UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	)	ER01-____-000

TESTIMONY OF
PHILIP R. LEIBER
ON BEHALF OF THE
CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CORPORATION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Philip R. Leiber and my business address is 151 Blue Ravine Road, Folsom, CA 95630.

Q. BY WHOM AND IN WHAT CAPACITY ARE YOU EMPLOYED?

A. I am employed by the California Independent System Operator ("ISO") as Treasurer and Director of Financial Planning.

Q. WHAT ARE YOUR DUTIES AND RESPONSIBILITIES?

A. As Director of Financial Planning, I am responsible for coordinating the development of the ISO's annual operating and capital budgets, variance reporting, and rate filings. I am also responsible for treasury functions, including the borrowing and investing of funds, and risk management. In addition to these responsibilities, I am the Project Co-Manager (Michael Epstein is the other Project Manager) of the ISO Unbundling Project Team ("Project Team"), which produced the unbundled Grid Management Charge ("GMC") proposal filed on November 1, 2000 in Docket No. ER01-313-000. To avoid confusion, I will refer to the November 1 filing as the "GMC Filing".

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.

A. I received my Bachelor of Business Administration and Master of Accounting from the University of Michigan. I hold a Certified Public Accountant ("CPA") license issued by the State of California, and hold the Certified Cash Manager ("CCM") designation.

Q. PLEASE STATE YOUR WORK EXPERIENCE PRIOR TO THE WORK YOU ARE DOING TODAY.

From 1992 through 1997, I was employed by Coopers & Lybrand, LLP in San Francisco, in various positions, most recently as a Manager in the Financial Advisory Services group, and prior to that assignment in the audit practice. I performed financial analysis activities in a variety of contexts, including mergers and acquisitions, business reorganizations, and litigation.

In the audit practice, I was responsible for the planning, executing, and reporting of financial audits of public and private companies, including some in the regulated utility industry, high technology, investment, and other industries.

My other employment has included teaching positions for university-level accounting courses, private CPA exam review courses, internal auditing and other public accounting firm experience.

I became involved in the electric industry restructuring efforts through my employment with Coopers & Lybrand. In late 1996, Coopers & Lybrand was retained by the ISO Restructuring Trust ("Trust"), a predecessor to the ISO, as financial administrator for the Trust. I worked in this capacity for approximately nine months, and then joined the ISO as an employee.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. As Director of Financial Planning, I am responsible for the ISO's annual budgeting process, and for the rate filings that result from this process. As a Co-Project Manager for the GMC unbundling effort completed earlier this year, I had responsibility for developing the ISO's unbundled GMC. I will discuss the budgeting process and how the 2001 budget information provided in this informational filing relates to the GMC Filing.

Q. HOW WILL YOUR TESTIMONY BE ORGANIZED?

In this testimony I will:

1) Discuss the relationship of this informational filing to the GMC Filing;

2) Discuss the open nature of the ISO's 2001 budgeting process;

3) Discuss the causes for the increase in the ISO's revenue requirement from 2000 to 2001;

4) Compare the cost allocation process with that set forth in the GMC Filing; and

5) Discuss changes in the budget from initial stakeholder review, including billing determinant forecast revisions and the overall effect on the proposed rates.

Q. ARE YOU SPONSORING ANY DOCUMENTS IN CONNECTION WITH YOUR DIRECT TESTIMONY?

A. Yes, I am sponsoring Attachments C-F, which were prepared under my direction and supervision. These documents include the Federal Energy Regulatory Commission ("FERC") Section 35.13 cost statements (Attachment

C), the Cost Allocation Matrix which supports the allocation of costs to the various ISO services, and the documentary support for the Cost Allocation Matrix, entitled "Analytical Support for the California ISO Grid Management Charge". The Cost Allocation Matrix is included as Appendix A to the Analytical Support document, which is itself Attachment D to this filing. Attachment E is the budget posting that was posted to the ISO's website on September 28, 2000 for stakeholder review. Attachment F is the budget as approved on November 30, 2000 by the ISO Board of Governors.

Q. AS YOU TESTIFY, WILL YOU BE USING ANY SPECIALIZED TERMS?

A. Yes, I will use capitalized terms as defined in the Master Definitions Supplement, Appendix A of the ISO Tariff.

Q. HOW DOES THIS FILING RELATE TO THE GMC FILING OF NOVEMBER 1, 2000?

A. The GMC Filing proposes the rate structure through which the ISO will recover its costs of operations. Specifically, the ISO proposes a new formula rate to replace the bundled GMC that the ISO has had in place since the inception of its operations in 1998. In the instant filing, the ISO provides the information necessary to calculate that formula rate and to allow the ISO to begin collecting the unbundled GMC effective January 1, 2001. This filing also provides information on the ISO's 2001 Budget, how the costs in that

budget were assigned to the ISO's three unbundled service categories, and how the overall rates were calculated.

Q. DID STAKEHOLDERS HAVE AN OPPORTUNITY TO REVIEW AND COMMENT ON THE ISO BUDGET?

A. Yes. The ISO operates an open, extended budget process that provides substantial opportunity for stakeholder comment on the ISO proposed budget. As described in my Direct Testimony in the GMC Filing, the process is as follows:

> The budget process begins in June and lasts through December. In June, the ISO's various divisions begin preparation of their proposed budgets for the subsequent year. These budgets are reviewed and modified through several iterations. By August, a proposed preliminary budget is completed and presented to the ISO's Finance Committee for comments and guidance. In September, the proposed budget is made available to the public through posting on the ISO's website. Stakeholders are invited to submit comments and ask questions about the budget, and the ISO conducts a public budget meeting in October for this purpose. In November, the ISO Board is provided with a summary of stakeholder comments received by the ISO, and the final version of the budget is submitted to the Board for approval. In December, the ISO staff prepares and submits the approved budget in the form of an informational filing with FERC.

GMC Filing, Ex. No. ISO-7, at 21. That process has been followed in developing this budget filing. In fact, the discussions concerning the 2001 Budget were even more extensive than in earlier years.

The proposed budget, providing for a total revenue requirement of $225,307,000, initially was presented to the Board's Finance Committee on September 21, 2000. ISO management presented various budget options providing for different levels of service and resultant costs and rates. To keep costs as low as possible, one alternative provided for a budget that would maintain service at the level provided during 2000, while a higher cost option provided resources to fund needed changes the ISO was expected to confront in 2001. The Finance Committee provided guidance and directed management to proceed with the budget proposal that included the resources necessary for the ISO to be fully responsive to the issues anticipated in 2001, including but not limited to Comprehensive Market Redesign, energy management system replacement, and ongoing investigations of the electric market by various governmental agencies.

Q. WHAT WERE THE NEXT KEY EVENTS IN THE 2001 BUDGET PROCESS?

A. The proposed budget was posted to the ISO's website on September 28, 2000. The ISO held its public budget workshop on October 19, 2000. The workshop was attended by the ISO officers, various managers and staff, and stakeholders. In the four-hour meeting, the budget was examined in great detail, and all interested parties were given the opportunity to participate in the discussion. On October 26, management presented the proposed budget to the Board. At that Board meeting, ISO management also provided an update on the status of the budget and the results of the October 19, 2000

meeting with stakeholders. After discussion, the Board directed ISO management to develop options to lower the budget. Management developed a list of possible cost reductions and presented these to the Finance Committee at its November 13, 2000 meeting. The Finance Committee voted to proceed with the budget initially presented, providing for a total revenue requirement of $225,307,000. The Board received further stakeholder comments at its November 30, 2000 Board meeting and then approved the budget at this level. The information contained in this filing results from the budget approved by the Board. The Board vote approving the 2001 Budget is included with this filing as Attachment G.

Q. HOW DOES THE 2001 ISO BUDGET DIFFER FROM THE 2000 BUDGET?

A. Overall, the ISO's total revenue requirement has increased from $178 million in fiscal year 2000, to $225 million in fiscal year 2001. The increase is attributable to increases in both the ongoing operation and maintenance ("O&M") costs of the ISO, and with debt service costs used to repay borrowings made to fund ISO capital expenditures.

Q. WHAT WERE THE CAUSES OF THE INCREASE IN O&M COSTS?

A. In short, an increase in responsibilities and tasks performed by the ISO, and continued changes to our market rules and structure, increased the ISO's cost of doing business. Since startup in March 1998, the ISO has added substantially to its responsibilities, and has had to perform vital functions to

ensure the reliability of the grid that were not originally contemplated. For instance, the ISO has had to lead efforts to encourage demand responsiveness programs in light of the tight energy supplies available to meet demand. Additionally, continued modifications to our market rules have required substantial changes to ISO computer software used to operate the grid and ISO markets. These changes have required not only up-front capital investments, but ongoing support costs for software maintenance agreements, computer hardware leases, and additional staff. Examples of this type of impact to our O&M costs include the ancillary service redesign efforts in 1999 and 2000, and the ongoing Comprehensive Market Design efforts, which will be implemented beginning in 2001. These efforts have caused and will continue to require substantial changes to ISO computer systems and staff that result in an increase in the ISO's ongoing costs. The ISO has also had to invest in tools and staffing to help it manage the grid effectively (for example procedures to handle out-of-market energy calls) and to meet regulatory requirements (for example, North American Electric Reliability Council-mandated Electronic Tagging requirements).

Q. WHAT CAUSED THE INCREASE IN DEBT SERVICE COSTS?

A. Increased debt service costs are a result of the ISO's capital spending program. Since our initial borrowing in 1998, which provided for $300 million for startup and development costs, we have had to borrow an additional $35 million in 2000, and will make a bond issuance in 2001 to cover capital

expenditures in that year and possibly future years. As noted above, our capital spending has been necessary to implement changes to our market rules, as well as to accommodate the overall increase in responsibilities and number of tasks performed by the ISO. The 2001 debt issuance (for which the ISO will submit shortly a Section 204 filing) will provide funding for several initiatives including:

- Replacement of the energy management system in 2001 to provide for a system that costs less to maintain in the future, and provides the functionality necessary to reliability operate the grid.
- Implement Congestion Management Reform/Comprehensive Market Redesign in accordance with FERC orders.
- Other system changes, including general information technology needs, other reliability-related enhancements, and facilities-related needs.

As noted in my Direct Testimony in the GMC Filing, the ISO publishes a proposed level of capital spending as part of its budget process, supported by a list of anticipated capital projects. The actual projects approved and implemented during the budget year, however, may differ from the list of projects supporting the budget. All proposed capital projects are subjected to an internal review process, and all projects with a value in excess of $1 million are reviewed and approved by the Board. The debt service included in the instant filing is related to the $37.774 million approved capital budget for 2001, and all spending from this budget will be subject to this review process.

Q. WAS THE COST ALLOCATION PROCESS PERFORMED IN THE MANNER OUTLINED IN THE GMC FILING?

A. Yes. The support for the O&M cost allocations were provided by the ISO managers to the ISO Finance Department, which applied that data to the approved 2001 Budget by cost centers (which are the areas of responsibility used to monitor and manage ISO costs). The ISO Finance Department then converted this data into the FERC account format required for this informational filing. The allocation methods used for each ISO cost centers are discussed in detail in the support for the "Analytical Support for California ISO Grid Management Charge" (Attachment D). The ISO's fixed assets were analyzed in the same manner as described in the GMC Filing and assigned to the service categories as appropriate.

The GMC Filing contained 1999 data to demonstrate the proposed unbundled structure. The instant filing provides additional information on year 2000 capital spending and proposed year 2001 capital spending. These items affect the allocation of debt service costs to the three Service Categories.

Q. WERE THERE SIGNIFICANT CHANGES IN THE RESULTS OF THE COST ALLOCATION PROCESS FROM THE 1999 DATA USED IN THE GMC FILING?

A. The overall results of the allocation process changed slightly. Based on 1999 cost data and assumptions, the percentage of ISO costs allocated to the

Control Area Services category changed from 45.1 percent in 1999 to 48.1 percent in 2001, while for the Inter-Zonal Scheduling category, the change was from 7.4 percent to 8.7 percent. For the Market Operations category, the change was from 47.5 percent to 43.2 percent in 2001. These changes are due to different allocation factors provided by each department, changes to the treatment of certain overhead costs, analysis of additional capital spending made by the ISO during 2000, and the inclusion of the planned 2001 debt issuance in the cost base.

Q. HOW WERE THE BILLING DETERMINANT FORECASTS DEVELOPED?

A. I discussed the billing determinant forecast development process in my Direct Testimony in the GMC Filing. We followed that approach in establishing the final estimates used in this informational filing, but we modified the forecasts after the preliminary budget was posted for stakeholder review on September 28, 2000. These modifications were necessary due to two factors: 1) better information on Control Area Gross Load, and 2) FERC's preliminary order issued on November 1, 2000 in Docket Nos. EL00-95-000, *et al*. ("November 1 Order"). As to the first item, the ISO continued to obtain better information on projected generation from Qualifying Facilities throughout October 2000. This resulted in a revision downward of the total Control Area Gross Load forecast for 2001. As to the second item, we modified our billing determinant forecast as a result of the anticipated impact of the November 1, 2000 Order, which contained a proposed modification to the ISO's market rules that would

have the effect of discouraging reliance on the ISO's Real Time energy markets. As a result, we revised downward the total energy volume we anticipate will be traded through the ISO's market, and accordingly the billing determinant for the Market Operations charge was reduced from 116,015,000 MWh to 102,394,000 MWh. Also, as a result of the same provision in the November 1 Order, we increased the forecasted billing determinant for the Inter-Zonal Scheduling category from 80,941,000 MWh to 87,536,000 MWh. These modifications were disclosed prior to the Board's vote on the budget on November 30, 2000 through a posting on the ISO's web site.

Q. WHAT WAS THE EFFECT OF THESE CHANGES ON THE RATES NOW PROPOSED COMPARED TO THE RATES POSTED ON SEPTEMBER 28?

The effect of the changes in the billing determinants noted above, and minor changes to the cost allocation percentages from the preliminary percentages posted on September 28, 2000 on the ultimate rates were as follows:

Category	Rate per 9/28/2000 Web posting	ISO Board Approved Budget & Rate
Control Area Operations	$.413	$.406
Inter-Zonal Scheduling	$.220	$.223
Market Operations	$.829	$.951

In the September 28, 2000 posting, we noted that such changes could result as the ISO assessed various factors. The following footnote was included in the September 28 posting on page 9, entitled "FY2000/FY2001 UNBUNDLED GRID MANAGEMENT CHARGE COMPARISONS"

Note:
Supporting documentation for GMC unbundling will be released subsequently. Billing determinants volumes may change based on market redesign and Ten-minute Settlements.

The Market Operations rate increased the most substantially of the three rates due to the decrease in the forecasted billing determinant volume for that Service Category, and an increase in the percentage of total ISO costs allocated to that Service Category (from 42.7 percent to 43.2 percent.) The Control Area Services charge decreased due to a reduction in the costs allocated to that category (from 49.4 percent to 48.1 percent) but was offset slightly by a decrease in the billing determinant volume from 269,803,000 MWh to 267,289,000 MWh. The rate for the Inter-Zonal Scheduling component increased slightly from $0.220 to $0.223 as a result of an increase in the costs allocated to this service from 7.9 percent to 8.7 percent, offset by an increase in the billing determinant volume from 80,941,000 MWh to 87,536,000 MWh.

The ISO could have retained the original rates as posted on September 28, 2000, but believed it was more important to have the rates reflect the most current and accurate information on ISO costs and projected billing determinant volumes.

Q. THANK YOU, MR. LEIBER. I HAVE NO FURTHER QUESTIONS.