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August 17, 2004

The Honorable Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

**Re: San Diego Gas & Electric Co., et al.
Docket Nos. EL00-95-081, et al.**

Dear Secretary Salas:

Enclosed please find one original and fourteen copies of the Compliance Filing of the California Independent System Operator Concerning the Allocation of Fuel Cost Allowance.

Also enclosed are two extra copies of this cover letter to be time/date stamped and returned to us by the messenger. Thank you for your assistance. Please contact the undersigned if you have any questions regarding this filing.

Sincerely,



Michael Kunselman

Counsel for the California
Independent System Operator Corporation

Enclosures

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

San Diego Gas & Electric Company,)	
Complainant,)	
)	
v.)	Docket Nos. EL00-95-081
)	EL00-95-074
Sellers of Energy and Ancillary Services)	EL00-95-086
Into Markets Operated by the California)	
Independent System Operator and the)	
California Power Exchange,)	
Respondents.)	
)	
Investigation of Practices of the California)	
Independent System Operator and the)	Docket Nos. EL00-98-069
California Power Exchange)	EL00-98-062
)	EL00-98-073

**COMPLIANCE FILING OF THE CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CONCERNING THE ALLOCATION OF FUEL COST
ALLOWANCE**

Pursuant to the Commission's directive in Paragraph 60 of its May 12, 2004 Order Addressing Fuel Cost Allowance Issues, 107 FERC ¶ 61,160 (2004) ("Fuel Cost Order"), the California Independent System Operator Corporation ("ISO") hereby provides this compliance filing detailing its proposed methodology for allocating fuel cost allowance amount during the October 2, 2000 through June 20, 2001 period ("Refund Period").

In the Fuel Cost Order, the Commission found that fuel cost allowance costs should not be assessed based on Control Area Gross Load. Instead, the Commission determined that the recovery of the fuel cost allowance should be assigned to "those that relied on the energy sales spot market to serve load."

Fuel Cost Order at P 60. The Commission directed the ISO to devise a methodology consistent with this principle, and pointed to two options suggested by NCPA that appeared to achieve this result.

The ISO has devised a methodology for allocating fuel allowance costs consistent with the Commission's directive in Paragraph 60 of the Fuel Cost Order. A detailed discussion of the ISO's proposed methodology, along with applicable equations, is included with this filing as Attachment A. This pleading briefly outlines that methodology, and highlights one important unresolved issue relating to the submission and allocation of fuel cost allowances.

I. METHODOLOGY FOR ALLOCATING FUEL COST ALLOWANCES

A. Outline of Methodology

The ISO's proposes a five-step methodology in order to allocate fuel allowance costs consistent with the Commission's requirement that those amounts be allocated to those entities that relied on spot market energy sales to serve load. This process will take place outside of the ISO's settlement rerun, but will be applied prior to the calculations of interest and final net amounts owed by and owing to each entity.

First, the ISO proposes to calculate the total net California Power Exchange ("PX") day-ahead and hour-ahead purchases for each participant for each applicable time interval.¹ This means that each participant's mitigated

¹ As discussed below, the ISO supports receiving and allocating fuel cost allowances on an hourly basis. Although it can perform this methodology using other time intervals, such as daily or monthly, using a lengthier interval will result in a less accurate assignment of costs.

sales² will be subtracted from its purchases for each time interval, to arrive at a net position. Those entities with zero or less net purchases will not be allocated a share of the fuel cost allowance costs for that interval. Next, the ISO plans to calculate the total net ISO spot market purchases for each participant for each applicable time interval, in the same manner as it calculated total PX sales.

Third, the ISO will total the net PX spot market purchases with net ISO spot market purchases, resulting in a total spot purchase amount for each participant. Next, the ISO proposes to divide each participant's total net spot market purchases for each applicable time interval by the total spot market purchases made by all entities during each time interval, in order to determine each participant's proportional share of the spot market purchases for each time interval.

Finally, the ISO will allocate the total amount of approved fuel cost allowances for each time interval based on each participant's share of the total spot market purchases made during those intervals, as determined in Step 4 above.

B. Time Interval for Allocation and Granularity of Data Received from Suppliers

One issue that has been unresolved up until this point is the question of which time interval to use in the allocation of fuel cost allowance amounts. As explained in Attachment A, the ISO believes that an hourly allocation of fuel cost allowances is most consistent with the Commission's Fuel Cost Order, as well as

² The ISO does not plan to include transactions exempt from mitigation in its netting calculation.

principles of cost causation. If the Commission does not agree with the ISO, however, the ISO's methodology can employ a different time interval, such as daily or monthly.

A closely associated issue is the granularity of the fuel cost allowance data that the ISO receives from suppliers. Simply put, the ISO cannot allocate fuel cost amounts based on a time interval that is shorter than the time interval by which the data is provided. In the Fuel Cost Order, the Commission proposed that suppliers provide fuel cost allowance amounts to the ISO on a monthly basis, and requested that the ISO inform the Commission if this format meets the ISO's needs. In a responsive pleading filed on May 24, 2004, the ISO stated that this format most likely met the ISO's needs, but that the ISO could not be certain until such time as it devised the methodology which is the subject of the instant filing, and that the ISO would advise the Commission at the time it submitted this methodology.³

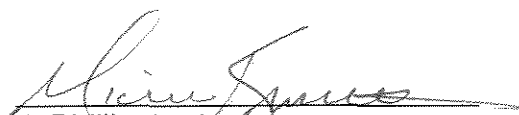
If the ISO receives fuel cost allowance data from suppliers on a monthly basis, the ISO will not be able to allocate those amounts to spot market purchasers in a time interval of less than a month (*i.e.* daily or hourly). Because the ISO believes that the most appropriate time interval for allocation of fuel cost allowance amounts is hourly, and in order to do so, the ISO must receive fuel cost data on an hourly basis, the ISO proposes that suppliers be required to submit their fuel cost allowance data to the ISO on an hourly basis.

³ Report of the California Independent System Operator on Emissions Offsets and Fuel Cost Allowance, Docket Nos. EL00-95-081, *et al.* (May 24, 2004).

II. CONCLUSION

The ISO respectfully requests that the Commission accept this filing, and find that it satisfies the Commission's directive that the ISO devise a methodology for allocating fuel cost allowance amounts to those purchasers that relied on spot market energy sales to serve load, as set forth in Paragraph 60 of the Fuel Cost Order.

Respectfully submitted,



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Dated: August 17, 2004

ATTACHMENT A

California ISO's Proposed Methodology for Allocation of Fuel Cost Allowance to Buyers of Spot Market Energy

I. Background

The Commission's May 12, 2004 Order Addressing Fuel Cost Allowance Issues, 107 FERC ¶ 61,166 (2004) ("Fuel Cost Order"), rejected allocation of fuel cost allowances based on gross load. Fuel Cost Order at PP 59-60. Therein, the Commission explained:

"The fuel cost allowance applies to spot market gas purchases made for spot market energy sales. Accordingly, we find that the recovery of the fuel cost allowance should be assigned to those that relied on the energy sales spot market to serve load. We direct the CAISO to devise a method that follows this principle...."

II. General Methodology

The ISO recommends that the general methodology for allocating fuel cost allowances to buyers of spot market energy incorporate the following elements.

- **Allocation of Fuel Cost Allowance and Charges Outside of ISO/PX Settlement Systems.** The allocation of fuel cost allowances should be applied externally to ISO/PX settlement system reruns, after settlement reruns, and prior to calculations of interest and final net amounts owed to and from each entity.¹ With this approach, two additional potential charges/credits for each entity would be included in the final calculation of "who owes what to whom": a Fuel Cost Allowance ("FCA"), approved by the Commission, and a Fuel Cost Charge ("FCC") representing the share (if any) of all FCA charges to be assessed to each entity purchasing energy in the PX or ISO spot markets. This approach also provides for increased transparency, as all PX and ISO settlement data and calculations used in the allocation to buyers of FCA charges approved by the Commission can be provided to parties for review.
- **Combination of PX and ISO Spot Markets.** Each entity's purchases in the PX and ISO spot market should be combined in calculating total spot market purchases. Because of portfolio scheduling in the PX and strategies which involved the circulation of energy from

¹ The May 12 Fuel Cost Order specifically directed the ISO to consider two options proposed by NCPA: (1) fuel cost allowance allocated on an hourly basis to those entities receiving refunds as a result of their spot market purchases, or (2) offset of fuel cost allowance against the refund liabilities of individual sellers. The ISO notes that these two approaches are not mutually exclusive, in that any methodology must ultimately offset FCA amounts against refunds owed by sellers and also adjust refunds received by other entities by an equal amount. The key issue with any methodology is whether these adjustments are made as an integral part of the ISO and PX settlement process, or as an additional adjustment to be made after re-calculations performed through the ISO and PX settlement systems. The ISO proposes the latter approach as the most appropriate and least problematic, and therefore provides a general methodology consistent with this approach.

the PX to the ISO market, allocation of costs between the ISO and PX for suppliers is often arbitrary. Similarly, the relative proportion of an entity's purchases in the PX versus ISO market is not a reasonable indicator for who should bear responsibility for costs incurred to meet overall market needs. Thus, each entity's purchases in the PX and ISO spot markets should be combined in calculating total spot market purchases.

- **Netting of Spot Market Sales from Purchases.** Net spot market purchases in the PX and ISO markets for each entity should be calculated by subtracting any sales in these markets from any purchases made by the same entity during the applicable time period (see below). Such "netting" is necessary to account for the fact that PX and ISO settlement data include both sales and purchases of spot market energy during the same time period for many entities. The IOUs, for instance, sold their supply into the PX Day Ahead market and then purchased it back through PX purchases. In the ISO billing process, sales and purchases of uninstructed energy by each Scheduling Coordinator's load and resources are combined into a single Uninstructed Energy amount for which each Scheduling Coordinator is charged or paid. Since total refunds owed to and by participants are ultimately based on net sales and purchases in the PX and ISO spot markets, such netting of spot market sales and purchases should also be done in calculating net purchases that should be subject to any FCA charges.
- **Block Forward and Other Excluded Transactions.** PX and ISO sales and purchases that are excluded from refund calculations should also be excluded from the calculation of net purchases subject to any FCA charges. This includes purchase and sales volumes in the PX Day Ahead market associated with positions in the PX block forward market, and any sales in the ISO markets pursuant to contracts with a duration of 24 hours or longer, or found to have been made pursuant to 202(c) of the Federal Power Act. Again, since these transactions are not included in calculation of total refunds owed to and by participants, it follows that these transactions should also be excluded from the calculation of net spot market purchases that should be subject to any FCA charges.²
- **Allocation of ISO Settlement Data for Entities Represented by PX as Scheduling Coordinator.** While the PX was in operation (through January 2001), the PX served as Scheduling Coordinator ("SC") in the ISO markets for a variety of participants, including California's major IOUs. Thus, in order to allocate FCA charges directly to entities for which the PX served as SC, all ISO settlement data for which the PX is the SC must be linked back to the PX participant responsible for the actual load or supply resource with which these ISO transactions are associated. In response to a request from the ISO for assistance in this process, the PX has recommended that the ISO perform this allocation, and has provided a master file that may be used to link ISO transactions to the specific PX participants responsible for the actual loads or supply resources. The ISO is currently linking this PX master file to ISO settlement data from the preparatory re-run, in order to

² For example, assume that for a given hour a load serving entity had total purchases of 300 MWs in the PX Day Ahead market, 100 MW of which represented a Block Forward market purchase that was excluded from refund calculations. Since the entity would receive refunds for only 200 MW of PX purchases (and the seller of the 100 MW Block Forward Contract would not owe refunds for this 100 MW), this 100 MW should also be excluded from the quantity of spot market purchases used to calculate the load serving entity's FCA charges.

verify the ISO's ability to perform this calculation with the data that has been provided by the PX.³

- **Aggregation of Transactions is Necessary for Some Entities.** For some participants, such as the California IOUs, there may be several different PX and ISO identification numbers that should be aggregated to develop an overall net position. For example, PG&E appears to have transactions under four different PX participant identifiers: PGAE, PGEU, PGPG and PGEX.
- **Applicable Time Interval.** Allocation of FCA amounts approved by the Commission should be allocated to buyers based on the net MWh of purchases made by each entity in both PX and ISO spot markets during some time interval (e.g., hourly, daily, monthly). Although the calculations set forth below can be performed using any one of these time intervals, the ISO believes it would be most appropriate to allocate approved FCA amounts on an hourly basis. Hourly allocation would result in the most accurate assignment, consistent with the principle of cost causation, of FCA costs to purchasers "that relied on the energy sales spot market to serve load." Fuel Cost Order at P 60. Also, the Fuel Cost Order mentions as one apparently reasonable alternative the allocation of fuel cost allowances on an hourly basis. *Id.*

It is important to understand that the ISO cannot allocate approved FCA amounts based on a time interval that is shorter than the time interval on which the data is provided. For instance, if the Commission agrees that it is appropriate to allocate FCA amounts to purchasers on an hourly basis, then the ISO must receive FCA amounts from suppliers on an hourly basis. The ISO could not, for example, allocate FCA amounts on an hourly basis if it receives FCA data aggregated only by month. Therefore, consistent with its belief that approved FCA amounts should be allocated on an hourly basis, the ISO believes that sellers should calculate and provide their FCA claims broken down by each hour during the refund period, rather than monthly.

³ The master file provided by the PX has over 1 million records, which must be linked with several hundred thousand ISO settlement records for real time energy transactions for which the PX is listed as the SC.

III. Methodological Details

Provided below is a more detailed, step-by-step description of the approach proposed by the ISO for allocating FCA charges approved by the Commission to buyers of spot market energy in the PX and ISO spot markets.

1. Total Net PX Purchases for Each Time Interval

First, total net purchases in the PX Day Ahead and Hour Ahead markets can be calculated as follows for each participant p in each time interval t :

$$\text{Net PX}_{p,t} = \text{DA/HA Purchases}_{p,t} - \text{DA/HA Sales}_{p,t} - (\text{BFM Position}_{p,t})$$

Where:

DA/HA Purchases_{p,t} = Sum of all Final PX Day Ahead and Hour Ahead Scheduled Quantities (Sched_MW) where Demand_Supply = 'D' (includes all schedules where Resource Type = "Export" and "SC Transfer Out")

DA/HA Sales_{p,t} = Sum of all Final PX Day Ahead and Hour Ahead Scheduled Quantities (Sched_MW) where Demand_Supply = 'S' (includes all schedules where Resource Type = "Import", "SC Transfer In", and "Generating Unit")

BFM Position_{p,t} = Net final position in PX Block Forward market for the relevant month, for all time intervals t included in hours covered by BFM contracts (Hours Ending 7-22, Monday through Saturday, excluding NERC holidays). A positive value indicates a *net purchase* of energy in the BFM by the participant during the relevant month, while a negative value indicates a *net sale* of energy in the BFM by the participant during the relevant month.

2. Total Net ISO Spot Market Purchases for Each Time Interval

For each participant p in each time interval t :

$$\text{Net ISO}_{p,t} = \text{Instructed Energy}_{p,t} + \text{Uninstructed Energy}_{p,t}$$

Where:

Instructed Energy_{p,t} = Sum of the final Billable Quantity for all Instructed Energy transactions (Charge Code = 401) from the ISO settlement records from the preparatory rerun (SS_Details). This includes incremental instructed energy (Billable Quality < 0) as well as decremental instructed energy (Billable Quality > 0).

Uninstructed Energy_{p,t} = Sum of the final Billable Quantity for all Uninstructed Energy transactions (Charge Code = 401) from the ISO settlement records from the preparatory rerun (SS_Details). This includes positive uninstructed energy (Billable Quality < 0) as well as decremental uninstructed energy (Billable Quality > 0). Includes uninstructed energy amounts for loads, generating resources, and imports/exports.

As noted above, transactions that are exempt from mitigation are also excluded from this calculation.

Also, as previously noted, instructed and uninstructed energy associated with participants with the PX as their SC must be calculated based on links between PX participant identifiers and ISO resource IDs in the master data provided by the PX.

ISO data for each 10-minute interval must be aggregated to the hourly level in order to combine these data with the PX data (which is hourly).

3. Total Net Spot Market Purchases Each Time Interval

$$\text{Net Spot Market Purchases}_{p,t} = \text{Net PX}_{p,t} + \text{Net ISO Purchases}_{p,t}$$

4. Calculate Each Participant's Share of Spot Market Purchases for Each Time Interval

$$\text{FCC_Pct}_{p,t} = \frac{\text{Net Spot Market Purchases}_{p,t}}{\sum \text{Net Spot Market Purchases}_{p,t}}$$

Where:

$$\text{Net Spot Market Purchases}_{p,t} > 0$$

5. Allocate Total Fuel Cost Allowances based on Participant's Share of Spot Market Purchases

Sum all FCA associated with mitigated sales of energy in the PX and ISO spot markets to be recovered by each generator (g) in each time interval (t) to determine total FCA (FCA_t), which is allocated to entities relying on imbalance energy from the ISO's real time market for time interval (t)

$$FCA_t = \sum_g FCA_{g,t}$$

Then calculate each participant's Fuel Cost Charge ($FCC_{sc,t}$) or total share of the FCA_t for each time interval t :

$$FCC_{p,t} = FCA_t \times FCC_Pct_{p,t}$$

Where:

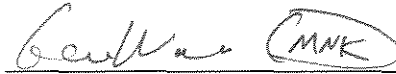
$FCC_{p,t}$ = Fuel Cost Charge (FCC) allocated to each participant p
in each time interval t

FCA_t = Sum of Fuel Cost Allowance (FCA) approved by FERC
for all sellers for time interval t

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list for the captioned proceeding, in accordance with Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, CA, on this 17th day of August, 2004.


Gene L. Waas