



DENNIS J. HERRERA  
City Attorney

THERESA L. MUELLER  
Deputy City Attorney  
DIRECT DIAL: (415) 554-4640  
E-MAIL: [theresa\\_mueller@ci.sf.ca.us](mailto:theresa_mueller@ci.sf.ca.us)

**Comments of the City and County of San Francisco on the ISO's September 20, 2004  
Revised Proposal for Honoring Existing Transmission Contracts**

**October 4, 2004**

The City and County of San Francisco (San Francisco) submits the following comments on the ISO's September 20, 2004 Revised Proposal for Honoring Existing Transmission Contracts (ETC Proposal). San Francisco has participated in every phase of the stakeholder process established to address ETCs following the July 22, 2003 MD02 filing at FERC. More recently, San Francisco reviewed the September 20, 2004 White Paper and participated in the Stakeholder Workshop to discuss the proposal held on September 27, 2004. San Francisco comments only on the proposal presented in the ISO's September 20, 2004 White Paper and will comment further as issues develop in the ongoing stakeholder process addressing this proposal.

In summary, the new proposals for scheduling and settling existing contracts are a significant improvement over the proposal filed in the ISO's July 22, 2003 MD02 filing at FERC. However, fundamentally the ISO continues to maintain its position that ETCs must be reformed to mechanically fit MRTU scheduling and settlement protocols, even as those protocols continue to change within the market design as a whole. ETC holders have not yet had an opportunity to discuss the myriad of ways such an exercise fundamentally alters the rights, obligations and prices represented in their existing contracts. The ETC proposal is formulated to treat ETC holders as if their scheduling and settlement were like all other load and the only risk requiring serious consideration is congestion. This is clear from the fact that the focus of the

ETC proposal is almost entirely on the question of providing a hedge to congestion. Clearly, congestion risk and related costs represent serious detrimental changes to ETCs, but congestion is not the only detrimental impact that can already be reasonably foreseen from the ISO's application of MRTU protocols to ETCs. An overview of San Francisco's Interconnection Agreement with Pacific Gas & Electric (IA) through the information San Francisco has provided to FERC makes clear that the impact on ETCs has only begun to be addressed by the ISO. For this reason, San Francisco has included this overview to provide a fuller picture of the complexity faced in assessing the degree to which MRTU would diminish San Francisco's rights under the IA.

It is clear that the ISO understands the breadth and complexity of ETC agreements. However, the proposals contained in the two white papers do not address that breadth and complexity. They deal fundamentally with the terms and prices the ISO is willing to offer ETC holders under a day ahead, hour ahead and real-time, point-to-point scheduling protocol. Given the many rights, obligations and prices contained in ETCs that are not yet even considered within the ETC Proposal's scope, this exercise can only be viewed as the beginning of a much longer exchange if the ISO's commitment to honoring ETCs under MRTU is to be at all meaningful.

**San Francisco/Pacific Gas & Electric Company Interconnection Agreement (IA):**

At the outset it is important to recall that the October 28, 2003 FERC Order directed the ISO to conduct further analysis on the likelihood that its Market Design Proposal, now called "Market Redesign and Technology Upgrade" or MRTU, would lead to diminished contractual rights of ETC holders. In its July 17, 2004 Order, FERC further directed jurisdictional parties to ETCs to file contract information with the FERC and invited non-jurisdictional parties to make informational filings as well. San Francisco made such a filing on July 23, 2004 in the new docket, Docket No. ER-928-000.

A basic description of San Francisco's IA provides the factual background to more fully understand the comments presented herein. For this reason, San Francisco includes here the supplemental information submitted to FERC to provide a preliminary overview of the complex rights and obligations that the IA represents.

San Francisco owns and operates non-jurisdictional hydroelectric facilities in the Tuolumne River watershed of Northern California, pursuant to provisions of the Raker Act<sup>1</sup>, and is a transmission customer of PG&E pursuant to an existing transmission contract ("ETC") on file with the Commission as PG&E Rate Schedule FERC No. 114 ("IA"). The IA is a comprehensive agreement specifically designed to effectuate the City's rights and obligations in compliance with the Raker Act. The Raker Act granted the City rights of way to federal lands in and next to Yosemite National Park for the purpose of developing water and power facilities now operated by the San Francisco Public Utilities Commission through Hetch Hetchy Water and Power. The City's system is a conglomerate of dams, hydroelectric plants, reservoirs, aqueducts, pipelines and transmission lines which provide power to San Francisco municipal uses, meet service obligations under the Raker Act to Modesto Irrigation District and Turlock Irrigation District ("Districts") and accommodate other sales to public utilities. These resources are managed not only for hydroelectric generation but also for provision of drinking water and in accordance with prudent watershed management practices in cooperation with and under the jurisdiction of the Department of the Interior. In addition, the Raker Act prohibits the sale of water or power to private entities for resale.

Under the IA, San Francisco has firm and non-firm transmission rights on PG&E's system. In addition, San Francisco owns and operates high voltage lines outside the ISO Control

---

<sup>1</sup> 38 Stat. 242 (1913).

Area interconnecting City generation to the Districts' load and to the PG&E system in the Central Valley and in the San Francisco Bay Area.

**San Francisco Service to Municipal Loads and other electric service customers:**

The IA provides for bundled services by and between PG&E and San Francisco from load forecasting and scheduling to delivery of City power to municipal loads and other customers. These services include:

- 1) Load Forecasting and pre-scheduling
- 2) Power Supply Management:
  - a. Supplemental Power
  - b. Maintenance Power
  - c. Emergency Power
  - d. City Reserve Requirements
  - e. Dependable Capacity
  - f. Coordinated Operation
  - g. Scheduling and Balancing Energy
- 3) Firm Transmission, Non-firm Transmission, Distribution
- 4) Metering, reliability services.
- 5) Settlement – includes the Municipal Deviation Account, which allows the City to reconcile the difference between actual and scheduled Municipal Load in half-hourly increments of energy.

**San Francisco Obligations to the Districts:**

San Francisco provides electric power to the Modesto and Turlock Irrigation Districts consistent with the Raker Act and agreements with the Districts. San Francisco owns and operates high voltage lines from Hetch Hetchy to interconnections directly with the Districts

without use of the CAISO-controlled grid. Bundled services to facilitate provision of power to the Districts are covered through a number of provisions within the IA.

#### Mitigating MRTU Impacts on the IA

The IA term is through 2015, which is substantially beyond the anticipated February, 2007 MRTU start-up date. It should be clear from the description above that the change in scheduling and settlement protocols are not the only contract rights likely to be diminished by the ETC proposal. San Francisco sincerely hopes the ISO will continue to advocate for a process that allows a detailed discussion and analysis over a reasonable time frame going forward.

Unfortunately, the ISO has thus far avoided addressing how it will honor the complex and diverse contract rights in ETCs when those rights do not translate into the scheduling and settlement protocols the ISO proposes in MRTU. For those rights that are easily translated and administered within the ISO's proposed Day Ahead, Simplified Hour Ahead and Real-time Markets, parties must still assess whether the costs, timelines and requirements for scheduling and ISO settlement practices honor those rights. For the other rights, such as the ability to schedule resources without reference to a specific location of source or the ability to deliver to load without specifying the location of load in a day ahead forward schedule but still receive firm transmission service, the likelihood of a diminution in contract rights under MRTU and increases in costs are a virtual certainty, absent additional consideration by the ISO for methods to accommodate those rights.

For those rights that can be expressed with reference to a locationally specific source and locationally specific load on a day ahead balanced schedule basis, the ISO has provided exemption from congestion costs and committed to scheduling priority. Under both the original July 22, 2003 proposal and the current proposal, schedule changes after the close of the day

ahead market would not be given first priority but rather accommodated in light of the ISO's total hour ahead schedules that clear the market. The same is true of scheduling changes between the hour ahead market and real-time markets. Thus, ETC holders with firm transmission contracts that provide for service up to and within the hour would experience new risk of curtailment in relationship to all other schedules for that time period.

For settlement purposes, the ISO now offers the new proposal it calls the "Perfect Hedge," in which the ISO preserves the current ETC exemption from congestion charges in each time period. This proposal uses the accounting credit-back mechanism utilized by the Midwest ISO for Grandfathered Contracts. The ISO has gone beyond the MISO protocol by applying the credit back mechanism for each market, not only the Day Ahead as was the case in the Midwest. San Francisco prefers this proposal over the CRR allocation proposal presented in the July 22, 2003 Filing; it is a significant step toward crafting solutions that do not introduce new costs or terms to ETC's under MRTU. Important concerns about scheduling and curtailment risks still remain as discussed below.

This proposal, by itself, does not fully address how the ISO will honor existing contracts nor answer the FERC directive to conduct an inquiry into the likelihood that MRTU will cause a diminution of contract rights for ETC holders. These comments do not purport to set forth a full listing of the ways in which the current proposal, even as modified in the September 20 White Paper, fails to honor existing contract rights. However, it is important to point to a few significant examples at this juncture in order to demonstrate the magnitude of the financial and operational risks the ISO's proposal would impose by not honoring the ETCs as they are currently structured. They include:

- 1) **Losses:** Currently, existing ETC holders charged for losses under the negotiated terms of the individual ETCs. The ISO now proposes to charge

ETC holders directly for marginal losses. The proposal is unclear as to whether losses will be assessed for balanced schedules in the Day Ahead or whether those charges would accrue only to changes after the close of the Day Ahead market. In either case, the new marginal loss calculation has made an increase in costs for losses a certainty under MRTU. There have been no changes to ETC terms and conditions admitting new treatment of losses. The only change is the ISO's method of calculating losses. The current method of loss calculation is a systemwide average. Since losses are a sub-component of the locational marginal price (LMP) itself, all load except ETC load will be settled at a load aggregation price. If ETC holders are charged directly for marginal losses, they will be the only load paying a pure marginal loss charge, since all other load will pay the aggregated loss charge as part of their LMP. Further, the ISO proposes to credit the anticipated over-collection of marginal losses to the CRR balancing account and then allocate those credits to CRR holders. The ETC Proposal is silent as to whether ETC holders will be allocated any portion of the marginal loss over-collection or whether they will simply be held to contributing to that systematic over-collection.

- 2) **Nodal pricing of real-time energy charged to ETC holder load only:** The ETC Proposal still maintains the policy that ETC loads will be the only loads on the system to be charged nodal real-time energy prices for hour ahead changes accommodated in real-time or real-time deviations from day ahead schedules. No justification for this discriminatory treatment has been offered. Further information is certainly required since the ISO proposes to charge ETC holders the nodal price regardless of whether there is congestion in the hour

ahead and real-time settlement period or not. This is an imbalance penalty and as such, it is purely punitive.<sup>2</sup> San Francisco urges reconsideration and rejection of this policy.

- 3) Identification of all ISO charges to ETC holders under MRTU:** Since the very first stakeholder meeting following the July 22, 2003 Filing, stakeholders have requested a full and complete list of all ISO charges it intends to impose upon ETC holders. The discussion in the September 20, 2004 White Paper is identical to that in its original white paper. No further information has been presented. (See ETC Proposal at section 6.3 on page 31.) In addition to losses, several other categories of costs to be assessed under MRTU are implicated in the scheduling and settlement protocols as applied to ETCs, including but not limited to uninstructed deviation penalties, reliability service procurement uplift and neutrality adjustment charges.

Under the ETC Proposal, the ISO plans to treat any ETC schedule changes from its day ahead schedule as if it were any other market participant in terms of scheduling priority under congestion conditions. ETC holders could be assessed RUC charges, RMR charges and other reliability procurement costs not currently charged to ETC holders. Many of these reliability and replacement reserve services and related costs to market participants are covered under prices, terms and conditions in ETCs. The ETC holders must have the ability to compare the ISO's new MRTU charge scheme in full detail in a side-by-side assessment with individual contracts if a

---

<sup>2</sup> The ETC Proposal discusses the need for specific load locations to be designated in ETC schedules. However, this requirement does not explain why the ISO would propose to settle that load at the nodal price rather than the load aggregation price, as it does for all other load. The ISO has stated in the past that charging ETC load nodal prices in real-time is an incentive mechanism to induce forward scheduling in the day ahead market. However, since the new

meaningful consideration of the impact on ETC's is to take place. To date, stakeholders do not yet have the necessary information from the ISO to make a full assessment of the impact of MRTU on their individual contracts.

**The “Perfect Hedge”:** The new proposal to exempt ETC holders from congestion charges as they are today is a welcome improvement over the CRR Allocation proposal in the July 22, 2003 filing. This is the right decision and San Francisco fully supports the proposal to the extent it addresses congestion cost risks implied by imposition of MRTU protocols on ETC holders.

The new “Perfect Hedge” option is far superior to the “CRR Allocation” option previously presented by the ISO. As the discussion above makes clear, addressing only the congestion management and settlement implications of the MRTU impact on ETCs ignores other significant changes to ETC rights. The “CRR Allocation” proposal truncated the discussion of the full range of changes to contract terms and prices implied by the ISO's July 22, 2003 treatment of ETCs. While the “Perfect Hedge” does not resolve them all either, it provides the first meaningful equivalent of the current congestion charge exemption offered by the ISO under MRTU to date.

The “Perfect Hedge” proposal should result in the elimination of the time pressure the ISO has asserted for resolution of ETC issues in general since it eliminates the need to model pricing and settlement of ETC schedules through capacity reservation. The ISO has claimed that resolution of ETC impact issues is “critical path” and must proceed prior to other start up concerns. On this basis, the ISO has rushed this process beyond all rationality toward a December decision. The “Perfect Hedge” proposal eliminates the need to design, build and test

---

“Perfect Hedge” proposal is designed to provide the means and incentive for ETC loads to schedule forward to the degree feasible, that justification is no longer relevant.

separate software to accommodate the capacity reservation strategy employed under the zonal model. In turn, it appears that all parties can now take a meaningful look at all the other unanswered and unresolved issues in the ETC context without jeopardizing the ISO's overall project timeline.

There is a remaining concern regarding the lack of scheduling priority given ETC schedules in the Simplified Hour Ahead and Real-Time markets. It is not clear why the ISO believes it appropriate that ETC holders must face new curtailment risk for schedules under contracts that provide firm transmission service without such risk. Firm transmission service means deliverability and the ISO's proposal on scheduling and curtailment of ETC schedules in the hour ahead and real-time markets under congestion conditions puts that deliverability in question. Further discussion is needed on this aspect of the proposal. As it stands, San Francisco cannot support this element of the "Perfect Hedge."

**Responsibility for Scheduling ETCs and Validating ETC Schedules:** San Francisco supports the ISO's move toward establishing a scheduling and validation procedure that would allow for an entity other than the PTO party to ETCs to perform those functions. The original proposal to maintain this function exclusively within the control and responsibility of the PTO created serious new problems for administration of ETCs, including but not limited to, non-transparency in settlement calculations underlying charges, interpretation and implementation of contract terms by only one party to the contract, and lack of oversight by the other party to the contract to determine the appropriateness of the method and result of those one-sided calculations.

San Francisco is still considering the practical and financial implications of the two alternatives presented in the ETC Proposal, that is, the potential for an automated process or for a designated third party representative for the ETC to schedule and validate ETC schedules under the new MRTU system. A number of practical considerations arose during stakeholder

discussion of these options making clear that further detail from the ISO and further consideration by stakeholders will be necessary before all parties can fully understand the relative merits of these two options. San Francisco intends to fully participate in those discussions.

San Francisco presents these comments in the spirit of continued exchange with the ISO on the impact of MRTU on ETC rights. We remain gravely concerned over the increased scheduling risk and cost impact of the MRTU proposal on our ETC. However, under a more reasonable schedule and with a greater recognition by the ISO of the impact MRTU will have on ETCs, meaningful approaches to honoring ETCs as they were negotiated can hopefully emerge. For this reason, San Francisco provides the comments herein and urges the ISO to continue with the on-going process without seeking FERC approval of the inchoate and costly proposal as it stands currently before the stakeholders.

Respectfully submitted,

DENNIS J. HERRERA  
City Attorney  
THERESA L. MUELLER  
Deputy City Attorney  
IRENE K. MOOSEN  
Special Counsel