



# Memorandum

**To:** ISO Board of Governors

**From:** Ryan Seghesio, Vice President, Chief Financial Officer & Treasurer

**Date:** December 11, 2019

**Re:** **Decision on 2020 budget**

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***This memorandum requires Board action.***

This memorandum summarizes the final 2020 GMC revenue requirement proposal that the Board is requested to approve and which will become effective January 1, 2020. A high-level review of the key budget sections follows in the discussion and analysis section; however, a more detailed description and review of the budget can be found in the 2020 Budget and Grid Management Charge Rates book, included as *Attachment A*.

At \$187 million, the proposed GMC revenue requirement is the lowest revenue requirement since 2006. The proposed amount is \$6.5 million less than the 2019 GMC revenue requirement. By diversifying revenue streams through efforts such as Reliability Coordinator services and EIM, the ISO is able to develop well-rounded budgets for its capital and operational needs all at an overall lower cost to its stakeholders.

Management recommends the following motion:

***Moved, that the ISO Board of Governors approves the 2020 GMC revenue requirement, capital/project budget, and resulting rates as set forth in Attachment A to the memorandum dated December 11, 2019.***

## DISCUSSION AND ANALYSIS

The annual revenue requirement is an integral component of the ISO's planning process and reflects the priorities and commitments made in the ISO's strategic vision.

The 2020 GMC revenue requirement, at \$187 million, is approximately \$15 million less than the FERC-approved \$202 million cap. This amount is \$6.5 million (or 3.4%) lower in comparison to the 2019 GMC revenue requirement. The ISO projects that the 2020 transmission volume will decrease to 238.4 terawatt-hours (TWh), which results in a

bundled cost per megawatt-hour (MWh) of \$0.7844, or a decrease of \$0.0229 per MWh from 2019.

The GMC revenue requirement has five components:

- Operating and maintenance (O&M) budget
- debt service;
- cash funded capital;
- other costs and revenues; and
- operating cost reserve adjustment from prior year.

A summary of the 2020 GMC revenue requirement compared to 2019 is as follows.

<b>GMC Revenue Requirement (\$ in millions)</b>	<b>2020 Budget</b>	<b>2019 Budget</b>	<b>Change \$</b>	<b>Change %</b>
Operations & Maintenance Budget	\$195.0	\$189.0	\$6.0	3.2%
Debt Service (including 25% reserve)	16.9	16.9	0.0	0.0%
Cash Funded Capital	28.0	25.0	3.0	12.0%
Other Costs and Revenues	(41.3)	(23.9)	(17.4)	72.8%
Operating Costs Reserve Adjustment	(11.6)	(13.5)	1.9	-14.1%
<b>Total GMC Revenue Requirement</b>	<b>\$187.0</b>	<b>\$193.5</b>	<b>(\$6.5)</b>	<b>-3.4%</b>
Transmission Volume Estimate in TWh	238.4	239.7	(1.3)	-0.5%
<b>Pro-forma bundled cost per MWh</b>	<b>\$0.7844</b>	<b>\$0.8073</b>	<b>(\$0.0229)</b>	<b>-2.8%</b>

### ***Operating and Maintenance Budget***

The O&M budget is the largest component of the revenue requirement; it accounts for the majority of the total revenue requirement. The 2020 proposed O&M budget is \$195 million, representing a \$6 million, or 3.2%, increase over 2019. The 2020 Budget and Grid Management Charge Rates book, included as *Attachment A*, presents the O&M budget in three different perspectives: delivery of services (objectives and processes), utilization of resources, and divisional costs.

A summary of the 2020 O&M budget by resource compared to 2019 is as follows.

<b>O&amp;M Budget by Resource (\$ in millions)</b>	<b>2020 Budget</b>	<b>2019 Budget</b>	<b>Change</b>
Salaries and Benefits	\$145.6	\$141.2	\$4.4
Occupancy Costs and Equipment Leases	2.9	2.9	-
Telecom, HW/SW Maintenance Costs	14.4	14.5	(0.1)
Consultants and Contract Staff	12.5	11.8	0.7
Outsourced Contracts and Professional Fees	12.0	11.1	0.9
Training, Travel, and Other costs	7.6	7.5	0.1
<b>Total</b>	<b>\$195.0</b>	<b>\$189.0</b>	<b>\$6.0</b>

- The salaries and benefits category will increase primarily due to merit increases offset slightly by a reduction in overtime expense.
- The occupancy costs and equipment category will remain flat in 2020.
- The telecommunications and hardware and software maintenance category will decrease slightly due to reduced negotiated telecommunication costs.
- The consultants and contract staff category will increase due to need for additional outsourced resources.
- The outsourced contacts and professional fees will increase due to additional outsourced tools to support efforts such as EIM and Reliability Coordinator services.
- The travel, training and other costs category will increase primarily due to the planned stakeholder symposium in 2020.

### ***Debt Service***

The debt service component of the 2020 GMC revenue requirement will remain at \$16.9 million. Debt service includes the principal and interest amounts due, plus the required 25-percent reserve. The outstanding bond principal going into 2020 is \$163.4 million.

A summary of debt service is as follows.

<b>Debt Service (\$ in millions)</b>	<b>2020 Budget</b>	<b>2019 Budget</b>	<b>Change</b>
Principal payments	\$5.4	\$5.2	\$0.2
Interest payments	8.1	8.3	(0.2)
<b>Subtotal</b>	<b>13.5</b>	<b>13.5</b>	<b>-</b>
25% debt service reserve	3.4	3.4	-
<b>Total Debt Service</b>	<b>\$16.9</b>	<b>\$16.9</b>	<b>\$-</b>

### ***Capital and Project Budget / Cash Funded Capital***

The proposed GMC revenue requirement includes a collection of \$28 million for cash-funded capital.

The 2020 capital/project budget is requested to be set at \$22 million. The current list of proposed projects that would consume the \$22 million budget is contained in *Attachment A*. These projects, and other proposed projects, will continue to be prioritized in 2020 under the ISO's capital/project approval process.

The excess capital amount collected, or \$6 million, will be contributed to the long-term capital reserve. The reserve contributes to the ability of the ISO to offer stable GMC revenue requirements year over year.

### ***Other Costs and Revenues***

Other revenue will increase \$17.4 million to \$41.3 million in 2020 primarily driven by the addition of the Reliability Coordinator Funding Requirement and additional EIM participants joining in April 2020 as well as higher anticipated forecasting revenue and interest earnings. These revenue items help bring the revenue requirement below the \$202 million FERC-approved cap.

A summary of other costs and revenues is as follows.

<b>Other Costs and Revenue (\$ in millions)</b>	<b>2020 Budget</b>	<b>2019 Budget</b>	<b>Change</b>
Reliability Coordinator Funding Requirement	\$18.5	\$4.3	\$14.2
Energy Imbalance Market Administrative Charges	9.5	8.6	0.9
Intermittent Resource Forecasting Fees	4.5	3.8	0.7
Interest Earnings	3.9	3.3	0.6
California-Oregon Intertie Path Operator Fees	2.0	2.0	-
Generation Interconnection Project Fees	1.4	1.5	(0.1)
HANA Administrative Fees	0.9	-	0.9
Scheduling Coordinator Application and Other Fees	0.6	0.4	0.2
<b>Total Other Costs and Revenue</b>	<b>\$41.3</b>	<b>\$23.9</b>	<b>\$17.4</b>

### ***Operating Cost Reserve Adjustment***

The operating cost reserve adjustment is primarily the cumulative result of the actual results versus the budgeted revenue requirement and the 25% debt service reserve collection from the prior year. For 2020, the ISO forecasts a credit from the operating reserve account of \$11.6 million based on the trued-up activity from 2018.

As with other revenue, this credit adjustment helps bring the revenue requirement below the \$202 million cap.

A summary of the operating reserve adjustment is as follows.

<b>Operating Cost Reserve Adjustment (\$ in millions)</b>	<b>2020 Budget</b>	<b>2019 Budget</b>	<b>Change</b>
Change in the 15% reserve for O&M budget	(\$0.9)	(\$1.6)	\$0.7
25% debt service collection from prior year	3.4	3.4	(0.0)
True-up of budget to actual revenues and other	9.1	11.7	(2.6)
<b>Total Operating Cost Reserve Credit / (Debit)</b>	<b>\$11.6</b>	<b>\$13.5</b>	<b>(\$1.9)</b>

**Grid Management Charge Rates, Fees, and Charges**

A comparison of the proposed 2020 rates and 2019 rates is as follows (\$ per unit).

<b>Summary of Rates (\$ per MWh)</b>	<b>2020 Rate</b>	<b>2019 Rate</b>	<b>Change \$</b>
<b>Grid Management Charges</b>			
Market Service Charge	\$0.0994	\$0.1065	(\$0.0071)
Systems Operations Charge	\$0.2788	\$0.2797	(\$0.0009)
CRR Services Charge	\$0.0078	\$0.0100	(\$0.0022)
<b>Supplemental Services Rates</b>			
EIM Market Service	\$0.0785	\$0.0841	(\$0.0056)
EIM System Operations	\$0.1087	\$0.1091	(\$0.0004)
RC Service Rate	\$0.0278		

The EIM administrative charges are derived from the GMC rates. As established in the latest cost of service study, EIM entities pay 79% of the market services rate and 39% of the system operations rate.

All miscellaneous fixed fees remain the same.

**Budget Process**

The ISO has provided several opportunities for public review and comment on the draft budget. This public input process commenced with a July budget kickoff meeting with stakeholders and followed with a stakeholder call held in November. The ISO posted materials from the meetings as well as stakeholder comments and ISO responses on its website. The stakeholder comments consisted of clarifying questions regarding items such as planned 2020 projects, operating cost reserve adjustment drivers, debt service usage, along with general O&M questions; the consensus was the stakeholders were supportive of the GMC revenue requirement. With Board approval, the ISO will post the proposed GMC rates on its website to be effective on January 1, 2020.

It should be noted that post-decision minor adjustments are sometimes required to align line items within the O&M budget due to final year-end headcount and cost center reorganizations. These year-end adjustments will not affect the final total approved budget.

## ***Conclusion***

The proposed 2020 GMC revenue requirement will provide sufficient funding to enable the ISO to deliver on the commitments it made to achieve its vision while still maintaining costs for stakeholders. Therefore, Management recommends that the Board approve the GMC revenue requirement attached to this memorandum.