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February 7, 2005

Via Electronic Filing

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

Re: California Independent System Operator Corporation
Docket No. ER03-683-___

Dear Secretary Salas:

Enclosed please find the Request for Rehearing and Motion for Clarification, and Motion for Stay, of the California Independent System Operator Corporation, submitted in the captioned docket.

Feel free to contact the undersigned with any questions. Thank you for your attention to this matter.

Respectfully submitted,

/s/ Bradley R. Miliauskas
Bradley R. Miliauskas

Counsel for the California
Independent System Operator
Corporation

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	))	**Docket No. ER03-683-___**

REQUEST FOR REHEARING AND MOTION FOR CLARIFICATION, AND MOTION FOR STAY, OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION

Pursuant to Section 313(a) of the Federal Power Act ("FPA"), 16 U.S.C. § 825l(a) (1994), and Rules 212 and 713 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission ("FERC" or "Commission"), 18 C.F.R. §§ 385.212, 385.713, the California Independent System Operator Corporation ("ISO")[1] respectfully submits this request for rehearing, motion for clarification, and motion for stay, concerning the Order on Rehearing and Clarification Requests, and Compliance Filing, issued on January 6, 2005 in the above-captioned docket, 110 FERC ¶ 61,007 ("January 6, 2005 Order"). The January 6, 2005 Order addressed issues raised in the proceeding on Amendment No. 50 to the ISO Tariff ("Amendment No. 50"). As explained below, the ISO seeks rehearing on two issues and clarification of the Commission's rulings on one other issue. The January 6, 2005 Order erroneously held that the ISO must make a stand-alone Section 205 filing to clarify an aspect of the decremental reference price methodology, even though the Commission, in an earlier order, had required the ISO to include that clarification in a compliance

[1] Capitalized terms not otherwise defined herein are used in the sense given the Master Definitions Supplement, Appendix A to the ISO Tariff.

filing, which the ISO did. The January 6, 2005 Order also erroneously misconstrued the ISO's conformance of one of its operating procedures on Intra-Zonal Congestion Management to reflect the Commission's directives in the original Amendment No. 50 order. The Commission should correct these errors on rehearing and should also grant the clarification discussed below.

I. BACKGROUND AND SUMMARY

On March 31, 2003, the ISO submitted Amendment No. 50 to implement a new, interim methodology for managing Intra-Zonal Congestion.[2] On May 30, 2003, the Commission accepted in part and rejected in part Amendment No. 50, to become effective, as modified, without hearing or suspension. *California Independent System Operator Corporation*, 103 FERC ¶ 61,265, at ordering paragraph (A) (2003) ("May 30, 2003 Order" or "Amendment No. 50 Order"). To comply with the May 30, 2003 Order, the ISO submitted a compliance filing on June 30, 2003 ("June 30, 2003 Compliance Filing") and an addendum to that compliance filing on July 18, 2003 ("July 18, 2003 Addendum"). On April 16, 2004, the Commission issued an order accepting in part and rejecting in part the ISO's compliance filings. *California Independent System Operator Corporation*, 107 FERC ¶ 61,042, at ordering paragraph (A) (2004) ("April 16, 2004 Order" or "First Compliance Order"). The ISO submitted a further compliance filing ("May 17, 2004 Compliance Filing") to comply with the April 16, 2004 Order. In the January 6, 2005 Order, the Commission addressed the May 17, 2004

[2] The ISO's current methodology for managing Intra-Zonal Congestion will be superseded by the implementation of a full-network model for Congestion Management, with locational (nodal) pricing, as part of the ISO's Market Redesign & Technology Upgrade ("MRTU").

Compliance Filing and the requests for rehearing and clarification submitted concerning the April 16, 2004 Order.

The ISO seeks rehearing on two issues addressed in the April 16, 2004 Order and clarification on another issue.[3]

First, the ISO seeks rehearing of the Commission's findings that (1) the ISO improperly implemented a standard for interpreting the Tariff term "competitive periods" developed by Potomac Economics ("Potomac"), the independent entity responsible for determining reference prices, without first incorporating the standard into the ISO Tariff through a stand-alone filing under Section 205 of the FPA, 16 U.S.C. § 824d, and (2) the ISO must provide refunds to Market Participants back to January 20, 2004 resulting from the implementation of this standard on that date. This finding is erroneous because it fails to recognize that, prior to the implementation of the standard, Section 7.2.6.1.1 of the ISO Tariff already contained a mechanism for the ISO to calculate decremental bid reference levels, based in part on input from Potomac. The standard developed by Potomac and implemented by the ISO after notice to Market Participants on January 20, 2004 simply implemented and interpreted that accepted tariff provision. No additional tariff filing was required to implement that authority. Indeed, the Commission has not required other independent system operators to include such standards in their tariffs. Once the Commission ruled, in the April 16, 2004 Order, that Potomac's standard should be incorporated in the ISO Tariff, the ISO appropriately complied by submitting as

part of the May 17, 2004 Compliance Filing a modification to Section 7.2.6.1.1, containing the Potomac standard. Because the mechanism in Section 7.2.6.1.1 was added to comply with a directive in the First Compliance Order, and provides a more complete description of the mechanism through which the ISO is complying with the Amendment No. 50 Order, the ISO acted reasonably in submitting the modification to Section 7.2.6.1.1 in its further compliance filing in this docket.[4] Finally, regardless of whether the Commission determines that the submission of the modification in a compliance filing was appropriate or that a separate Section 205 filing is required, the Commission should permit the ISO to make the modified Section 7.2.6.1.1 effective January 20, 2004 (the date the standard was implemented) or, at the latest, April 16, 2004 (the date the Commission approved the use of the standard, subject to the inclusion of such standard in the tariff, which the ISO did in its May 17, 2004 Compliance Filing).

Second, the ISO seeks rehearing of the Commission's finding that the ISO must provide refunds because it improperly eliminated the use of Adjustment Bids from Generating Units to manage Intra-Zonal Congestion by modifying Section 2.1 of ISO Operating Procedure M-401. This finding erroneously failed to account for the impact of the Commission's directive, in its original Amendment No. 50 Order, that the ISO manage Intra-Zonal Congestion using decremental reference prices. May 30, 2003 Order at P 41. Because decremental reference prices are determined for all generating resources, the

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[3] In addition, as explained in Sections III.A and III.B, below, if the Commission were to deny rehearing on the two issues the ISO raises and direct the ISO to make refunds, the ISO would require clarification from the Commission as to the methodology for determining refunds.

requirement to use decremental reference prices to manage Intra-Zonal Congestion effectively eliminated the need for the ISO also to rely on Adjustment Bids for that purpose. The ISO appropriately modified its operating procedure to reflect the *impact* of the Commission's May 30, 2003 Order on Intra-Zonal Congestion Management with respect to decremental energy; the modification did *not* signify any further change in ISO operations. In fact, once the ISO began using decremental reference prices for Intra-Zonal Congestion Management, as directed by the Commission, it never had occasion to use Adjustment Bids for that purpose. The market rerun ordered in the January 6, 2005 Order therefore would represent a complicated and expensive exercise for no purpose.

Third, the ISO requests clarification that no further modifications are required to comply with the Commission's directive to include a provision in the ISO Tariff that gives generators the opportunity to recover their Start-Up Costs after their units have been shut down by the ISO to manage Intra-Zonal Congestion. The May 17, 2004 Compliance Filing modified Section 7.2.6.1 of the ISO Tariff to provide precisely such an opportunity to generators.

II. SPECIFICATIONS OF ERROR

The ISO respectfully submits that the January 6, 2005 Order erred in the following respects:

1. The Commission erred in finding that the ISO must provide refunds because Potomac's interpretation of the ISO Tariff concerning bid reference

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[4] Out of an abundance of caution, the ISO will file in the near future the modification to Section 7.2.6.1.1 that had been included in the May 17, 2004 Compliance Filing as a conditional Section 205 filing, Amendment No. 65 to the ISO Tariff ("Amendment No. 65").

levels was implemented prematurely and was submitted through a compliance filing in this docket, rather than in a stand-alone filing pursuant to Section 205 of the FPA.

2. The Commission erred in finding that the ISO must provide refunds because it improperly eliminated the use of Adjustment Bids under Section 2.1 of ISO Operating Procedure M-401.

III. REQUEST FOR REHEARING

A. The Requirement That The ISO Make A Section 205 Filing To Implement the Independent Entity's Standard For Identifying Competitive Periods For Purposes Of Determining Bid Reference Levels Is Erroneous.

1. Background

In the May 30, 2003 Order, the Commission required the ISO to "use reference prices for dec[remental] bids to be administered by an independent entity" and directed "the independent entity that determines the reference prices for the AMP [Automated Mitigation Procedures] to develop this decremental bid reference price." May 30, 2003 Order at PP 41, 54. The ISO, in the July 18, 2003 Addendum, informed the Commission that it and the independent entity – Potomac – had agreed on a methodology for calculating decremental reference prices, and in that same filing, the ISO included the methodology in proposed Tariff Section 7.2.6.1.1, to be effective May 30, 2003. As relevant here, Section 7.2.6.1.1 provides for decremental bid reference levels to be determined based on "the accepted decremental bid, or the lower of the mean or the median of a resource's accepted decremental bids if such a resource has more than one

accepted decremental bid in competitive periods over the previous 90 days . . . ." Tariff Section 7.2.6.1.1(a)(1). The effect of this quoted (and Commission-approved) tariff language was to establish in the ISO Tariff a limit on decremental bid reference levels (*i.e.*, the lower of the mean or the median of accepted decremental bids) that would be used by the ISO in the event that a resource had more than one accepted decremental bid in competitive periods. Potomac (not the ISO) would identify "competitive periods" for purposes of implementing this mechanism.[5]

Potomac proceeded to specify its interpretation of the ISO Tariff[6] regarding when "competitive periods" exist for purposes of the ISO's application of Section 7.2.6.1.1 (and thus the circumstances in which the limit on decremental bid reference levels in Section 7.2.6.1.1(a)(1) applies).[7] Potomac explained its interpretation of the ISO Tariff in a January 16, 2004 memorandum to the ISO Market Monitoring Unit; it stated that the standard would clarify "when an offer would be deemed to have been accepted in competitive periods." Transmittal Letter for May 17, 2004 Compliance Filing at Attachment A. The ISO informed

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[5] As explained below, the specification in Section 7.2.6.1.1(a)(1) that only bids considered during "competitive periods" would be considered, without an explanation of the standard to be used by Potomac to identify competitive periods, is virtually identical to language accepted by the Commission for the AMP procedures in the ISO Tariff and for similar procedures in the tariffs of other independent system operators.

[6] In the present filing, this is also referred to as Potomac's standard.

[7] As Potomac has explained, the term "competitive periods" is not defined in the ISO Tariff; rather it is a term of art in economics. Comments of Potomac Economics Ltd. To the Supplemental Protest of Coral Power, L.L.C., Energia Azteca X, S. de R.L. de C.V. and Energia de Baja California, S. de R.L. de C.V., Docket No. ER03-683-003 (filed Feb. 17, 2004), at 6. Normally, competitive periods are defined as those in which offers are accepted in sequence, that is, units are accepted (or curtailed) in order of their relative cost (across the relevant zone). *Id.* Potomac stated that it developed its test in order to address concerns about the application in the ISO markets of the normal definition of competitive periods. *Id.* *See also* May 17, 2004 Compliance Filing at Attachment A (containing January 16, 2004 memorandum from Potomac Economics that makes these same points).

Market Participants of Potomac's interpretation of the "competitive periods" standard in the Tariff and its application of this standard in a market notice issued January 20, 2004. *See id.*

In the First Compliance Order, the Commission accepted proposed Section 7.2.6.1.1 to determine decremental reference bid levels, effective as of May 30, 2003. See April 16, 2004 Order at PP 44-46 and ordering paragraph (A). The Commission also "direct[ed] the CAISO to incorporate the new test [for competitive periods] in section 7.2.6.1.1 of its tariff," and directed the ISO to submit a compliance filing within thirty days. *Id.* at P. 62 and ordering paragraph (B). To comply with that mandate, the ISO proposed changes to Section 7.2.6.1.1(a)(1) in the May 17, 2004 Compliance Filing that reflected Potomac's standard.

In the January 6, 2005 Order, the Commission recognized that in the April 17, 2004 Order it directed the ISO to file Potomac's standard in a compliance filing. January 6, 2005 Order at P 25. However, in the January 6, 2005 Order, the Commission made a 180 degree turn and, without explanation, "clarified" that the standard will not be effective until (1) the ISO files tariff changes incorporating the standard in a filing pursuant to Section 205 of the FPA, to be effective on a prospective basis, and (2) that Section 205 filing is accepted by the Commission. January 6, 2005 Order at P 31. The Commission stated that "[b]ecause the implementation of the Potomac-proposed tariff revision without prior Commission approval has resulted in rates that are not currently on file with the Commission," the ISO was directed to provide refunds for the period starting January 20, 2004

(the date the ISO issued a market notice stating that the independent entity responsible for determining reference prices was going to start applying the standard) through the effective date of the prospective filing pursuant to Section 205 of the FPA. *Id.* The Commission also directed the ISO to submit an assessment of refund amounts owed to any owing by each Market Participant and a proposal for processing the refunds. *Id.* at P 32.

2. The ISO Appropriately Filed the Revisions to Section 7.2.6.1.1 to Implement the Independent Entity's Standard in a Compliance Filing in This Docket.

The Commission's finding that the ISO implemented the mechanism for determining entities' decremental reference prices without ISO Tariff authority, using "rates that are not on file," is erroneous. As explained above, the May 30, 2003 Order directed the ISO to use decremental reference prices to manage Intra-Zonal Congestion and, on July 18, 2003, the ISO filed Section 7.2.6.1.1(a)(1) of the ISO Tariff to establish the mechanism it would use for calculating decremental bid levels for this purpose, stating in that provision that decremental bid reference levels would be determined, in certain circumstances, based on a resource's "accepted decremental bid[s] in competitive periods over the previous 90 days." In the First Compliance Order, the Commission accepted these revisions effective May 30, 2003, over seven months *before* the ISO began implementing the Potomac standard on January 20, 2004.

Significantly, no party protesting or commenting on the July 18, 2003 Addendum complained that the tariff mechanism was incomplete because it did not specify the standard the independent entity would use to identify competitive periods. Nor could the Commission have found the language in the July 18,

2003 Addendum to be insufficient for purposes of calculating decremental reference prices, given that the Commission previously had found similar language concerning accepted bids in "competitive periods over the previous 90 days" to be sufficient for purposes of the calculation of reference price levels by Potomac for the ISO (with respect to AMP reference prices) and for other independent system operators.[8] The Commission had not required that those tariff provisions include more detailed language setting forth the standard that would be used to determine whether a bid had been accepted in a "competitive period." Indeed, if the tariff language added to Section 7.2.6.1.1 in the July 18, 2003 Addendum were insufficient, in and of itself, to authorize the ISO to base decremental reference price levels on bids submitted during recent competitive periods, as determined by Potomac, then all of these other tariff provisions are similarly deficient, and the other independent system operators (NYISO and MISO) and Potomac (with regard to the ISO's AMP process) necessarily must be employing "rates that are not on file" on a daily basis. This plainly is not the case: the Commission has never required that the standards being utilized to

[8] The Commission has approved tariff language of both the New York Independent System Operator ("NYISO") and the Midwest Independent Transmission System Operator ("MISO") whereby reference levels are determined based on a unit's accepted bids in "competitive periods over the previous 90 days for similar hours." *Midwest Independent Transmission System Operator, Inc.*, 108 FERC ¶ 61,163, at P 300 (2004); *New York Independent System Operator, Inc.*, 99 FERC ¶ 61,246, at 62,054 (2002) (approving, *inter alia*, Section 3.1.4(a) of the NYISO's FERC Electric Tariff Volume No. 2, *see* Third Revised Sheet No. 470B). Further, over two years ago, the Commission approved tariff language whereby AMP reference levels are determined based on accepted bids "in competitive periods over the previous 90 days." *California Independent System Operator Corporation*, 100 FERC ¶ 61,060, at P 57, *order on reh'g*, 101 FERC ¶ 61,061 (2002) (approving language found in the ISO's FERC Electric Tariff, First Replacement Volume No. II, MMIP Section 3.1.1.1(a)). In none of these orders did the Commission state what was meant by "accepted bids in competitive periods," and none of the tariff language approved by the Commission defined the term "competitive periods."

identify "competitive periods" to implement these other tariff provisions must be included in tariff language.

On January 16, 2004, when Potomac completed its task of determining how to identify competitive periods to implement Section 7.2.6.1.1(a)(1), there was no indication that the Commission required the standard to be specified in the ISO Tariff, rather than as an interpretation and implementation detail developed by the independent entity under the "rule of reason."[9] The Commission's ruling in the April 16, 2004 Order changed the situation by directing the ISO "to incorporate the new test into section 7.2.6.1.1 of its tariff." April 16, 2004 Order at P 62. The Commission also specifically directed the ISO to "make a compliance filing, as discussed in the body of this order, within thirty days of the date of this order." April 16, 2004 Order at ordering paragraph (B). *See also* January 6, 2005 Order at P 25. The ISO reasonably and appropriately complied with the Commission's ruling by including in the May 17, 2004 Compliance Filing a modification to Section 7.2.6.1.1 to incorporate Potomac's standard for identifying competitive periods.

The January 6, 2005 Order's "clarification" of the April 16, 2004 Order to mandate compliance through a separate Section 205 filing, rather than through the compliance filing prescribed by the earlier order represents an unexplained, unnecessary, and unjustified about-face that imposes onerous new obligations on the ISO and has a significant adverse impact on customers. It is well-settled

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[9] *See, e.g., New England Power Pool*, 95 FERC ¶ 61,253, at 61,877 (2001) (finding that, pursuant to "rule of reason," independent system operator did not need to include implementation details in its tariff); *Pennsylvania-New Jersey-Maryland Interconnection, et al.*, 81 FERC ¶ 61,257, at 62,267 (1997) (same).

that a compliance filing is an appropriate vehicle for a jurisdictional entity to submit tariff changes that implement specific Commission rulings.[10] There was nothing ambiguous about the directive in the First Compliance Order that would suggest to the ISO that this normal route was unavailable. To the contrary, the Commission specifically ordered the ISO to submit a compliance filing and gave no indication that the ISO was to use a vehicle other than this compliance filing to comply with the directive to "incorporate the new test into section 7.2.6.1.1 of its tariff." Indeed, this language interprets or clarifies language submitted as part of a *previous* compliance filing, the July 18, 2003 Addendum, which the Commission approved in all other respects.

Moreover, the "competitive periods" language in the July 18, 2003 Addendum was, as explained above, similar to the "competitive periods" language that the Commission approved and found sufficient for the NYISO and MISO, and for Potomac with respect to AMP. Because Section 7.2.6.1.1 already contained sufficient language, similar to the language that the Commission approved for other independent system operators and for Potomac with respect to AMP, it was reasonable to add the Potomac standard, which was an interpretation or clarification of that language, via a compliance filing rather than a Section 205 filing.[11]

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[10] *See, e.g.*, *California Independent System Operator Corporation*, 93 FERC ¶ 61,104, at 61,289 (2000) ("In the May 31 Order, the Commission required those modifications which the ISO has correctly identified as corresponding to the May 31 Order. Therefore, we accept the tariff sheets submitted in strict compliance with the May 31 Order.")

[11] Given that Potomac is an independent entity that the Commission has already entrusted with making subjective decisions, the Commission should have no qualms about permitting the Potomac standard to go into effect through a compliance filing rather than a Section 205 filing, provided that the Potomac standard is applied on a non-discriminatory basis. The Commission has previously recognized that Potomac should have authority in determining reference levels. In

The Commission itself confirmed the reasonableness of the ISO's use of a compliance filing to provide the additional detail in Section 7.2.6.1.1, when it described the requirements of the First Compliance Order in the January 6, 2005 Order. In the later order, the Commission stated:

> Accordingly, [in the First Compliance Order] we directed the CAISO to incorporate the new test into section 7.2.6.1.1 of its tariff. This new test would establish additional criteria, in the context of decremental reference bid calculations, governing when an offer would be deemed to have been accepted in competitive periods.[15]
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> [15] *Id.* [Previous footnote (footnote 14) cites to April 16, 2004 Order at ordering paragraph (B).]

January 6, 2005 Order at P 30. *See also id.* at P 25 (directing the ISO to "submit a compliance filing" to incorporate Potomac's standard into the ISO Tariff). Like the ISO, the Commission viewed the compliance filing prescribed in ordering paragraph (B) of the April 16, 2004 Order as encompassing the modification of Section 7.2.6.1.1 of the ISO Tariff to incorporate Potomac's standard for competitive periods.

The January 6, 2005 Order contains no justification for disregarding the language of the April 16, 2004 Order and denying the ISO the ability to use a compliance filing to satisfy its obligations under that order. All interested parties

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that regard, in approving the use of an independent entity to calculate AMP reference prices, the Commission addressed the argument of some parties that the independent entity might simply be "plugging in" numbers using the ISO's previously identified criteria. The Commission ruled that the independent entity would not simply be plugging in numbers, but rather would be applying the criteria specified in the Commission's orders, and this would involve the independent entity's making subjective decisions. *California Independent System Operator Corporation*, 101 FERC ¶ 61,061, at P 33 (2002). The criteria specified in the Commission's orders included the calculation of AMP reference levels based on "the lower of the mean or the median of a resource's accepted bids in competitive periods over the previous 90 days," as embodied in MMIP Section 3.1.1.1(a). *See supra* note 8. Potomac has been interpreting this provision – which is similar to the Commission-approved provision in the July 18, 2003 Addendum – since October 2002, and the Commission has never questioned the process by which Potomac makes subjective decisions to interpret the provision.

had the opportunity to file comments and protests on the ISO's May 17, 2004 Compliance Filing to make known any concerns they had with respect to the manner in which the ISO incorporated Potomac's standard into the ISO Tariff. Due process does not require the establishment of a new, separate proceeding for this process to be repeated. Moreover, the January 6, 2005 Order identifies no substantive flaw in the manner in which the ISO incorporated Potomac's standard into the ISO Tariff. Even if such a shortcoming had been identified, there is no explanation why any necessary investigation could not take place in this docket, in which the Commission had the ISO's May 17, 2004 Compliance Filing before it for over seven months before it issued the January 6, 2005 Order. In contrast, as explained in the next section, disregarding the tariff revisions filed in the ISO's May 17, 2004 Compliance Filing and requiring a new stand-alone Section 205 filing would create significant hardships for the ISO and would unfairly and adversely impact consumers.[12] Accordingly, the Commission should grant rehearing and reverse its ruling that the ISO acted improperly in using a compliance filing, rather than a stand-alone Section 205 filing to fulfill its obligation under the April 16, 2004 Order to add Potomac's interpretation of "competitive periods" to the ISO Tariff.

[12] For the reasons explained in the present filing, the ISO appropriately used a compliance filing to incorporate the test into the ISO Tariff. Nevertheless, in the near future the ISO will submit the test in a Section 205 filing (Amendment No. 65), as a precautionary measure to ensure that the test can be employed as quickly as possible even if the Commission does not grant the relief requested here. If, on the other hand, the Commission grants rehearing as requested in this filing and determines that the test does not need to be included in a Section 205 filing, that determination will presumably supersede any Commission findings as the Section 205 filing.

3. The Commission Should Make the ISO Tariff Revisions Incorporating the Potomac Standard Effective the Date the Standard was Implemented or, in the Alternative, on the Date that the Commission Approved the Use of the Standard.

Regardless of whether the Commission accepts the ISO Tariff revisions submitted in the May 17, 2004 Compliance Filing or continues to insist that the revisions be submitted in a stand-alone Section 205 filing, rather than a compliance filing, the Commission should make the Potomac standard effective January 20, 2004, or at the very latest April 16, 2004.

As explained above, months before the ISO began to implement the Potomac standard on January 20, 2004, the ISO had filed tariff language in the July 18, 2003 Addendum setting forth the mechanism through which decremental reference prices would be established, including the use of bids submitted during "competitive periods," as identified by Potomac. Notwithstanding the Commission's subsequent ruling that the standard pursuant to which the independent entity identifies "competitive periods" should be added to the ISO Tariff, the ISO acted reasonably in beginning to implement the standard on January 20, 2004, after notice to Market Participants. At the time, the ISO was under the obligation imposed by the Commission's May 30, 2003 Order to use decremental reference prices to manage Intra-Zonal Congestion. The ISO had filed with the Commission the tariff provisions setting forth the mechanism through which it would do so, in compliance with the May 30, 2003 Order, and those provisions were subsequently accepted, subject only to the incorporation of the standard for identifying competitive periods (and other minor changes). April

16, 2004 Order at PP 44-46, 58-62, and ordering paragraphs (A) and (B). Moreover, as explained above, at the time the standard was implemented on January 20, 2004, Section 7.2.6.1.1 already contained language concerning "competitive periods" that was just as specific as the similar, Commission-approved language used by the NYISO and MISO and by Potomac with respect to AMP. Contrary to the Commission's erroneous belief, the ISO *was* implementing the "rate on file" when it began to employ the Potomac standard on January 20, 2004.

Requiring recalculation and refunds in these circumstances is entirely inappropriate. The ISO was proceeding in good faith to implement the Commission's directives in the May 30, 2003 Order, based on the authority contained in tariff provisions that had been filed with the Commission months earlier. The ISO also issued a market notice stating that the independent entity responsible for determining reference prices was going to start applying the standard. As noted above, the Commission has stated that the use of the Potomac standard for competitive periods was "necessary to correct a fundamental flaw in the proposed decremental reference bid methodology." April 16, 2004 Order at P 62. The Commission has recognized that "related necessary changes" in a compliance filing can become effective on the date that the underlying rates went into effect. *New York Independent System Operator, Inc.*, 99 FERC ¶ 61,125, at 61,536 (2002). The Potomac competitive periods standard clearly constituted "related necessary changes" to the mechanism filed

in the July 17, 2003 Addendum and so should be made effective on the date the standard was implemented – January 20, 2004.[13]

Moreover, no valid purpose would be served by requiring the ISO to recalculate the results of the ISO's Intra-Zonal Congestion Management processes for all periods back to January 20, 2004 to eliminate the effects of the Potomac standard for determining competitive periods. As explained above, in the First Compliance Order, the Commission found that implementation of the Potomac standard was "necessary to correct a fundamental flaw in the proposed decremental reference bid methodology." April 16, 2004 Order at P 62. If the ISO were now to recalculate decremental reference price levels using a *different* approach to identifying competitive periods, it would be forced to revert to the flawed approach that was corrected by the implementation of the Potomac standard on January 20, 2004. Unless the Commission grants rehearing, the ISO therefore would be required to replace decremental reference levels determined using the approved standard with an approach the Commission has found to be "fundamental[ly] flaw[ed]." The ISO does not believe the Commission intended such an irrational result.

If the Commission intended the ISO to recalculate decremental reference levels using a *different* approach to identifying competitive periods, that alternative standard is nowhere identified in the January 6, 2005 Order. As noted above, the tariff language on file when the Potomac standard was implemented stated that decremental price levels would sometimes be based on bids accepted

[13] The "underlying rates" in Amendment No. 50 went into effect on May 30, 2003, but the test was not implemented until the following January.

during "competitive periods," but, like the other tariff provisions upon which it was based (those of the NYISO and MISO, and Potomac with regard to AMP), did not specify the standard for identifying those periods. Therefore, if the Commission denies rehearing and continues to insist that the ISO calculate refunds based on the differences between the prices calculated using the Potomac standard and some other approach to identifying competitive period, the ISO require guidance from the Commission indicating the alternative approach to the identification of competitive periods that the ISO should employ. Without that guidance, the ISO could not calculate refunds, because it does not know the benchmark against which the decremental reference prices calculated by Potomac should be measured. The ISO respectfully submits that the identification of a *new* alternative to the Potomac standard for identifying competitive periods so that refunds may be calculated would be a pointless exercise. The Commission instead should grant rehearing to permit the tariff language reflecting the Potomac standard to become effective on January 20, 2004.

If the Commission does not make the tariff modifications effective on January 20, 2004, then at the latest, the Commission should make the revised tariff language incorporating Potomac's standard effective April 16, 2004, the date of the First Compliance Order, in which the Commission found that the standard should be included in the ISO Tariff. The Commission made that finding based on arguments presented in a supplemental protest, comments, and an answer, rather than any proposal contained in a compliance filing or a filing pursuant to Section 205 of the FPA. *See* April 16, 2004 Order at PP 50-62.

Therefore, the only legal basis for Commission action is Section 206 of the FPA, 16 U.S.C. § 824e.[14] Section 206 states in relevant part that, if the Commission finds that any rate, charge, or classification of any public utility is unjust or unreasonable, "the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order." 16 U.S.C. § 824e(a). The Commission is also required to establish a "refund effective date," between sixty days and seven months after a complaint is filed. 16 U.S.C. § 824e(b). Treating the February 2, 2004 supplemental protest that raised this issue as the equivalent of a complaint, the date of the April 16, 2004 Order is within the permissible period for a refund effective date.

Further, it would be unfair to consumers to require an effective date for Potomac's interpretation after April 16, 2004. In the April 16, 2004 Order, the Commission directed the ISO to file Potomac's standard in a compliance filing. The ISO justifiably relied on the Commission's directive in the April 16, 2004 Order to make a compliance filing, and did so on May 17, 2004. Now, in the January 6, 2005 Order, the Commission is instead requiring the ISO to make a Section 205 filing in order to implement the standard. If the Commission had wanted to require the ISO to make a Section 205 filing instead of a compliance filing it could have said so – but did not – in its April 16, 2004 Order. Now, to

[14] In the April 16, 2004 Order, the Commission found that "the changes proposed by Potomac Economics were necessary to correct a fundamental flaw in the proposed decremental reference bid methodology . . . . We will . . . direct the CAISO to incorporate the new test into section 7.2.6.1.1 of its tariff." April 16, 2004 Order at P 62. Since Section 206 provides the only potential authority for this Commission action, this statement appears to be equivalent to a finding that the decremental reference bid methodology is unjust and unreasonable if the test were to not be used.

comply with the January 6, 2005 Order, the ISO could be required to make millions of dollars of refunds to suppliers (which dollars would come from the pockets of ratepayers). Such refunds would be unnecessary if the Commission had ruled in the April 16, 2004 Order that the ISO needed to make a Section 205 filing (rather than a compliance filing) to implement Potomac's interpretation. Thus, under these circumstances, it is inequitable to ratepayers to require the ISO to implement Potomac's standard via a Section 205 filing that will be implemented on a prospective basis. This issue could have been avoided more than nine months ago if the Commission had directed a Section 205 filing instead of a compliance filing in the April 16, 2004 Order.

4. The Commission's Treatment of Potomac's Standard Is Inconsistent With Its Treatment Of Start-Up Costs For Shut-Down Units.

The Commission's reversal of position in the January 6, 2005 Order, refusing to allow the ISO to implement Potomac's standard for determining accepted bids in competitive periods effective January 20, 2004, is inconsistent with the Commission's treatment of another compliance issue in the same Order. Elsewhere in the January 6, 2005 Order, the Commission directed the ISO to submit changes in a compliance filing to provide generators the opportunity to recover Start-Up Costs for units shut down by the ISO to manage Intra-Zonal Congestion, and specified that the change would take effect as of May 30, 2003. January 6, 2005 Order at P 20. The Commission presented no rationale for its decision to require a Section 205 filing and a prospective effective date for Potomac's standard, but a compliance filing and a retroactive effective date for the recovery of Start-Up Costs.

In fact, there is no rational basis for the different requirements of those two rulings in the January 6, 2005 Order. Both rulings concern retroactive tariff changes the ISO proposed in the May 17, 2004 Compliance Filing in compliance with Commission directions in the First Compliance Order. The May 17, 2004 Compliance Filing included both: (1) tariff language describing Potomac's standard for identifying competitive periods, which the ISO proposed to make effective as of January 20, 2004, the date the standard was implemented;[15] and (2) tariff language to provide for the recovery of Start-Up Costs, which the ISO proposed to make effective May 30, 2003. *See* May 17, 2004 Compliance Filing at Attachment A (at Substitute Original Sheet No. 204B and Third Substitute Original Sheet No. 204A). Thus, the ISO proposed the Potomac standard and the recovery of Start-Up Costs, both with a retroactive effective date, in the same compliance filing. As noted above, a retroactive effective date is appropriate for "related necessary changes" in a compliance filing. *New York Independent System Operator*, 99 FERC at 61,536.

The Commission has approved both the Potomac standard for competitive periods and the recovery of Start-Up Costs as integral parts of the interim approach to Intra-Zonal Congestion Management. It is arbitrary and capricious for the Commission to require the second of these required changes to take effect retroactively through a compliance filing, but to require a prospective effective date and a stand-alone Section 205 filing for the first. The Commission should grant rehearing to permit the Potomac competitive period standard, as

[15] The effective date shown on the Tariff sheet containing the Potomac standard was May 30, 2003, but the standard could only be implemented starting January 20, 2004, after Potomac

well as the provision for the recovery of Start-Up Costs, to be made effective retroactively pursuant to the May 17, 2004 Compliance Filing.

B. The ISO Appropriately Removed the References to Adjustment Bids in Section 2.1 of Operating Procedure M-401 and Does Not Need to Provide Any Refunds.

Prior to the issuance of the Amendment No. 50 Order on May 30, 2003, the ISO used Adjustment Bids to manage Intra-Zonal Congestion. In that order, however, the Commission directed the ISO to manage Intra-Zonal Congestion through the use of decremental reference prices. May 30, 2003 Order at P 41. The ISO complied with the Commission's directive. *See* Transmittal Letter for June 30, 2003 Compliance Filing at 1-4 (listing changes to the ISO Tariff to implement Intra-Zonal Congestion Management through decremental reference prices).

The ISO recognized that once it started using decremental reference prices to manage Intra-Zonal Congestion, it would need to use Adjustment Bids as to Generating Units for that purpose only in cases where there were insufficient decremental reference prices (or no decremental reference prices) to manage Intra-Zonal Congestion. The ISO also recognized, however, that such cases would never arise in practice, because decremental reference prices are always determined for all generating resources. Therefore, the ISO's use of decremental reference prices as required by the May 30, 2003 Order meant that the ISO would always rely on decremental reference prices from Generating Units, and would never have occasion to rely on Adjustment Bids from Generating Units, to manage Intra-Zonal Congestion.

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informed the ISO that it had developed the new standard.

It was the recognition of this reality that led the ISO to modify Section 2.1 of its Operating Procedure M-401. That operating procedure describes how the ISO will dispatch Generating Units to manage real-time Intra-Zonal Congestion, and Section 2.1 concerns the dispatching of Generating Units for in-sequence Imbalance Energy. The ISO modified Section 2.1 by removing the references therein to the use of Adjustment Bids in the dispatching of Generating Units. The ISO submitted the modified Operating Procedure for informational purposes as part of the June 30, 2003 Compliance Filing and explained that the operating procedure "has been updated in accordance with the Amendment No. 50 Order." Transmittal Letter for June 30, 2003 Compliance Filing, at 4. The revised operating procedure was made effective July 1, 2003, the day after the June 30, 2003 Compliance Filing was submitted. See June 30, 2003 Compliance Filing at Attachment C.

In the April 16, 2004 Order, the Commission stated that the removal by the ISO of references to Adjustment Bids from Section 2.1 of Operating Procedure M-401 was inappropriate and directed the ISO to "restore the use of Adjustment Bids." April 16, 2004 Order at P 49. The ISO requested clarification or, in the alternative, rehearing of this directive.[16] In the January 6, 2005 Order, the Commission denied the ISO's request. January 6, 2005 Order at PP 13-17. The Commission directed the ISO to "restore the *status quo ante* and provide refunds to parties affected by the improper elimination of Adjustment Bids under

[16] Motion for Clarification or, in the Alternative, Request for Rehearing of the California Independent System Operator Corporation, Docket No. ER03-683-004 (May 17, 2004), at 2-4 ("May 17, 2004 ISO Motion").

Operating Procedure M-401 from the time the elimination was effectuated through October 1, 2004." January 6, 2005 Order at P 17.[17]

These Commission statements suggest that the Commission misunderstands the reason why the ISO stopped using Adjustment Bids to *manage Intra-Zonal Congestion.* The Commission appears to believe that the ISO made a decision separate from and unrelated to its compliance with the May 30, 2003 Order to stop using Adjustment Bids to manage Intra-Zonal Congestion and reflected this independent decision in the removal of the references to Adjustment Bids in Section 2.1 of the operating procedure. In fact, as explained above, it was the Commission's directive in the May 30, 2003 Order requiring that the ISO use decremental reference prices for Intra-Zonal Congestion Management that rendered the reference in the operating procedure to the use of Adjustment Bids an anachronism. The ISO removed the references to *Adjustment Bids in Section* 2.1 solely to reflect the impact of the May 30, 2003 Order on Intra-Zonal Congestion Management. The ISO's modification did not involve any other changes in ISO operations.

If the ISO had not modified Section 2.1 of the operating procedure to eliminate the references to Adjustment Bids, those references would not have had any effect on ISO operations, and more importantly, the operating procedure would have presented a misleading picture of the ISO's approach to Intra-Zonal

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[17] October 1, 2004 was the date on which Amendment No. 54 to the *ISO Tariff* ("Amendment No. 54") went into effect. January 6, 2005 Order at P 15. In earlier submittals in the Amendment No. 50 proceeding, the ISO explained that Amendment No. 54 contained tariff revisions that eliminated the use of Adjustment Bids for managing Intra-Zonal Congestion (and Inter-Zonal Congestion) *in real time. Motion for Leave to File Answer and Answer of the* California Independent System Operator Corporation to the Motion to Intervene and Protests

Congestion Management following the May 30, 2003 Order. Even with the references to Adjustment Bids in the operating procedure, the ISO would still have used decremental reference prices to manage Intra-Zonal Congestion in compliance with the May 30, 2003 Order. The ISO still would have had no occasion to use Adjustment Bids to manage Intra-Zonal Congestion. Therefore, the removal of these references was nothing more than administrative "clean up" to reflect the ISO's implementation of the methodology approved in the May 30, 2003 Order.[18]

The Commission's belief that the ISO changed the operating procedure "based upon a Commission decision in the October 2003 Order on Amendment No. 54," also stems from this misunderstanding. *January 6, 2005 Order at P 15.* The text of the revised operating procedure, and the timing of the revision, indicate that the ISO made to reflect the May 30, 2003 Order, not an Amendment No. 54 order. As explained in the revised operating procedure, the revisions were made "*to reflect the dispatch of decremental reference bids.*" June 30, 2003 Compliance Filing at Attachment C, page 12 (emphasis added). And the

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Concerning the June 30, 2003 Compliance Filing, Docket No. ER03-683-003 (Aug. 5, 2003), at 16; May 17, 2004 ISO Motion at 2-3.

[18] The Commission also asserts that "by not utilizing Adjustment Bids to manage intra-zonal congestion in real time," the ISO violated Section 7.2.4.1.4 of its tariff. January 6, 2005 Order at P 16. The Commission quotes the language in Section 7.2.4.1.4 stating that the ISO "shall also use incremental Adjustment Bids from Generating Units and Adjustment Bids from other resources in the ISO's real-time system operation for Intra-Zonal Congestion Management and to decrement Generation in order to accommodate Overgeneration conditions." January 16, 2005 Order at P 16. Section 7.2.4.1.4 merely provides authority for the ISO to use Adjustment Bids as one means of managing Intra-Zonal Congestion; the section says nothing about the sequence the ISO follows for Intra-Zonal Congestion Management. The sequence the ISO follows is provided in Operating Procedure M-401. Pursuant to that sequence, and as described in the text above, the ISO always relies on decremental reference prices and has no occasion to use Adjustment Bids. Therefore, it is not the case that the ISO has refused to use Adjustment Bids in accordance with Section 7.2.4.1.4, only that the ISO has no need to use them due to the Commission's directive in the original Amendment No. 50 order.

July 1, 2003 effective date of the revised operating procedure confirms that it was not revised to comply with any order issued in the Amendment No. 54 proceeding because Amendment No. 54 was not even filed with the Commission until July 8, 2003.

The fact that the ISO has only used decremental reference prices to manage Intra-Zonal Congestion, and has not used Adjustment Bids, means that the ISO would have managed Intra-Zonal Congestion in exactly the same way even if the references to Adjustment Bids had not been deleted from Section 2.1 of the operating procedure. Because the deletion of the references had no effect on how the ISO managed Intra-Zonal Congestion, there are no refund amounts for the ISO to pay resulting from the deletion of those references.[19]

IV. MOTION FOR CLARIFICATION

In the January 6, 2005 Order, the Commission directed the ISO to modify its tariff to provide that, if a Generating Unit is instructed by the ISO to shut down to manage Intra-Zonal Congestion, and is subsequently re-started, the Owner of that Generating Unit will have the opportunity to recover its Start-Up Costs. The

[19] If the Commission were to find that it was incorrect for the ISO to use decremental reference prices, rather than Adjustment Bids to manage Intra-Zonal Congestion, and thus that the ISO should have been using a different process for managing Intra-Zonal Congestion to satisfy the requirements of the May 30, 2003 Order, then refunds might be required. In that case, the ISO would require Commission guidance as to the different process it should have undertaken. The January 6, 2005 Order provides no indication regarding what different process the Commission might envision. Moreover, even if the Commission were to provide the required clarification as to the different process, determining refunds in that case would be at best an extremely complicated undertaking. The ISO would have to determine – presumably for a time-period starting in 2003 (when the original Amendment No. 50 Order was issued) – how Intra-Zonal Congestion would have been managed under that different process, make a comparison with the process the ISO actually employed, and then calculate refunds based on the disparities between the two processes. However, in order to engage in that exercise, the ISO would first have to figure out how its Intra-Zonal Congestion Management would have run if the ISO had

Commission required this tariff modification to be made effective May 30, 2003. January 6, 2005 Order at P 20 and ordering paragraph (F). The ISO believes it has already complied with this directive. The May 17, 2004 Compliance filing contained changes to Tariff Section 7.2.6.1 – bearing an effective date of May 30, 2003 – to allow generators the opportunity to recover their Start-Up Costs. *See* May 17, 2004 Compliance Filing at Attachment B (at Sheet No. 204A). The ISO justified the proposed changes by stating that, in the April 16, 2004 Order, the Commission noted the view of one party (Coral Power, L.L.C., *et al.* ("Coral Power")) that generators should be given the opportunity to recover their Start-Up Costs, and noted the ISO's willingness to modify its tariff to provide for that opportunity, but did not appear to direct the ISO expressly to modify the tariff. The ISO stated that it was requesting clarification on this issue in the May 17, 2004 ISO Motion, and that it proposed to amend Tariff Section 7.2.6.1 to provide generators the opportunity for cost recovery. Transmittal Letter for May 17, 2004 Compliance Filing at 3-4. The January 6, 2005 Order referenced the ISO's request for clarification, but did not acknowledge the changes to Tariff Section 7.2.6.1 contained in the May 17, 2004 Compliance Filing. January 6, 2005 Order at P 20. The ISO requests that the Commission clarify that no further changes are necessary for the ISO to comply with its directive to allow generators the opportunity to recover their Start-Up Costs.[20]

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managed Intra-Zonal Congestion in a different way. Figuring that out may well be impossible, and at the very least it would be an exceedingly complex undertaking.

[20] The ISO notes that Coral Power, the only party that protested the May 17, 2004 Compliance Filing, was silent regarding the ISO's proposal to provide generators the opportunity to recover their Start-Up Costs. *See* Protest of Coral Power, L.L.C. and Energia Azteca X, S de R.L. de C.V. and Energia de Baja California, S de R.L. de C.V. to May 17, 2004 Compliance Filing, Docket No. ER03-683-005 (filed June 7, 2004). Therefore, Coral Power appeared to be

V. MOTION FOR STAY

The Commission may stay its action "when justice so requires." 5 U.S.C. § 705; *ISO New England, Inc.*, 94 FERC ¶ 61,015, at 61,023 (2001). The ISO respectfully requests that the Commission grant a stay of its directives to the ISO to provide refunds purportedly resulting from a premature implementation of Potomac's standard concerning bid reference levels (*see supra* Section III.A)[21] and from the deletion of the references to Adjustment Bids in Section 2.1 of Operating Procedure M-401 (*see supra* Section III.B).

Justice requires a stay in the present circumstances. As explained in Section III.A and Section III.B, the Commission should find that refunds are not required with regard to either of these issues, and, even if the Commission finds that refunds are required, the Commission needs to resolve significant issues before the ISO can even begin to determine the refund amounts. Therefore, refunds are not needed, and even if they were needed, the ISO is unable to determine what the refund amounts should be.

For these reasons, the ISO submits that it does not make sense for ISO Settlements personnel to begin the enormous effort that will be required to determine refund amounts given that refunds could be subsequently overturned, and given that any determinations of refund amounts would need to be redone

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satisfied with the ISO's proposal. To be sure, Coral Power, in its May 17, 2004 request for rehearing and clarification of the April 16, 2004 Order (at 6-9), asked the Commission to require the ISO to permit the recovery of Start-Up Costs, but Coral Power submitted that request before it had a chance to see the provisions concerning the recovery of Start-Up Costs contained in the May 17, 2004 Compliance Filing.

[21] The ISO also requests that the Commission grant a stay of its directive to the ISO to provide an assessment of refund amounts owed to and owing by each Market Participant and a proposal for processing the refunds. Concurrently with the present filing, the ISO is submitting a

based on the outcome of subsequent Commission clarifications. This is especially true given that the Settlements personnel that would be required are completely occupied with other critically important work at this time. The Settlements personnel are engaged "around-the-clock" in work on the rerun of the ISO Settlements system that is required by the Commission in the California refund proceeding and work on other reruns of the ISO Settlements system. The ISO also is currently implementing a new Settlements and Market Clearing System for parallel operations in Fall 2005 and implementing 2004 Grid Management Charge settlement changes. If Settlements staff were required to immediately start work on determining refund amounts in the present proceeding, that could only be done by drawing them off from those other important matters. Further, the ISO currently has over 70 recalculation items that will need to be prioritized and planned for implementation prior to or after the completion of the parallel operations of the new Settlements and Market Clearing System. The priority given to any refund rerun stemming from the January 6, 2005 Order would need to be weighed against the priority given to the other 70 or so recalculation matters in queue.

In sum, justice requires the granting of a stay of the Commission's directives to provide refunds.

VI. CONCLUSION

WHEREFORE, for the above-stated reasons, the ISO respectfully requests that the Commission grant rehearing, clarification, and a stay of its

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motion for extension of time to submit that assessment of refund amounts, until after the

January 6, 2005 Order, and that the Commission further find, determine, and order as described above.

Respectfully submitted,

/s/ Kenneth G. Jaffe

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Dated: February 7, 2005

Commission has considered the present filing in an order on rehearing.

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, California, on this 7th day of February, 2005.

/s/ Anthony Ivancovich
Anthony Ivancovich