the ISO to schedule off-Grid transactions, such as those on the COTP. If the submission of schedules determines whether a Scheduling Coordinator is the Scheduling Coordinator for particular ISO Controlled Grid transactions, 97 FERC ¶ 61,151, the outcome is the same for both on-Grid and off-Grid transactions.

B. PG&E'S Citation of Extrinsic Evidence Does Not Refute Its Status as Scheduling Coordinator for the COTP Transactions.

As noted above, in light of PG&E's responsibilities under its agreements with the ISO and its scheduling of the COTP transactions, PG&E's liability for the costs of Ancillary Services that the ISO procured in connection with COTP transactions does not turn upon whether PG&E formally agreed to be the Scheduling Coordinator for the COTP schedules. Even if it did, however, PG&E's citation of evidence that it did not agree to Scheduling Coordinator responsibilities is unpersuasive.

First, PG&E notes statements in the ISO's Amendment No. 2 filing letter regarding PG&E's refusal to act as Scheduling Coordinator and cites the Commission recognition of that refusal. PG&E Br. at 7. Because the Amendment No. 2 filings were made prior to the meeting on March 24, 1998, at which the ISO contends PG&E agreed to pay the charges, *see* ISO Br. at 9, and the Commission's statements were based on those filings, this evidence is irrelevant.

Next, PG&E cites testimony by the ISO that the COTP SC ID is different from other SC IDs. PG&E Br. at 8 (citing Tr. 1165:17 – 1166:1 (R. 03215-16) and Tr. 1356:19-22 (R. 03406)). Actually, the testimony simply indicates that the ISO treats the COTP SC ID differently in that the ISO transferred the Ancillary Services cost to another PG&E SC ID in the final statements and in other unspecified ways. There is no suggestion in the testimony that PG&E, by virtue of those differences, is not a Scheduling Coordinator or is exempt from Scheduling Coordinator responsibilities. PG&E also asserts that contemporaneous ISO notes show that PG&E was not in agreement that it would be responsible for COTP related charges (citing PG&E Exh. 8 and 9 (R. 04404-09)). The first set of notes concerns a March 16, 1998, meeting, which (like the Amendment No. 2 filings) was prior to the meeting at which the ISO contends PG&E agreed to pay the charges and is not dispositive. *See* ISO Br. at 9. The second set of notes does not discuss charges. Although it does refer to PG&E being a "small sc," there is no indication what the author intended by the phrase. She was not asked in testimony what the phrase meant and whether it had any implications for PG&E's cost responsibility. *See* Tr. 888 - 1069 (R. 02940-03119). The only other evidence cited by PG&E concerns its ignorance of the transfer of COTP-related charges from the COTP SC ID to another PG&E SC ID. As the ISO explained in its Initial Brief, this testimony is simply not credible. ISO Br. at 9.

III. There Is no Impediment to the Commission's Rejecting the Arbitrator's Interpretation of the ISO Tariff.

In its Initial Brief, the ISO explained that section 13.4.2 of the ISO Tariff establishes the scope of review. ISO Br. at 15. It only calls for deference with

regard to findings of fact, implying *de novo* review of conclusions of law. The ISO stated that because the arbitrator's interpretation of the ISO Tariff is a legal conclusion, it warrants *de novo* review by the Commission. *Id*. Intervenors oppose *de novo* review on two grounds. First, they assert that the arbitrator's conclusion that the Tariff is clear on its face turned on a factual assessment of the record and the application of clear precedent, and that the review is therefore largely a factual question. ISO Br. at 5. Second, they urge the Commission to apply a deferential standard of review even if the interpretation is a legal issue. *Id*.

A. The Interpretation of the ISO Tariff is a Question of Law.

Contrary to all logic, Intervenors argue that a determination whether Tariff language is clear on its face depends upon the factual record.[15] *Id*. Although Intervenors identify testimony regarding the meaning of the Tariff language, Int. Br. at 7, such testimony is at best opinion, not fact. Moreover, only if the Tariff language were ambiguous – and both the ISO and Intervenors contend that it is not – does factual evidence become relevant. Whether Tariff language is ambiguous is a question law. *See Consolidated Gas Trans. Corp. v. FERC*; 771 F.2d 1536, 1544 (D.C. Cir. 1985); *Tarpon Transmission Co.*, 42 FERC ¶ 61,050 at 61,277, n. 6.

Intervenors' citation of *Great Northern Ry. Co. v. Merchant's Elevator Co.*, 259 U.S. 285 (1922) is inapt. Int. Br. at 6. In *Great Northern*, the Court stated that when "words are used . . . in a peculiar meaning," "extrinsic evidence may be

[15] As noted above, the Intervenors also note that the interpretation requires the application of precedent. The evaluation of precedent, of course, is a quintessential legal issue.

necessary to determine the meaning of the words appearing in the document." *Id.* at 291-92. The fact that the ISO's interpretation of the Tariff differs from that offered by the Arbitrator and the Intervenors does not imply that the ISO's interpretation depends upon giving terms a "peculiar meaning." The Court identified two circumstances in which this might be necessary: where technical words not commonly understood are used, or to establish a usage of trade or locality. The ISO has not argued that the plain meaning of the Tariff depends on the interpretation of technical terms or on particular trade usage. Indeed, no party has introduced evidence regarding technical meanings of Tariff terms or trade usage.

Contrary to Intervenors' assertion, the ISO does not argue that the ISO Tariff does not mean what it says. Rather, the ISO contends that the ISO Tariff means *exactly* what it says: it *does not* say that the ISO may only charge Scheduling Coordinators for Ancillary Services to the degree that they schedule on the ISO Controlled Grid; it *does* say the ISO is authorized to procure such Ancillary Services as are necessary to ensure the reliability of the ISO Controlled Grid. Whether the ISO is correct is a question of tariff interpretation, an issue of law that is for the Commission to decide.

B. The Commission Should Review Questions of Law *De Novo*

Intervenors' arguments that the Commission should defer to the Arbitrator's interpretation even if it involves a question of law are no more persuasive. Intervenors rely upon the Commission's Policy Statement Regarding Regional Transmission Groups[16] and upon Order No. 578[17] in an effort to establish an

[16] Policy Statement Regarding Regional Transmission Groups, FERC Stats. & Regs. ¶ 30,976, 30,8777 (1993).

"overwhelming" policy for a narrow standard of review and a "commitment" to honoring the results of arbitration proceedings. Int. Br. at 8. Yet, in the Policy Statement, the Commission only made a commitment to give "appropriate" deference to such results. In its Initial Brief, the ISO quoted the Commission's understanding of "appropriate" deference in full. ISO Br. at 14. In particular, the Commission stated, "[J]ust as we would not defer to an administrative law judge's decision that is directly contrary to Commission policy, we would not defer to an arbitrator's decision that is directly contrary to Commission policy." *Id.* at 41631.

Intervenors' citation of Order No. 578 also fails to establish any Commission preference for deferring to arbitrators' conclusions of law in circumstances such as those presented by this proceeding. As an initial matter, Intervenors misstate the Commissions' order. Int. Br. at 9. The Commission stated that vacatur would be necessary if an award "contravenes the public interest or is in any other way inconsistent with statutory requirements;" it did *not* state that vacatur was appropriate "only" in such circumstances. FERC Stats. & Regs. at 31,328. Indeed, the Commission went on to state, "On balance, given the Commission's statutory responsibilities, decisions on vacatur will necessarily have to be made on a case by case basis." *Id.*

Moreover, the policies of Order No. 578 are simply not applicable here. Order No. 578 did not involve Commission review of arbitration awards under the terms of tariffs or contracts. Rather, it involved arbitration of disputes that are brought in the first place before the Commission. It was intended to implement

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[17] Alternative Dispute Resolution, FERC Stats. & Regs. ¶ 31,018, 31, 328 (1995).

the Administrative Dispute Resolution Act ("ADRA") of 1990.[18] The Commission retains the right to determine which disputes are appropriate for alternative dispute resolution. Those regulations do not apply here, even by analogy.

Even if the ADRA were applicable to this dispute (which is outside the scope of the statute), it would not limit review as Intervenors argue. At the current time, under the ADRA, review of arbitration awards is covered by the Federal Arbitration Act ("FAA").[19] In turn, the FAA establishes very limited grounds for review. 9 U.S.C. § 10. The review limitations of the FAA, however, would not dictate deference to the Arbitrator's conclusions of law. Review limitations under the FAA act only as a default: they do not apply when the underlying arbitration agreement specifies a broader scope of review. *Lapine Tech. Corp. v. Kyocera Corp.*, 130 F.3d 884, 888 (9th Cir. 1997); *Gateway Technologies, Inc. v. MCI Telecom. Corp.,* 64 F.3d 993, 996 (5th Cir. 1995). In this instance, section 13.4.1 of the ISO Tariff allows an appeal based on much broader grounds:

> [T]hat the award is contrary to or beyond the scope of the relevant ISO documents, United States federal law, including without limitation, the FPA, and any FERC regulations or decisions, or state law.

Any policy of deference to an arbitrator's award that might be drawn from policies of Order No. 578 and the ADRA (if there were any) would simply be inapplicable here.[20]

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[18] *Id.*

[19] 5 USC § 581(1)(b). In an order subsequent to Order No. 578, the Commission conformed its regulations with 1996 amendments to the ADRA and deleted the regulations providing for vacatur of awards. Complaint Procedures, FERC Stats. & Regs. ¶ 31,071 (1999).

[20] For the same reasons, Intervenors' assertions that de novo review of questions of law, because of more limited review in the FAA and California law, would encourage forum shopping are unfounded. The law is well established if this dispute were subject to the FAA (which is not clear) that the scope of review under the FAA would nonetheless be governed by the provisions of the ISO Tariff, not by the limitations of 9 U.S.C. §10. *Id.* California law similarly provides for ex-

Intervenors remaining arguments in favor of deference to the Arbitrator (made in the final section of their brief) also fail. Int. Br. at 64. First, they note that the Commission earlier rejected a request for direct appeal of ISO decisions because the Commission had neither the time nor resources to address all the issues that might arise. *Id*. At 65-66. Intervenors contend that applying a *de novo* standard would encourage needless litigation and eliminate the resource saving potential of arbitration. Intervenors ignore the fact that this proceeding has already saved resources: a hearing has been conducted and a record established without use of Commission resources. Intervenors also ignore the fact that the ISO does not advocate *de novo* review of factual findings, but only of legal conclusions, which are rightly in the purview of any reviewing body. That this is the first arbitration that that has been brought to the Commission in four years of ISO operation suggests that Intervenors concerns about overburdening the Commission are highly exaggerated.

Second, Intervenors cite *Kansas Gas & Electric Co.* 27 FERC ¶ 61,335, *reh'g granted in part*, 28 FERC ¶ 61,112 (1984), for the proposition that the Commission has previously reviewed an arbitration decision and concluded that the primary question to be decided was whether the filed rate was consistent with the arbitration award. Int. Br. at 66. Intervenors' argument is once again selective and misleading. In *Kansas Gas & Electric Co.*, the Commission was not called upon to *review* an arbitration award under a tariff that provided for appeal to the Commission. Rather, the Commission was presented with a rate that

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panded review according to the provisions of the underlying instrument providing for arbitration. *Pacific Gas & Electric Co. v. Superior Ct.*, 19 Cal Rptr.2d 295 (1993). There is no reason for a

arose out of a binding arbitration, i.e., it was acting to *implement* the award. It accordingly required the protesting customers to abide by their contractual agreement to accept the arbitration. Even so, the Commission did not shirk its statutory responsibilities. It did *not* "note[ ] that "the primary question . . . was whether the filed rated is consistent with the arbitration award," Int. Br. at 66, n.237. Rather, the Commission stated, "[W]e shall limit our review to *whether KG&E's rates are cost justified and* whether they properly reflect the AAA award." 27 FERC at 61,647 (emphasis added). Indeed, the Commission set the rate for hearing. Further, on rehearing, the Commission allowed litigation of an issue not considered in the arbitration because the parties had concluded that it was an issue best evaluated by the Commission. 68 FERC at 61,195. Here, analogously, the ISO Tariff specifically provides for review and, by implication, *de novo* review of legal conclusions. ISO Tariff §§ 13.4.1, 13.4.2.

In sum, there is no Commission policy calling for deference in circumstances such as those presented here. Indeed, under the case-by-case approach endorsed by the Policy Statement, *de novo* review of the Arbitrator's tariff interpretation is appropriate. The proceeding concerns novel issues of tariff construction that has potential implications on the Commission's policy of encouraging the development of a Regional Transmission Organization that can assume control area functions. The proceeding also has reliability implications for third-parties that were not involved in the arbitration and who depend on the Commission to construe and implement the tariff provisions that protect grid reliability. There is no reason for the Commission to depart from well-established principles

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court to apply a standard different from that applied by the Commission.

under which conclusions of law are reviewed *de novo.* *Vector Pipeline, LP v. Acres of Land*, 157 F.Supp 2d 949 (2001); *Harris v. Parker College Chiropractic*, 2002 U.S. App., Lexis 4782 (2002).

REQUEST FOR GUIDANCE

In its Initial Brief, the ISO requested that if, despite the considerations that the ISO discussed, the Commission disagreed that the ISO Tariff provides the authority for the ISO to charge PG&E, as Scheduling Coordinator, for Ancillary Services that the ISO has procured in connection with transactions on the COTP, that the Commission direct the ISO to make appropriate filings to provide such authority and permit the ISO to recover the costs of the Ancillary Services it has previously provided.

The ISO would also request that, if the Commission disagrees with the ISO's interpretation of its authority and does not direct such filings, the Commission provide the ISO with guidance regarding the proper allocation of the costs imposed by the arbitration award. Section 13.5.3.1 of the ISO Tariff directs the ISO to attempt to ascertain which Market Participants are responsible for payment of an Award by the ISO and allocate the payment of the award equitably among such Market Participants. Market Participant is broadly defined to include not only Scheduling Coordinators but also any entity that participates in the Energy Marketplace through buying, selling, transmitting, or distributing Energy or Ancillary Services into, through, or out of the ISO Controlled Grid. If the ISO is unable to identify such Market Participants, it is to allocate the payment to all Scheduling Coordinators through Neutrality Adjustments.

CONCLUSION

For the foregoing reasons, the Commission should reverse the decision of the Arbitrator and issue an order that:

(1) permits the Market Participants to retain the $14,172,337.08 paid by PG&E for Ancillary Services and other costs during the period April 1998 through April 1999;

(2) permits the ISO to recover from PG&E an amount of at least $40,376,867 for Ancillary Services incurred to support COTP Schedules from May 1999 through June 30, 2001, plus interest;

(3) declares that PG&E is responsible to pay for any Ancillary and related services the ISO has procured since June 30, 2001, or will in the future procure, to support COTP Schedules submitted to it by PG&E; and

(4) declares that PG&E is required to continue to act as the COTP Scheduling Coordinator and provide the ISO with any Scheduling information or data necessary to enable the ISO to discharge its obligations under the Tariff and as the certified WSCC Control Area Operator until such time as the Commission authorizes otherwise.

Respectfully submitted,

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