

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

San Diego Gas & Electric Company)	Docket Nos. EL00-95-000
v.)	<i>et al.</i>
Sellers of Energy and Ancillary Services)	
)	
Investigation of Practices of the California)	Docket Nos. EL00-98-000
Independent System Operator and the)	<i>et al.</i>
California Power Exchange)	
)	

**COMMENTS OF THE CALIFORNIA INDEPENDENT
SYSTEM OPERATOR CORPORATION CONCERNING
JOINT OFFER OF SETTLEMENT INVOLVING
THE AUTOMATED POWER EXCHANGE**

Pursuant to Rule 602(f) of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (“Commission”), 18 C.F.R. ¶ 385.602(f) (2006), and the Commission’s “Notice of Filing” issued on January 10, 2007 in the above-captioned dockets, the California Independent System Operator Corporation (“CAISO”)¹ hereby submits its comments on the Joint Offer of Settlement (“APX Settlement”) filed between a number of participants in markets operated by the Automated Power Exchange (“APX”) (collectively, the “Settling Parties”)² in the above-captioned proceedings on January 5, 2007.

¹ Capitalized terms not otherwise defined herein are used as defined in Appendix A to the ISO Tariff, or in the APX Settlement and Release of Claims referred to in the text.

² The Settling Parties consist of APX, American Electric Power Service Corp., Avista Energy, Calpine Energy Services, El Paso Marketing, UC Davis Medical Center, Merrill Lynch Capital Services, BP Energy, Tractebel Energy Marketing, Aquila Merchant Services, Salt River Agricultural Improvement and Power District, Allegheny Energy Supply Company, TransAlta Energy Marketing, Sempra Energy Solutions, Constellation NewEnergy, Commonwealth Energy Corporation, Sacramento Municipal Utility District, Morgan Stanley Capital Group, Enron Energy Services, Enron Power Marketing, Sierra Pacific Industries, Coral Power, and Puget Sound Energy.

I. COMMENTS

A. The APX Settlement Directly Affects the ISO's Interests

The ISO is a non-profit public benefit corporation organized under the laws of the state of California and is responsible for the reliable operation of the transmission grid comprising the transmission systems of the three investor-owned utilities, and also certain municipalities. The ISO is not a signatory to the APX Settlement. However, the ISO will be responsible for certain aspects of the financial implementation of this settlement, and pursuant to the terms of the APX Settlement, will be required to reflect the financial consequences of the APX Settlement on its books of account. Therefore, the ISO has a direct and substantial interest in the Commission's treatment of the APX Settlement.

B. The ISO Supports the APX Settlement Subject to Certain Qualifications

The ISO has always supported the general principle that the end to complex litigation through settlement is the preferred process as opposed to the continuation of that litigation for all litigants, or for even a selected subset of the litigants. In addition, this Commission has consistently encouraged parties to resolve disputes whenever possible through settlement.³ The refund proceeding has now been ongoing for over five years. Against this backdrop, the ISO continues to support the general principle of settlement as embodied in the APX Settlement. The approval of the proposed APX Settlement will allow the resolution of long-standing issues sooner than would otherwise be the case.

³ *Cities of Anaheim, Azusa, Banning, Colton, and Riverside, California v. California Independent System Operator Corporation*, 96 FERC ¶ 61,024, at 61,065 (2001).

Nevertheless, as discussed below, the ISO does have several concerns with respect to the APX Settlement. Most of these concerns result from the fact that the settlement at issue is aimed exclusively at resolving claims between and among the APX and its market participants. It does not resolve claims relating to the direct participation of the Settling Parties in the ISO and PX markets. In this respect, the APX Settlement is unique among the settlements that have been filed with and approved by the Commission in this proceeding, and because of this feature, it is particularly important to ensure that other participants in the ISO and PX markets are not adversely impacted as a result of this Settlement.

C. The Distribution to APX Should Reflect the Net of its Balances in the ISO and PX Markets

The ISO's first concern with the APX Settlement regards the mechanism by which funds will be transferred to APX by the ISO and PX. The terms of the APX Settlement provide that upon approval of the Settlement, the ISO and PX will transfer to APX receivables and other amounts owed to APX. However, based on the ISO's most current refund data, APX is a Debtor in the ISO's markets. Specifically, the ISO's current data shows that APX owes the ISO market approximately \$6.1 million. This figure includes all unpaid amounts, refunds, and preparatory rerun adjustments, as well as interest on unpaid amounts and refunds.

The ISO understands, however, that APX is a significant creditor in the PX markets, in the range of approximately \$54 million. Taking into account both its ISO and PX market activities, APX is owed somewhat less than \$50 million. It would be inappropriate for the PX, upon approval of the APX Settlement, to

distribute to APX the full amount that it owes to the APX as a result of APX activity in the PX markets, without making some provision for the amounts owed by APX to the ISO markets. Doing so would clearly harm non-parties to the APX Settlement in that it would give APX and its participants a payment priority over other parties in this proceeding. The ISO does not read the APX Settlement as requiring such a result; the APX Settlement merely states that the ISO and PX will release to the APX “all funds owed to APX.”⁴

In order to solve this potential problem, the PX has agreed, upon approval of the APX Settlement, to distribute a portion of the total amount owed by the PX to APX to the ISO, based on the ISO’s best calculation of what APX owes to the ISO markets at that time. For instance, if at the time the Settlement is approved, the ISO shows APX as owing the ISO markets \$6.3 million, then the PX will distribute to the ISO \$6.3 million from the total amount that the PX owes to APX.⁵ The ISO will hold this amount until such time as the Commission orders a distribution. Under this approach, at the time of distribution, APX will receive the total net amount of money that it is owed based on its activities in both the ISO and PX markets during the period covered by the APX Settlement. The ISO submits that this procedure is the fairest manner of interpreting the ISO and PX obligation to release to APX “all funds owed to APX,” and intends to follow this procedure absent explicit Commission direction to the contrary.

⁴ APX Settlement, Section 4.5.

⁵ As discussed below, APX’s balance with the ISO and PX may change prior to any approval of the APX Settlement. Thus, the numbers discussed herein may change to some degree. However, the theory of payment would remain the same, namely, the PX will pay to the ISO an amount equal to the ISO’s best estimate of what APX owes the ISO.

D. The Distribution to APX Should Reflect a Best Estimate of its Liabilities Based on the Available Data

Another issue that the ISO has with the APX Settlement concerns the viability of the data used to make distributions required pursuant to the terms of the Settlement. Namely, the data concerning APX's position in the ISO markets that the ISO will use to implement the terms of the APX Settlement is unlikely to be final by the March 1, 2007 "drop dead" date for approving the Settlement.⁶ This is the case for several reasons.

First, although the ISO is currently in the process of completing the financial adjustment phase of its refund rerun process, it has yet to finalize and upload calculations concerning the allocation of fuel cost allowances and cost filings, as well as determining interest on those two components. Assuming that the Commission does approve the APX Settlement by March 1, 2007, the ISO may not know the impact of these components on APX.⁷ Although the ISO does not anticipate that APX's position will be dramatically altered by the final calculations on fuel costs and cost filings, there will almost certainly be some change to APX's liabilities in the ISO markets.

Moreover, there are a number of issues arising out of the two Ninth Circuit Court of Appeals decisions concerning this proceeding that have a strong potential to require further adjustments in the positions of market participants

⁶ The Settlement Parties request that the Commission approve the APX Settlement no later than March 1, 2007. In fact, the APX Settlement provides that, absent Commission approval by March 1, 2007, unless the Settling Parties agree to such modification or condition, the APX Settlement will terminate and be of no further force and effect.

⁷ The ISO believes that it will, by March 1, have finished its calculations concerning fuel cost allowances, but is less confident that the calculations regarding cost filings, as well as interest on these two components, will be complete at that time.

during the Refund Period. The ISO cannot even speculate at this time how such adjustments might impact APX's position in the ISO markets.

As a consequence of the fact that APX's final obligations in the ISO markets will almost certainly not be known by the time the APX Settlement is approved, the ISO believes that the directive in the Settlement for the ISO and PX to release to APX "all funds owed to APX," must be interpreted to mean all funds owed to APX based on the best estimate of APX's balances in the ISO and PX markets available at the time the Settlement is approved. This means if the ISO has not completed its calculations concerning the allocation of fuel cost allowances/and or cost filing amounts, as well as associated interest, by the time the Commission approves the APX Settlement, the ISO will use its best efforts and most current data to estimate the financial effects on APX of any outstanding calculations. The ISO will then use this estimate to determine APX's balance with respect to the ISO markets, for purposes of calculating the distribution to APX under the Settlement. The ISO will then perform a "true-up" at the time it invoices the results of this proceeding, which will result in either more money distributed to APX, consistent with the terms of the Settlement, or an additional liability for APX and its participants, which would be treated as explained in Section I.E below.

Barring a Commission order to the contrary, the ISO intends to use this approach in implementing the APX Settlement and reflecting it on its accounts. The ISO also understands that the PX will be proposing in its comments on the APX Settlement that the Commission grant it a 10-business-day window after the

Settlement is approved in order to complete its interest calculations. The ISO supports this proposal, and commits to using this time to further refine its own calculations. Prior to the end of this 10-day period, the ISO will make available to parties in this proceeding its best estimate of APX's then-current balance in the ISO markets. The ISO will use this data to implement the terms of the Settlement.

E. The Commission Should Clarify that the APX Settlement Does Not Absolve the Parties to that Settlement from the Obligation to Pay Additional Amounts that May be Determined to be Owed to the ISO Markets

Although the APX Settlement does address the scenario in which the APX later receives additional monies from the ISO and PX, it appears to be silent with respect to the situation in which adjustments made after the APX Settlement becomes effective result in increased liability to the ISO and/or PX markets. Unlike the various "global" settlements approved by the Commission in this proceeding, there is no provision in the instant Settlement addressing the circumstances under which APX may end up owing additional amounts to the ISO and/or PX, nor is there a provision providing for an escrow to provide financial security if such a situations does occur. This may come about because of the circumstances described above – *i.e.*, due to further calculations by the ISO and PX based on current Commission orders and/or recalculations required as a result of future Commission decisions made under the auspices of Court of Appeals rulings. In any event, the ISO is particularly concerned about receiving full payment of any additional amounts owed. Because the APX Settlement does not address this subject, the ISO requests that in any order approving the APX

Settlement, the Commission confirm that approval of the APX Settlement in no way absolves the APX or its participants⁸ from the obligation to pay any additional amounts, above and beyond those distributed pursuant to the APX Settlement, owed to the ISO and/or PX markets as a result of calculations performed by the ISO and/or PX after approval of the Settlement.

To avoid potential shortfalls in the ISO's markets, it is crucial that the ISO receive any additional monies that might be owed based on calculations performed after the approval of the Settlement. Any such shortfalls may leave the ISO in the position of being unable to clear its markets at the conclusion of these proceedings. The ISO's tariff specifies that any shortfall will be borne by its Market Participants. The result would be to unfairly burden Market Participants that are not a party to the APX Settlement with obligations incurred as a direct result of APX's participation in the ISO Markets. If the APX Settlement is interpreted in a manner so as to allow the APX and its participants to escape liability or payment responsibility for their activities in the ISO Markets, then the Settlement could have an adverse impact on third parties. Therefore, the ISO submits that the silence of the APX Settlement on this issue should be read as not absolving the APX and its participants of any liability they might otherwise have to pay additional amounts determined, after the approval of the Settlement, to be owed as a result of APX's participation in the ISO and PX markets. The

⁸ Pursuant to the Commission's October 16, 2003 "Order on Rehearing," 105 FERC ¶ 61,066 at PP 170-171 (2003), APX participants are directly liable for those refunds where there is sufficient data to permit direct apportionment of liability, and APX and its participants are jointly and severally liable for refunds for which there is insufficient data to determine apportionment.

ISO respectfully requests that the Commission make such a finding in any order approving the APX Settlement.

F. The Commission Should State that the ISO's Directors, Officers, Employees and Consultants Will Be Held Harmless With Respect to the Settlement and Accounting Activities that The ISO Will Have to Perform in Order to Implement the APX Settlement.

As with previous settlements filed and approved in this proceeding, the circumstances of the APX Agreement make it necessary to hold harmless the market operators (*i.e.*, the ISO and PX) that are ultimately tasked with implementing this Settlement,⁹ along with their directors, officers, employees and consultants. Therefore, in any order approving the APX Settlement, the Commission should state that the ISO, along with its directors, officers, employees and consultants, will be held harmless with respect to the settlement and accounting activities that it will have to perform in order to implement the APX Settlement, and that neither the ISO, nor its directors, officers, employees or consultants, will be responsible for recovering any funds disbursed pursuant to the APX Settlement, which are subsequently required to be repaid. As noted above, the Commission has already approved hold harmless language for the

⁹ The ISO has requested hold harmless treatment in comments on previous settlements filed in this proceeding with respect to Duke, Williams, Mirant, Enron, PS Colorado, Reliant, and Idacorp. The Commission has, to date, provided the ISO with hold harmless treatment with respect to all of these settlements. See 109 FERC ¶ 61,257 (2004) (order accepting the Duke settlement), 111 FERC ¶ 61,107 (2005) (order accepting the Mirant settlement), 111 FERC ¶ 61,186 (2005) (order on rehearing of the order approving the Williams settlement), 113 FERC ¶ 61,171 (2005) (order accepting the Enron settlement), 113 FERC ¶ 61,235 (2005) (order accepting the PS Colorado settlement), 113 FERC ¶ 61,308 (2005) (order accepting the Reliant settlement), 115 FERC ¶ 61,230 (order approving the Idacorp settlement). The ISO requests that the Commission approve such language for each such settlement that it has approved, or may approve, in these proceedings.

ISO and the PX in the context of the California Parties' settlements with a number of entities. The factors that justified holding the ISO and PX harmless with respect to the implementation of these other settlements apply with equal force to the APX Settlement.

As with previous settlement agreements in this proceeding, the flow of funds pursuant to the APX Agreement will require unprecedented accounting adjustments on the part of the ISO. These accounting adjustments will not be made under the terms of the ISO Tariff, but rather pursuant to the APX Agreement, the terms of which have been determined by a subset of parties to this proceeding. A Market Participant might file a complaint or bring suit against the ISO, and/or its directors, officers, employees and consultants, claiming that the ISO did not make appropriate accounting adjustments, and as a result did not reflect the appropriate amount of refunds or receivables owing to that Market Participant.

Moreover, because the APX Settlement has been filed prior to the final orders in the refund proceeding, it is not certain that the Settling Parties' estimates of payables and receivables are accurate, and due to the complexity of the settlement, there may be additional, unforeseen impacts to ISO Market Participants. It is possible that such impacts would cause Market Participants to bring actions against the ISO (or its directors, officers, employees and consultants), as a result of the ISO's implementation of the APX Agreement.

These problems may be amplified as the Commission approves more settlement agreements in this proceeding. The Commission has already

approved the settlements reached by Williams, Dynegy, Duke, Mirant, Reliant, Enron, PS Colorado and Idacorp with the California Parties. As the volume of settlements increases, the task of implementing those settlements will become more and more complicated. Likewise, the possibility a party will bring an action against one, or both, of the market operators also increases. For this reason, the ISO believes that it is critically important that the Commission hold the ISO (along with its directors, officers, employees, and consultants) harmless with respect to the implementation of all of the settlements reached in this proceeding that involve the flow of monies through the ISO Markets.

A hold harmless provision would also be appropriate because the ISO is a non-profit public benefit corporation, and it would not be reasonable to subject its officers, employees, and consultants to suits claiming individual liability for engaging in the accounting necessary to implement the APX Settlement. These individuals should not be subjected to litigation, along with its attendant costs and expenditure of time, for merely implementing a settlement authorized by the Commission.

Finally, there is nothing in the APX Settlement that counsels against, or is inconsistent with, granting the ISO and the individuals associated with it the protection requested here.

For these reasons, the Commission, in any order approving the APX Settlement, should state that the ISO, along with its directors, officers, employees, and consultants will be held harmless with respect to the settlement and accounting activities that the ISO will have to perform in order to implement

the APX Settlement, and that neither the ISO, nor its directors, officers, or employees, or consultants will be responsible for recovering any funds disbursed pursuant to the APX Settlement, which are subsequently required to be repaid.

II. CONCLUSION

Wherefore, for the reasons stated above the ISO respectfully states that it supports the APX Settlement and will work with the parties to the Settlement to implement it. The ISO also respectfully requests that the Commission find that approval of the APX Settlement in no way absolves the APX or its participants from the obligation to pay any additional amounts, above and beyond those distributed pursuant to the APX Settlement, owed to the ISO and/or PX markets as a result of calculations performed by the ISO and/or PX after approval of the Settlement. The ISO also requests that the Commission state, in any order approving the APX Settlement, that that the ISO, along with its directors, officers, employees, and consultants will be held harmless with respect to the settlement and accounting activities that it will have to perform in order to implement the APX Settlement, and that neither the ISO, nor its directors, officers, or employees, or consultants will be responsible for recovering any funds disbursed pursuant to the APX Settlement, which are subsequently required to be repaid.

Respectfully submitted,

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Certificate of Service

I hereby certify that I have this day served a copy of this document upon all parties listed on the official service list compiled by the Secretary in the above-captioned proceedings, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated this 19th day of January, 2007 at Folsom in the State of California.

/s/ Daniel J. Shonkwiler

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