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July 22, 2005

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 Nos. ER03-746-000, *et al.*
San Diego Gas & Electric Co., *et al.*
Docket Nos. EL00-95-081, *et al.*
California Independent System Operator Corporation and California Power Exchange
Docket Nos. EL00-98-069, *et al.*

Dear Secretary Salas:

Enclosed please find one original and fourteen copies of the Addendum to the Eighteenth Status Report of the California Independent System Operator Corporation on Re-Run Activity filed in the above-captioned dockets.

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

Sincerely,

Michael Kunselman

Counsel for the California Independent System Operator Corporation

Enclosures

ADDENDUM TO CAISO'S JULY 11, 2005 REFUND STATUS REPORT

DETAILS CONCERNING THE FINANCIAL ADJUSTMENTS TO BE MADE BY THE ISO AS PART OF THE REFUND PROCESS

I. BACKGROUND

The purpose of this addendum is to clarify the ISO's efforts during the financial adjustment phase and also to identify what is needed from participants and the Commission in order for the ISO to begin and complete that process.

Further work on the various financial adjustments is currently on hold pending receipt of the audited fuel cost allowance claims from the generators, as well as emissions offset information, and any cost-based rate filings. Based on prior Commission orders the ISO anticipates receipt of most of the fuel cost audit information from Ernst & Young on or before August 1, 2005 and receipt of fuel cost information from FTI Consulting ("FTI") relating to Williams on or before November 1, 2005. There are, however, still outstanding issues relating to the receipt of emissions data and the filing and approval of cost-based rate filings.

The ISO's financial adjustment phase will consist of the following:

a. Adjustments relating to the allocation of emissions, fuel cost allowances, and any cost-based rate filing approved by the Commission

b. Interest calculations

At the conclusion of this phase, the ISO will file with the Commission a compliance filing detailing these adjustments.

The ISO will also perform adjustments relating to global settlements. The ISO will file these adjustments in the compliance filing detailing the various financial adjustments and interest calculations, or in a subsequent filing, depending on the amount of time required to complete the settlement adjustments.

Each of these individual adjustments is described in detail below:

II. ALLOCATION OF FUEL COST ALLOWANCES

A. Background

The Commission's orders in this proceeding have permitted generators to claim an additional fuel cost allowance based on their actual daily cost of gas incurred to make spot market sales in the PX and ISO markets.[1] The Commission has required that generators submit their fuel cost allowance claims to the auditor Ernst and Young, who is currently in the process of verifying, for all but one of the claimants, that these calculations have been performed in accordance with the Commission's orders in this proceeding. Pursuant to the Commission's direction, Ernst and Young is expected to provide the final data on fuel cost allowance claims to the ISO by August 1, 2005, so that the ISO can allocate these fuel costs to participants during the Refund Period. With respect to one claimant, Williams, the Commission ordered that its fuel cost claim would be verified by FTI, and would be due to be delivered to the ISO for allocation on November 1, 2005. All of the fuel cost data will be made available and allocated on an hourly basis.

B. ISO Allocation Methodology

With respect to the methodology for allocating the verified fuel cost allowance claims, pursuant to the Commission's various orders addressing allocation issues, the ISO plans to allocate verified fuel cost allowance amounts to purchases made during each hour in which a verified fuel cost allowance claim has been made for sales of instructed and/or uninstructed energy in the ISO's spot market.

In order to perform this calculation, the ISO will first sum up the total verified fuel cost allowance claims for sales of instructed and/or uninstructed energy in the ISO's spot market by all participants for each hour. Fuel cost allowance claims for sales in the PX market will be allocated by the PX, and will therefore not be included in the ISO's calculations.

Second, the ISO will determine the total amount of each participant's mitigated purchases made in its spot markets for each applicable hour. For instructed energy, mitigated purchases by each SC will be calculated by summing up the volume (MWh) of all instructed decremental energy transactions by that SC with an initial transaction price greater than the MMCP. For uninstructed energy, mitigated purchases by each SC will be calculated by summing up the volume (MWh) of all net negative uninstructed energy quantities (on an SC level, by congestion zone) for intervals when (a) the SC has a net negative deviation for which it received a charge for uninstructed energy (Charge Type 401), and (b) the total amount charged when the SC's net negative deviation was "mitigated" (*i.e.* reduced as a result of the ISO's refund calculations).

The ISO will identify intervals when charges for net negative deviations were "mitigated" as follows:

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[1] *See, e.g., San Diego Gas & Electric Co., et. al,* 102 FERC ¶ 61,317 (2003) ("March 26 Order") at P 61.

- For each interval (and for each congestion zone, when congestion occurred), the ISO will add unit charges" (*i.e.* $/MWh amounts) assessed to each SC with negative deviations under the 401 and 481 Charge Types during the preparatory rerun.

- For each interval (and for each congestion zone, when congestion occurred), the ISO then will add unit charges (*i.e.* $/MWh amounts) assessed to SCs' negative deviations under the 401 and 481 charge codes during the refund rerun.

- If the total amount ($/MWh) assessed to SCs with negative deviations under the 401 and 481 Charge Types was lowered during the refund rerun relative to the preparatory rerun, then all net uninstructed deviations during that interval (for that congestion zone, when congestion occurred), represent "mitigated" purchases of uninstructed energy.

Next, the ISO will sum up each participant's total mitigated spot market purchases (instructed and uninstructed) for each applicable hour, and divide this total by the total spot market purchases made by all entities during each applicable hour, in order to determine each participant's proportional share of the mitigated spot market purchases for each applicable hour.

Finally, the ISO will allocate the total amount of approved fuel cost allowances for sales of instructed and/or uninstructed energy in the ISO's spot market during each applicable hour based on each participant's share of the total mitigated spot market purchases made during those hours.

It should also be noted, as the ISO explained in its request for clarification/rehearing of the Commission's December 20, 2004 order,[2] that because the PX served as the SC for multiple participants, including the state's three major investor-owned utilities ("IOUs"), the ISO must allocate fuel cost allowances for purchases of ISO spot market energy made by the PX as SC to the PX, for the PX to then allocate these charges to participants for whom the PX served as the SC. For the PX Day Ahead and Hour Ahead markets, the PX may allocate FCA claims directly, because no netting of PX and ISO sales and purchases is permitted. In its March 18, 2005 order,[3] the Commission clarified that this was the proper manner for allocating fuel cost allowance claims associated with PX transactions.

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2 *San Diego Gas & Electric Co., et. al*, 109 FERC ¶ 61,297 (2004) ("December 20 Order").
3 *San Diego Gas & Electric Co., et. al*, 110 FERC ¶ 61,293 (2003) ("March 18 Order").

C. Outstanding Issues

In the ISO's July 11, 2005 Status Report, the ISO indicated that the receipt of fuel cost data from Williams three months later than the data received with respect to other claimants would mean a concomitant delay in the commencement of the financial adjustment phase of the ISO's refund compliance process. The reason for such a delay is due to the fact that Williams was one of the largest suppliers of energy in the ISO markets during the Refund Period. Thus, any allocation of fuel cost allowances that the ISO performs without the fuel cost data from Williams would be grossly incomplete and of little to no use to any of the parties in this proceeding, or the Commission, even as an intermediate calculation. Therefore, it is the ISO's intent to wait to begin its allocation of fuel cost allowances, and other financial adjustments, until it receives the Williams data on November 1, 2005. The ISO regrets that such a delay is necessary, but for the reasons stated herein, the ISO believes that progressing without the Williams data and later revising the results with the Williams data will not advance the overall schedule.

III. ALLOCATION OF EMISSIONS OFFSETS

A. Background

The Commission's orders in this proceeding have made clear that certain suppliers are entitled to offsets to their respective refund liabilities due to emissions-related costs.[4] In the March 26 Order, the Commission approved emissions offsets for several parties, [5] and required two parties, LADWP and Pasadena, to re-calculate their emissions costs on a pro-rata basis. The Commission also found that Reliant should be required to calculate its emissions costs on a pro-rata basis, but clarified that the California Generators' existing pro-rata allocation exhibit could be used for this purpose. In the March 26 Order, the Commission also concluded that emissions offsets should be allocated based on Control Area Gross Load.[6]

Subsequently, in its October 16, 2003 Order on Rehearing,[7] the Commission granted the California Parties' request for rehearing and concluded that emissions offsets should only be available for mitigated intervals.[8]

In its Status Report on Emissions Offsets and Fuel Cost Allowance, filed in this proceeding on May 24, 2004, the ISO explained that it understood that

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4 *San Diego Gas & Electric Co., et al.*, 96 FERC ¶ 61,120 (2001) at 61,159 ("July 25 Order").

5 The Commission approved emissions costs offset figures submitted by Duke, Dynegy and Williams, and found that Reliant should utilize the pro-rata allocation exhibit already prepared by the California Generators.

6 *Id.* at P 122.

7 *San Diego Gas & Electric Co., et al.*, 105 FERC ¶ 61,066 (2003) ("October 16 Order").

8 *Id.* at P 153.

before it could allocate emissions offsets, parties would first have to complete any Commission required recalculations. This includes recalculations relating to the Commission's ruling that emissions costs could only be claimed for mitigated intervals.[9] The ISO then explained that once the Commission approves these figures, the ISO will require only a final emissions cost offset figure from each party, that is, the total amount of emissions costs that the Commission permitted a party to offset for the entire Refund Period.

B. ISO Emissions Allocation Methodology

Once the ISO has the final emissions cost figures for all relevant entities, the ISO will then aggregate all of the Commission-approved emissions offsets and allocate this aggregate amount *pro rata* to Market Participants based on their total Control Area Gross Load for all mitigated intervals during the Refund Period, consistent with the Commission's directive in the March 26 Order. The reference to "mitigated intervals" means that for purposes of allocation, the ISO will only count Control Area Gross Load that occurred during intervals in which the mitigated price exceeded the historical market clearing price. The ISO believes that this allocation methodology is appropriate, because only those emissions costs incurred with respect to mitigated intervals are available for offset. Thus, it stands to reason that only that Control Area Gross Load that occurred during mitigated intervals should be allocated these costs.

C. Outstanding Issues

At this point, both LADWP and Pasadena have filed updated emissions cost claims with the Commission. The California Parties have challenged both of these filings. The Commission has yet to rule on these filings. The ISO understands that even those entities whose emissions offsets were approved in the March 26 Order will need to recalculate their emissions costs to conform with the Commission's ruling in the October 16 Order that those costs are only available for mitigated intervals. Also, Reliant recently filed with the Commission a proposed common template for emissions costs submissions to the ISO, which the ISO commented on, noting that although it did not oppose the adoption of a common template, it only required for each entity a final, Commission approved emissions cost offset number in order to perform the allocation.

In order to meet its most recent schedule for completion of the financial adjustments phase, the ISO will require all of the approved emissions cost offset figures no later than the date on which it receives all of the audited fuel cost data.

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9 Therein, the ISO stated that the individual parties claiming emissions costs should be the ones responsible for performing this calculation, rather than the ISO, because those parties are fully capable of doing so.

IV. ADJUSTMENTS TO EFFECTUATE ANY APPROVED COST-BASED RATE FILINGS

A. Background

In its orders in the Refund proceeding, the Commission has stated that it would permit marketers an opportunity to submit cost evidence on the impact of the refund methodology on their overall revenues over the refund period, and to file for cost-based recovery if they can demonstrate that the refund methodology results in a total revenue shortfall for all jurisdictional transactions during the Refund Period.[10]

In an order issued on December 10, 2004, the Commission invited parties to provide initial and reply comments on the substance, format and support of the cost-based filings.[11] A number of parties filed comments on these issues. One of the issues that the Commission specifically flagged for comment was what, if any, problems would arise if the Commission were to order refunds first by those sellers not seeking cost-based recovery, instead of waiting to issue refunds until all sellers' cost-based recovery filings have been filed and processed by the Commission. In its comments, the ISO explained that such a procedure would prove problematic, because this proposal would double the timeframe for calculations and quality checks associated with the financial adjustment phase and with the adjustments based on global settlements. Also, the ISO would need to modify its software or worse, perform another settlement production re-run. And finally, multiple financial clearings would be greatly complicated by the bankruptcies that are involved during the Refund Period.

B. ISO Methodology for Allocating Cost-Based Filings

At present, given the outstanding issues relating to this matter, the ISO has not developed a methodology for allocating the results of any cost-based filings that may be approved by the Commission. However, the ISO has given it some consideration, and believes that a methodology similar to the one that will be used for allocating fuel cost allowances may be appropriate. Additional analysis and final development of a methodology, however, will need to await an order resolving the outstanding issues relating to the cost-based filings.

The ISO is also considering the appropriate format for receipt of this data, and will provide more details in its next monthly status report.

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10 *San Diego Gas & Electric Co., et al.*, 97 FERC ¶ 61,275 (2001) at 62,193-194 ("December 19 Order").

11 *San Diego Gas & Electric Co., et al.*, 109 FERC ¶ 61,264 (2004) ("December 10 Order").

C. Outstanding Issues

The Commission has yet to rule on these issues raised in the December 10 Order and in the comments provided by parties in response to that order. As the ISO explained at the technical conferences held last year in the Refund proceeding, and in written comments filed after those conferences, in order to meet its schedule for completion of the refund process, the ISO must receive any Commission-approved cost-based filings at the same time that it receives emissions and fuel cost allowance data. This is the case because of the reasons articulated by the ISO in its comments in response to the December 10 Order, as reiterated above.

V. CALCULATION OF INTEREST

A. Background

The Federal Energy Regulatory Commission ("Commission") in its order in the Refund Proceeding dated July 25, 2001[12] ordered that interest be charged at the Commission rate (as specified in 18 CFR § 35.19a) on all unpaid invoices, both for debtors and creditors, for the Refund Period. The ISO plans to follow a three-step process in order to implement this directive.

B. ISO Interest Calculation Methodology

1. Reversal of Interest Originally Charged During the Refund Period

In order to implement the above-referenced Commission ruling regarding interest during the Refund Period, all interest originally charged to debtors during the Refund Period by the ISO must first be reversed.

After each monthly clearing, the ISO originally calculated interest on each unpaid invoice (this interest is referred to as default interest) from a debtor, from the payment date for the final settlement of the previous month to either the date of payment or the payment date of the preliminary settlement for the current month. The default interest was aggregated for all unpaid invoices of that debtor and, originally, was entered on the invoice for the next trade month. Later, the default interest was entered on the second following month's invoice. Default interest was originally included in the Unaccounted For Energy ("UFE") charge type, until February 2001 when a separate charge type was created to account for it.

The details concerning interest charges by trade month were maintained by the ISO accounting department and reconciled with the ISO settlements

[12] July 25 Order at 61,519.

department in order to insure that SCs were properly charged interest during the Refund Period. In order to prepare to reverse the original interest amounts charged during the Refund Period, all of the default interest charges for defaults during the Refund Period were aggregated and summarized. These amounts will be provided to ISO settlements staff, who will incorporate them into the settlements database, to be aggregated into the final invoices that will be generated at the end of the refund process.

2. Calculation of Interest on Unpaid Invoices during the Refund Period

The ISO accounting department has maintained a spreadsheet detailing the invoicing and clearing of every month from October 2000 through the current trade month. This worksheet was used to extract the Grid Management Charge("GMC"), Accounts Receivable ("AR") and Accounts Payable ("AP") invoicing activity for the trade months of October 2000 through June 2001. It contains for each SC for each trade month for each invoice type the date and amounts relating to:

- Amounts Invoiced
- Adjustments
- Offsets
- CERS Adjustments
- Collections and/or Payments
- Ending Balance

From the schedules of pre-October 2, 2000 activity and post June-2001 activity, two special adjustments were made:

- October 2000 – Adjustments to exclude pre-October 2 activity
- June 2001 – Adjustments to exclude post-June 20 activity

Because GMC charges are assumed to occur on the last day of the month and are not allocated to any intra-month periods. Thus:

- All October 2000 GMC invoices are included in the interest calculations.
- All June 2001 GMC invoices are excluded from the interest calculations.

For October 2000 and June 2001, the ISO accounting department applied cash payments, receipts and offsets on a first-in, first-out basis. That is, collections were first applied to the earliest period i.e. pre June 21, 2001 until those charges were paid in full and then to the post June 20, 2001 charges.

ISO accounting has tracked the amounts and activity by date for each SC during the Refund Period with a subtotal by quarter, as quarterly compounding is required by the Commission. As described above, in order to avoid double counting, interest previously charged to an SC will be reversed. Interest will then be calculated on the amount outstanding using the Commission rate, starting from the original payment date, including all subsequent invoice activity, and then compounded quarterly. The Commission's interest rates are available on the Commission's web site.[13]

The total interest on the GMC and AR invoices will then be aggregated. There will most likely be a difference between the aggregate interest to be collected by the ISO on the GMC and AR and the interest on the AP invoices. That is, the interest received by the ISO will not match the amount of interest to be paid out by the ISO. Pursuant to the Commission's directive[14] this difference between interest receivable and payable is to be prorated between both creditors and debtors.

The Commission also allowed the PX to adjust its interest amounts based on the rate actually earned by the PX on the funds it collected from certain Market Participants and has maintained in an escrow account.[15] The mechanics of the PX adjustment have not been worked out. However, the ISO will have to provide the results of its compliance filing to the PX, so that the PX can calculate its interest adjustment and provide that adjustment back to the ISO. The ISO will then take the PX adjustment and allocate it to all remaining debtors and creditors based on their aggregate interest balances.

3. Calculation of Interest on Refund Amounts

The final refund amounts include the amounts from transactions that were mitigated pursuant to the Commission's refund methodology, the emissions offsets, fuel cost adjustments, and any cost-based rate adjustments. Because the post -January 17, 2001 hour ending 22 charges for SCE and PG&E were re-billed to CERS, the refund amounts relating to these entities must also be re-billed to CERS. The charges relating to these IOUs for the post-January 17 period were reclassified to CERS as well. All of the refund amounts are entered as if they occurred on the payment date for the trade month relating to the underlying transactions. Interest was then calculated on the amount outstanding using the Commission rates from the original payment date and compounded quarterly as discussed above.

For refund amounts, the total AR and AP will be equal. Thus, there will be no difference between interest receivable and payable on refunds, and therefore no allocation of any difference is necessary.

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[13] This information is available at http://www.ferc.gov/legal/ferc-regs/acct-matts/interest-rates.asp .

[14] October 16 Order at P 105.

[15] *San Diego Gas & Electric Co., et al.*, 107 FERC ¶ 61,165 (2004) at P 34.

C. Outstanding Issues

The ISO is not aware of any outstanding issues concerning interest calculations.

VI. ADJUSTMENTS FOR GLOBAL SETTLEMENTS

The final step in the ISO's adjustment process is accounting for the impacts of the various Commission-approved settlements entered into between various parties to this proceeding. Because the ISO is not a party to these settlements, the ISO does not plan to perform its own interpretation of the terms of these settlements in order to arrive at a series of appropriate financial adjustments. Rather, the ISO expects to receive from the various settlement parties an official statement indicating to the ISO the adjustments that it should make to the ultimate post-refund adjustment financial position of each affected entity in order to account for these settlements.

VII. FINANCIAL CLEARING OF AMOUNTS OWED AND OWING BASED ON COMMISSION APPROVED REFUND ADJUSTMENTS

Once the Commission approves the rerun and all associated adjustments made by the ISO, the ISO anticipates that the Commission will issue an order directing the ISO to invoice parties for the entire Refund period, based on the Commission-approved adjustments described herein.

CERTIFICATE OF SERVICE

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

Dated at Folsom, CA, on this 22nd day of July, 2005.

Katherine Corradetti
(916) 608-7021