

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

San Diego Gas & Electric Company,)	
Complainant,)	
)	Docket No. EL00-95-000
)	
v.)	
)	
Sellers of Energy and Ancillary Services)	
Into Markets Operated by the California)	
Independent System Operator and the)	
California Power Exchange,)	
Respondents)	
)	
Investigation of Practices of the California)	Docket No. EL00-98-000
Independent System Operator and the)	
California Power Exchange)	
)	
California Independent System Operator)	Docket No. ER03-746

**ANSWER OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR TO
CALIFORNIA PARTIES’ MOTION FOR CLARIFICATION ON
ISO/PX RERUN ISSUES**

Pursuant to Rules 212 and 213 of the Commission’s Rules of Practice and Procedure,¹ the California Independent System Operator Corporation (“CAISO”) submits this answer to the California Parties’ July 24, 2015 Motion for Clarification on ISO/PX Rerun Issues. In their motion, the California Parties argue that the CAISO and the California Power Exchange (“PX”) have diverged from the Commission’s directives with regard to how to determine and allocate the refund shortfalls resulting from the Ninth Circuit’s decision in *Bonneville Power Admin. v. FERC*,² which found that the

¹ 18 C.F.R. § 385.213 (2015).

² *Bonneville Power Admin. v. FERC*, 422 F.3d 908 (9th Cir. 2005) (“BPA”).

Commission did not have authority to require governmental entities to pay refunds in these proceedings. The California Parties are incorrect. The CAISO has been transparent in its intended calculations, scrupulously following Commission directives.

I. BACKGROUND AND SUMMARY OF ANSWER

In its order on remand from the *BPA* decision, the Commission vacated all of its orders in these proceedings to the extent that they ordered governmental entities to pay refunds.³ The Commission recognized, however, that removing the refund obligation for governmental entities would create a shortfall in the total amount of refunds, and that shortfall would need to be reflected in reduced refund amounts received by buyers. The Commission adopted a two-step process for the CAISO and PX to implement the *BPA* mandate: (1) calculate the amount of the refund shortfall, which involves determining the amount of refunds that would have been owed by each governmental entity absent the *BPA* decision; and (2) allocate the refund shortfall by reducing the amount of refunds that would otherwise be received by refund recipients. With respect to the first (calculation) step, the Commission directed the CAISO and PX to determine the refund shortfall for each governmental entity based on netting their purchases and sales in each hour during the refund period.⁴ With respect to the second (allocation) step, the Commission adopted the CAISO's proposal to utilize a simplified pro rata reduction of refunds to each refund recipient, and directed the CAISO and PX to implement such an

³ *San Diego Gas & Elec. Co.*, 121 FERC ¶ 61,067 (2007) ("October 19, 2007 Order").

⁴ *San Diego Gas & Elec. Co.*, 125 FERC ¶ 61,214 at PP 17-19 (2008) ("November 20, 2008 Order").

approach based on refund recipients' "final net refund position in relation to total net refunds."⁵

The California Parties object to three components of the CAISO's *BPA* results: (1) the CAISO's calculation of the refund shortfall associated with each exempt governmental entity based on sales and purchases only in its markets, rather than combining the CAISO and PX markets; (2) the CAISO's allocation of the resulting refund shortfalls to refund recipients based on each refund recipient's refund position over the entire refund period, as opposed to its hourly positions; and (3) the CAISO's allocation of the *BPA* shortfalls based on refund recipients' total net refunds, after accounting for cost recovery offsets and other refund offsets that the Commission had approved for suppliers, as opposed to allocating the *BPA* shortfalls based on refunds calculated before factoring in those offsets.

The CAISO developed its *BPA* calculation and allocation process based on a careful analysis of the relevant Commission orders. Moreover, the CAISO has been fully transparent as to its intended process, providing parties regular updates through status reports filed with the Commission and distributions of the results of its calculations. In doing so, the CAISO has solicited and taken into account parties' comments on various aspects of its process, including the *BPA* shortfall allocation. The CAISO is thus confident that its process for calculating and allocating the *BPA* shortfalls complies with the Commission's orders in this proceeding.

The first two of the California Parties' objections to the CAISO's process are without merit because they are based on overbroad readings of passages taken out of

⁵ October 19, 2007 Order at P 39.

context, apparently attempting to cast uncertainty on the Commission's directives regarding the calculation and allocation of the BPA refund shortfalls. The third objection, that the allocation of the cost recovery offset should take account of the results of the *BPA* shortfall allocation, raises essentially the same issue that the CAISO addressed in response to a motion that the California Parties filed in 2008, which the Commission has yet to rule on. Lacking any argument based on the actual language of the Commission's orders, the California Parties provide only a bare allegation that the CAISO's process of allocating the *BPA* shortfalls based on the results of the cost recovery allocation is "inequitable." Because the CAISO's process is derived directly from the language of the Commission's orders, this argument is in effect a collateral attack on those Commission orders.

For these reasons, the California Parties' motion should be denied. Alternatively, the Commission should defer consideration of these arguments until such time as it considers and rules on the CAISO's refund rerun compliance filing, which it contemplates filing this Fall.⁶ Doing so would provide the Commission with the benefit of having before it the full record and explanation of the CAISO's refund calculations, including all of the offset allocations. Also, in addition to the three issues presented in the California Parties' instant motion, the CAISO anticipates that the California Parties will raise numerous other challenges to the CAISO's compliance filing. Therefore, ruling on these three issues now will provide little in the way of additional certainty. It would be more efficient for the Commission to simply rule on these issues along with all other

⁶ The CAISO anticipates filing shortly after the date of this answer a new status report in which it will provide additional details regarding its anticipated schedule for future activities in this proceeding.

issues involving the CAISO's refund calculations at the time the CAISO makes its compliance filing.

II. ANSWER

A. The CAISO Correctly Calculated BPA Shortfall Amounts Based on Sales and Purchases in its Markets

In their motion, the California Parties contend that the Commission's orders require the CAISO and PX to calculate a single *BPA* refund shortfall for each governmental entity based on its net purchases and sales in both the CAISO and PX markets for each hour, as opposed to separate CAISO and PX refund shortfall totals based on purchases and sales in their respective markets.⁷ The California Parties are mistaken.

First, the California Parties' argument conflicts with the fundamental principle underlying the Commission's methodology for determining the *BPA* shortfall, as set forth in the November 20, 2008 order in these proceedings. Therein, the Commission directed the CAISO to calculate governmental entities' refund amounts "using the billing and payment procedures set forth in the CAISO Tariff," which includes netting purchases and sales during each hour.⁸ The CAISO's billing and payment procedures in effect during the refund period only provided for netting purchases and sales for transactions that took place in the CAISO's markets. They did not require or permit the CAISO to net participants' CAISO market transactions against transactions that occurred in the PX markets. Therefore, there is no basis to conclude that the

⁷ California Parties Motion at 4-6.

⁸ *San Diego Gas & Elec. Co.*, November 20, 2008 Order at PP 17-19 (citing and quoting CAISO Settlement and Billing Protocol 3.2.1).

Commission intended to the CAISO to combine the transactions in its markets with those in the PX for purposes of calculating governmental entities' refund shortfalls.

The California Parties' interpretation is also inconsistent with the manner in which the November 20, 2008 Order addressed the issue of how to account for the PX's participation as a scheduling coordinator in the CAISO markets. In its original order on remand from the Ninth Circuit's decision, the Commission made clear that it could not require governmental entities to pay refunds relating to transactions entered into in the CAISO and PX markets.⁹ That order, however, did not take into account the fact that the PX, which is a FERC-jurisdictional public utility, was a CAISO scheduling coordinator. Absent further clarification, governmental entities that sold in the PX would have been exempted from owing refunds to the PX, but the PX – because it is not an exempt governmental entity – would have owed refunds to the CAISO in connection with the corresponding sales that it made in the CAISO's markets on behalf of those governmental entities. This would have resulted in a cash shortfall in the PX markets.

To avoid this problem, the Commission, in the November 20, 2008 Order, required the PX to provide the CAISO with a reversal adjustment for transactions made on behalf of governmental entities, which the CAISO would then allocate to net refund recipients in its own market along with other *BPA* related shortfalls.¹⁰ This directive would have not have made sense, however, if the Commission had intended for the CAISO and PX to combine their transactions in calculating a single *BPA* shortfall for each governmental entity. If the Commission had intended a combined market

⁹ October 19, 2007 Order at P 36.

¹⁰ November 20, 2008 Order at PP 35-38.

calculation, as the California Parties allege, the CAISO/PX coordination concern would have been entirely different: namely, making sure that any shortfall amount allocated to the PX matched its refund credit from the CAISO. There would have been no need, however, for the Commission to require the CAISO to provide the PX a credit of its own in the CAISO markets.

As these passages in the November 20, 2008 Order make clear, the Commission contemplated that the CAISO and PX would determine the refund shortfalls resulting from the *BPA* decision separately, by calculating each governmental entity's sales and purchases in their respective markets. This outcome is also consistent with the Commission's underlying methodology for calculating refunds in the first instance, which required the CAISO and PX to perform reruns of their settlements systems to apply the Commission-mandated mitigated market clearing price ("MMCP") based on purchases and sales in their individual markets.¹¹

The California Parties do not address these passages in the November 20, 2008 Order, but rather base their argument solely on language contained in two subsequent Commission orders addressing the CAISO and PX compliance filings for the preparatory rerun compliance filings: the July 15, 2011 order, and the February 3, 2012 order denying rehearing of the July 15 order.¹² In neither of these orders, however, did the Commission state or suggest that it intended to revise the methodology described in the November 20, 2008 Order, or provide any other indication that the CAISO and PX

¹¹ See, e.g., *San Diego Gas & Elec. Co.*, 96 FERC ¶ 61,120 at 61,519 (2001) ("Once the ISO has calculated the hourly market clearing prices for the refund period, this data should be used by both the ISO and PX to rerun their settlement/billing processes and all penalties.")

¹² California Parties Motion at 5 (citing *San Diego Gas & Elec. Co.*, 136 FERC ¶ 61,036 (2011) ("July 15, 2011 Order"), *order on reh'g*, 138 FERC ¶ 61,092 (2012) ("February 3, 2012 Order")).

should calculate the BPA refund shortfalls jointly. To the contrary, in the July 15, 2011 Order, the Commission concluded that the rationale set forth in the November 20, 2008 Order for hourly netting when the CAISO calculates the shortfall amount for each governmental entity should apply with equal force to the PX, and explicitly directed the PX “*to perform its final refund calculations netting purchases and sales over hourly intervals to reflect the period during which the obligation was incurred.*”¹³ This discussion of a separate PX shortfall calculation would make no sense if the Commission intended the CAISO and PX to jointly calculate BPA shortfalls based on governmental entities’ net positions between their markets.

The California Parties’ reliance on the February 3, 2012 Order avails them no better. They point to paragraph 23 of that order as “unequivocal” evidence of the Commission’s intent that the CAISO and PX determine the *BPA* shortfall based on governmental entities’ sales and purchases netted between their two markets. However, paragraph 23 does not address the *BPA* shortfall calculation or allocation process. Instead, it merely affirms the Commission’s finding in the July 15, 2011 Order that the release of principal amounts to governmental entities must account for any remaining balance between the CAISO and PX markets “so that the CAISO and CalPX markets can be financially cleared together.”¹⁴ The California Parties’ argument conflates two separate issues: the calculation and allocation of the BPA adjustment for each governmental entity, which the Commission has described as being performed separately by the CAISO and PX, and the ultimate financial clearing and distribution of

¹³ July 15, 2011 Order at P 40 (emphasis added).

¹⁴ July 15, 2011 Order at P 30.

the resulting funds from the PX. Paragraph 23 in the February 3, 2012 Order simply reinforces the Commission's conclusion that the CAISO and PX markets should be jointly cleared on a financial basis, an outcome which both the CAISO and PX have explicitly supported.¹⁵

Finally, as discussed in greater detail in the PX's answer to the California Parties' motion, having the CAISO and PX calculate combined BPA refund shortfall amounts raises practical issues with respect to the different invoice cycle and payment due dates in the CAISO and PX markets. These issues would need to be resolved before the CAISO and PX could perform a joint calculation. This would require the CAISO and PX to either seek Commission guidance prior to performing such a calculation, thereby further delaying the resolution of this proceeding, or simply decide these issues between themselves, which would still involve a risk of delay if any party subsequently challenged the CAISO's and PX's decisions and prevailed.

B. The CAISO Correctly Allocated the BPA Shortfall to Net Refund Recipients on a Refund Period-Wide Basis

In the October 19, 2007 Order, the Commission agreed with the CAISO that *BPA* shortfalls should be allocated through a simplified *pro rata* reduction of refunds to each refund recipient, and directed the CAISO to implement such an approach based on

¹⁵ If the California Parties are correct that the Commission's statement reaffirming that the CAISO and PX markets will be "financially cleared together" should be broadly read to mean that the CAISO and PX must calculate *BPA* refund shortfalls jointly, the implications of this would be far-reaching. Because there is nothing in the Commission's statement limiting it to the *BPA* calculations, adopting the California Parties' interpretation would presumably require the CAISO and PX to jointly perform all of the various other refund and offset calculations. The CAISO and PX would then need to re-do not only the *BPA* calculations, but most of their other calculations as well. In context, it seems extremely unlikely that the Commission intended this brief statement of reaffirmation to modify the manner in which the CAISO and PX have performed their calculations to date.

each refund recipient's "*final* net refund position in relation to *total* net refunds."¹⁶ The most plausible reading of this language, given the terms "final" and "total," is that the Commission contemplated that the CAISO and PX would allocate the BPA shortfall based on parties' aggregate refunds for the entire refund period, rather than, as the California Parties argue, based on whether parties happened to be net refund recipients for some granular portion of the refund period (e.g. hourly).¹⁷ This interpretation is further supported by the fact that the Commission analogized the treatment of *BPA* shortfalls in the October 19, 2007 Order to the manner in which it decided to allocate the interest shortfall amongst PX participants: "based upon the *final net interest position* for each participant in relation to the *total* amount of the interest shortfall."¹⁸ The Commission has directed that the PX interest shortfall be allocated on a period-wide basis.¹⁹

Moreover, at the time it issued the October 19 Order, the Commission could not have intended that the CAISO allocate *BPA* shortfalls based on hourly net refunds, rather than net refunds over the entire refund period. The hourly netting methodology, which the Commission created for purposes of calculating the underlying *BPA* refund shortfalls, was not developed until over a year later, in the November 20, 2008 Order, and the Commission had not used an hourly netting methodology for any purpose

¹⁶ October 19, 2007 Order at P 39.

¹⁷ The California Parties also argue that the allocation of *BPA* refund shortfalls should be performed jointly based on hourly net refund positions between the CAISO and PX markets. This argument is without merit for the reasons set forth in Section II.A *supra*.

¹⁸ October 19, 2007 Order at P 39, fn. 49.

¹⁹ See *San Diego Gas & Elec. Co.*, 110 FERC ¶ 61,336, at P 41, 56 (noting that under the interest shortfall allocation methodology chosen "a share fraction would be derived based upon the absolute value of each participant's interest for its final account balances in relation to the total amount of the interest shortfall. The interest shortfall would then be allocated according to each participant's share fraction.")

previously in this proceeding. Accordingly, the Commission could not have intended that to be the allocation formula when it issued the October 19, 2007 Order, and the phrase therein directing the CAISO to allocate the BPA shortfalls based on “total net refunds” should have its natural meaning – *i.e.*, net refunds over the entire period.

The California Parties do not address any of this in their motion, but rather base their position on the rationale that the Commission “expressly rejected period-wide netting” in the November 20, 2008 Order.²⁰ This argument is without merit. The Commission’s discussion of period-wide netting in the November 20, 2008 Order was focused entirely on the methodology for calculating the amount of refunds that would, absent the BPA decision, have been owed by governmental entities – *i.e.*, the BPA shortfall itself. The Commission directed the CAISO to calculate this shortfall by netting, for each hour, the “sales and purchases” made by governmental entities. The Commission did not address the mechanism for allocating shortfall amounts to refund recipients, other than to reiterate the directive from the October 19, 2007 Order that it be based on parties’ final net refund position in relation to total net refunds. The fact that the Commission left its earlier conclusions regarding the allocation mechanism undisturbed in the BPA Rehearing Order is understandable given that the subject of the California Parties’ request for rehearing that prompted the passage at issue in the November 20, 2008 Order was how to calculate the shortfall offsets, rather than how to allocate them to refund recipients. For these reasons, there is no basis to support the California Parties’ conclusion that the November 20, 2008 Order modified the allocation

²⁰ California Parties Motion at 8.

methodology established in the October 19, 2007 Order, or otherwise required the CAISO to allocate the BPA shortfall to parties on an hourly basis.

The only other authority that the California Parties cite in support of their argument is the Commission's directive in its June 18, 2009 Order that "the allocation methodology should be consistent with the manner in which the . . . offsets are calculated."²¹ This statement relates to cost offset allocations, not BPA shortfall allocations, and was made in reference to the rationale for combining the CAISO and PX markets for purposes of both calculating and allocating the cost offsets. It does not support the California Parties' desired outcome here.

Finally, the CAISO disputes the California Parties' characterization of the CAISO's *BPA* shortfall allocation methodology as "monthly" in nature.²² The CAISO assigned allocation results to specific months solely for the purpose of interest calculations, and doing so did not affect the actual methodology for allocation of the *BPA* shortfall among net refund recipients.

C. The CAISO Appropriately Allocated BPA Shortfalls Based on Market Participants' Final Refund Positions, Including Fuel Cost, Emissions, and Cost Recovery Offsets

In its Forty-Sixth status report (filed October 21, 2011), the CAISO set forth its process for integrating the *BPA* refund shortfall allocation with the allocation of cost recovery offsets, both of which the Commission required the CAISO to allocate based on market participants' "net refunds." The CAISO explained that because the cost recovery offsets are allocated based solely on the result of the MMCP rerun, the CAISO

²¹ San Diego Gas & Elec. Co., 127 FERC ¶ 61,250 at P 46 (2009) ("June 18, 2009 Order").

²² California Parties Motion at 7.

would allocate cost offsets first and then use those results, as well as the results of the fuel cost and emissions offsets, as the basis for allocating the *BPA* refund shortfalls.

The California Parties now contend that the CAISO has “the order wrong,” and should have calculated the cost recovery offset after the *BPA* shortfall calculation and allocation.²³ Although the California Parties discuss this as a question of “order,” the central issue is how best to resolve the fact that the Commission directed the CAISO to allocate both the cost recovery offsets and *BPA* shortfalls based on market participants’ “net refunds.”²⁴ The answer, and the basis for the CAISO’s process, can be found by reading the Commission’s May 12, 2006 Order addressing the allocation of cost recovery offsets²⁵ in conjunction with its October 19, 2007 Order on *BPA* shortfalls. This issue, albeit framed somewhat differently, was previously addressed by the California Parties and CAISO in the context of the California Parties’ December 18, 2007 Motion for Clarification on Specified Rerun Calculations and Allocations.

²³ In their comments on the CAISO’s *BPA* results, the California Parties did not assert that the CAISO had allocated the cost recovery offsets and *BPA* shortfalls in the wrong order, but rather, pointed out the challenges in attempting to allocate all of the various offsets to cross-market hourly results. The CAISO agrees with this sentiment, and it further demonstrates that the CAISO’s process is based on the most logical reading of the Commission’s orders, because it avoids any challenges associated with attempting to perform a cross-market hourly allocation.

²⁴ This distinction is not merely semantic. For instance, the California Parties note that they previously filed a motion raising the issue of whether the refund offset relating to the cost of fuel incurred by generators “should be applied prior to the cost offset allocation,” and suggest that although the Commission has not ruled on this motion, the June 18, 2009 Order in these proceedings “makes clear that the fuel adder allocation should come before the cost offset allocation. The CAISO agrees that the June 18, 2009 Order required the calculation of the fuel cost offset first, insofar as it directed the CAISO to add any fuel cost amounts allocated to sellers with cost recovery offsets to that seller’s cost recovery offset before allocating those offsets to net refund recipients. As explained on page 12 of its Forty-Sixth status report, the CAISO complied with this directive. However, this does not mean that the Commission intended the CAISO to include the allocation of fuel costs in determining net refunds, for purposes of allocating the cost recovery offsets. As explained below, and in the CAISO’s response to the California Parties’ earlier motion, the Commission made clear in its May 12, 2006 Order addressing cost recovery filings that the allocation of the approved cost recovery amounts should be performed based on the MMCP results alone.

²⁵ *San Diego Gas & Elec. Co.*, 115 FERC ¶ 61,171 (2006) (“May 12, 2006 Order”).

As the CAISO explained in its response to that motion, even though the Commission used the term “net refunds,” in both the May 12, 2006 and October 19, 2007 Orders, the CAISO concluded that the Commission used this term to mean different things in the different orders. In the May 12, 2006 Order, the Commission used the term to mean a participant’s refund position based solely on the results of the MMCP rerun, before accounting for offsets for fuel cost and emissions.²⁶ In contrast, the Commission’s October 19, 2007 Order directed the CAISO and PX to allocate the *BPA* shortfall as a “pro rata reduction to refund recipients based on their *final* net refund position in relation to total net refunds.”²⁷ The reference to “*final* net refund position[s]” clearly encompasses all of the adjustments to participants’ refund positions, including any relevant offsets. This difference in usage reflects the fact that “net refunds” is not a term of art that has the same meaning regardless of context, but merely a description of the different calculations and goals in the two orders. Based on the definition in the May 12, 2006 Order, the CAISO believes that the Commission intended it to allocate cost recovery offsets based solely on MMCP results, and then combine those results with the results from allocating the other offsets to arrive at market participants’ final net refund positions, which, in accordance with the October 19, 2007 Order, the CAISO used as the basis for allocating the *BPA* refund shortfalls.

²⁶ *Id.* at P 34 (stating that net refund positions would be determined by “netting each market participant’s refund obligation (amount of energy sold at prices above the MMCP) with its refund receipt (amount of energy purchased at prices above the MMCP)”). See also Response of the California Independent System Operator to California Parties’ Motion for Clarification on Specified Rerun Calculations and Allocations and Request for Additional Time to Respond to Issues Regarding Fuel Cost and Emissions Offsets, Docket Nos. EL00-95-164, et al. (January 2, 2008) at 2-4.

²⁷ October 19, 2007 Order at P 39.

The California Parties do not explain how the Commission's orders provide for a different result. Instead, they rest their argument on the bare assertion that the CAISO's process will lead to inequitable results because some governmental entities will not be required to pay a share of the cost recovery offsets. This "equity" argument is contingent on the California Parties' interpretation of "net refund recipients," which as explained above, is incorrect with respect to the allocation of cost recovery offsets versus *BPA* shortfalls. There is no inequity involved in the results of the CAISO's calculations because the Commission did not contemplate that "net refund recipients," for purposes of allocating cost recovery offsets, would factor in the *BPA* adjustments. If the California Parties believe that the Commission's orders in these proceedings lead to inequitable results, then the appropriate mechanism for expressing those concerns was through a request for rehearing of those orders. Raising the issue of "equity" now is, in effect, a collateral attack on the Commission's orders, and should be rejected.

Moreover, the California Parties' preferred process is no less vulnerable to an argument regarding equities. For instance, the California Parties concede that fuel costs should be factored into the allocation of *BPA* shortfalls "because they impact the amount of refunds that are owed to any buyer on account of its sales in any hour, and thus failure to consider them in the Bonneville Shortfall calculation will yield incorrect net refund amounts in the Bonneville Shortfall calculation and allocation in that hour."²⁸ Yet the same can be said of cost recovery offsets, because they also "impact the amount of refunds that are owed to any buyer." Thus, if the *BPA* shortfalls and cost recovery allocations were instead performed in the order requested by the California Parties, the

²⁸ California Parties' Motion at 10.

result would be inequitable under the California Parties' own rationale, as it would require the CAISO to allocate the *BPA* shortfalls without considering the impact of cost recovery offsets on participants' net refund positions. Put another way, one of the two offsets – for cost recovery amounts or for the *BPA* shortfalls – must be allocated first, and the California Parties' equitableness argument would apply with equal force to either approach. Accordingly, it does not provide a basis for requiring the CAISO to perform its calculations differently.

III. CONCLUSION

For the reasons set forth herein, the CAISO requests that the Commission deny the California Parties' motion, or, alternatively, defer ruling on the motion until such time as the Commission considers and rules on the CAISO's refund rerun compliance filing.

Respectfully submitted,

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Dated: August 10, 2015

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of this document upon the email listserv established by the Commission for this proceeding.

Dated this 10th day of August, 2015 in Washington, DC.

/s/ Michael Kunselman

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