

**AMERICAN ARBITRATION ASSOCIATION
COMMERCIAL ARBITRATION TRIBUNAL**

Arbitration Re:

Case No. 74 198 Y 00625 04

PACIFIC GAS & ELECTRIC COMPANY et al.

Claimant

v.

CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION

Respondent

FINAL AWARD AND DECISION

(September 30, 2005)

I. Introduction and Summary of Procedural History

This final arbitration award and decision is issued pursuant to Sections 13.3.10 and 13.3.11.1 of the Dispute Resolution Procedure (“DRP”) in the Federal Energy Regulatory Commission (“FERC”) Electric Tariff of the California Independent System Operator Corporation (“CA ISO” or “ISO”), as well as the schedule and procedures adopted by the arbitrator’s various orders in this American Arbitration Association (“AAA”) proceeding.

This arbitration was initiated with the AAA by Pacific Gas & Electric Company (“PG&E”) against CA ISO on June 10, 2004, under Article 13 of the CA ISO FERC Electric Tariff (“Tariff” or “CA ISO Tariff”). (Item by Reference 1, hereafter “IBR-1”).

On October 10, 2004, AAA formally appointed the undersigned as the sole arbitrator pursuant to the DRP, (Exhibit Arbitrator No. 2, hereafter “Ex. Arb-2”), and these extensive and lengthy proceedings commenced. CA ISO filed a formal answer to the PG&E claim on November 11, 2004.

The following entities submitted interventions and became parties at the outset under Supplemental Procedure 3.3 of the DRP: Southern California Edison Company (“SCE”); Transmission Agency of Northern California (“TANC”); City of Santa Clara (“SVP”); City of Redding (“Redding”); Modesto Irrigation District (“MID”); M-S-R Public Power Agency (“MSR”); Turlock Irrigation District (“TID”); Northern California Power Agency (“NCPA”) and Sacramento Municipal Utility District (“SMUD”). Subsequently, and at various times, NCPA, SCE, SVP, M-S-R and TID withdrew from the arbitration (on November 13, 2004; March 29, 2005; April 1, 2005; April 1, 2005; and April 22, 2005, respectively).

The SMUD, TANC, MID, and Redding intervening parties (hereafter “Joint Intervenors”) fully participated in the entire case through counsel, including in the evidentiary hearings, all briefing and final oral arguments. The Joint Intervenors aligned as a group with PG&E on all key issues.

The date for the final award in this arbitration, pursuant to DRP Section 13.3.10 (which envisions issuance of a final award within six months from date of the appointment of the arbitrator) was extended on two occasions at the request of, and/or with full concurrence of, all parties. At the initial pre-hearing conference in October 2004, the end-date was originally established as August 31, 2005, in order to accommodate CA ISO’s and SCE’s notice that a summary disposition motion phase was

required. Extensive briefing and in-person oral arguments on that threshold, and potentially dispositive, stage concluded in February 2005. With issuance of an order denying summary disposition in March 2005, the decision due date then was extended to September 15, 2005, with hearings scheduled for mid-July 2005. At the close of those evidentiary hearings, the award date was extended a second time to September 30, 2005, to allow for the full review and consideration by the arbitrator of additional post-hearing briefing, the large number of lengthy exhibits, the extensive evidentiary record, voluminous legal/regulatory authority, and the in-person post-hearing oral arguments scheduled for August 30, 2005. (Hearing Transcript at pages 884-885, hereafter “Tr. 884-885”).

There have been a number of important interim orders issued in this arbitration. The most significant was the March 11, 2005, lengthy order denying CA ISO’s (and then-party SCE’s) motions for summary disposition, as described above, because the movants had not satisfied the unique and high standard for such disposition established in DRP Section 13.3.6. Another important order was issued on May 10, 2005, concerning PG&E’s motion for official notice of limited portions of the evidentiary record in an earlier arbitration, arguably applicable to the matters involved here. Finally, on May 19, 2005, the arbitrator issued an order concerning a CA ISO motion to strike portions of the prepared filed testimony of PG&E and Joint Intervenors. Those three motions and their resulting orders are discussed in various sections of this award where appropriate.

Four full days of evidentiary hearings were held in San Francisco, California, from July 12 to July 15, 2005. The evidentiary record formally closed at the end of the hearings on July 15. Five witnesses appeared -- three for PG&E, one for SMUD and one

for CA ISO (all of whom had submitted prepared direct and rebuttal testimony) -- and were cross-examined, resulting in 895 pages of transcribed examination. In total, 105 exhibits and items-by-reference became part of the evidentiary record.

The parties submitted three initial post-trial briefs, totaling 104 pages, on August 2, 2005, and three reply briefs, totaling 70 pages, on August 17, 2005. At least half of those briefs were accompanied by lengthy appendices of materials. A final oral argument of approximately five hours was held in San Francisco on August 30, 2005. (Transcript of August 30, 2005, Oral Arguments at pages 896-1130, hereafter “Orals Tr. at 896-1130”).

With this arbitrator having fully reviewed and considered the fulsome testimonial record, as well as all of the exhibits, briefs and arguments, the matter is now fully ripe for decision/award.

At the final day of the evidentiary hearings on July 15, 2005, all of the parties concurred that a typical “reasoned” arbitration award in the following form and detail would fully satisfy the requirement of DRP Section 13.3.11.1 that the written decision “shall include findings of fact and law.” (Tr. 883-884).

In addition, despite some intimation earlier in the arbitration (by SCE, in particular, before it withdrew) that there might be some limitations on the jurisdiction of the arbitrator in terms of the non-arbitrability of certain matters, the parties all concurred in the end that no such potential barriers existed. (Orals Tr. 1083-1084). Thus, findings and conclusions on all of the key issues raised in the arbitration follow.

No attempt has been made to address and/or dispose of all arguments raised in the extensive post-hearing briefing or at the oral argument session. That would require a

written award/decision even more voluminous than the one already required by the extensive record, briefing and argument. However, all of the claims at the heart of the matter are fully addressed herein.

II. The Basic Dispute and Its Background

The dispute here has its roots in the California energy crisis of 2001 and centers around so-called Must Offer Obligation Charges (“MOO Charges” or “MOO”) billed by CA ISO to PG&E beginning in June of that year. The imposition of those charges to PG&E technically ended as of December 31, 2004, (PG&E Exhibit No. 3, Attachment 1, hereafter “Ex. PGE-3, Att. 1”), but the parties all acknowledged that final calculation of those charges and their reflection in the regular settlement statements from CA ISO to PG&E have continued to the present time, as they are “subject to adjustment based on reruns in the CA ISO Market.” (CA ISO Initial Brief at page 49, hereafter “CA ISO IB at 49”). While the parties fully concur that the charges in dispute, to the date of the closing of the evidentiary record on July 15, 2005, total \$14,319,378.14, (Ex. PGE-3; Tr. 415-416; Orals Tr. 940 and 1072), the final charges involved cannot be fully measured as of the date of this decision. The implications of that are addressed in the concluding order section of this award.

The MOO Charges consist of three separate components and arise collectively in three distinct sections of the Tariff: Section 2.5.23.3.6.1 (Emissions Cost Charges), Section 2.5.23.3.7.1(Start-Up Costs), and Section 5.11.6.1.4 (Minimum Load Cost Compensation Charges). (IBR-1). These charges came into existence when, as part of the mitigation plans for the California energy crisis, FERC authorized CA ISO to pay generators in the state for the three referenced services, in part, to ensure system

reliability. [See San Diego Gas & Electric Co., 95 FERC 61,418 (2001) and Exhibit No. PG&E 2 at p. 3, hereafter “Ex. PGE-2 at 3].

PG&E and its supporting Joint Intervenors urged that the imposition or levy of the MOO Charges on PG&E, as related solely to any transmission transactions on, or schedules involving, the California-Oregon Transmission Project (“COTP”) and/or so-called “Bubble” transactions are unauthorized and impermissible under the Tariff. Consequently, PG&E (and Joint Intervenors) seeks recovery by PG&E of all such charges already paid and relief from any such additional obligations. Importantly, PG&E did not dispute the imposition of MOO Charges for any and all transactions not involving the COTP or the Bubble (and there are presumably many), so application of such charges in those other circumstances was not at issue in this arbitration. (PG&E-2 at 6-7 and Orals Tr. 942).

CA ISO’s fundamental position was that the MOO Charges as applied to COTP and Bubble transactions are authorized and fully collectible for such transactions. Hence, CA ISO maintained no refunds are in order.

For purposes of this arbitration, COTP is the major transmission line connecting the two states, while the Bubble consists of facilities owned by the Western Area Power Administration or SMUD for which transactions are not scheduled over facilities that are part of the ISO Controlled Grid, as that term is defined in the ISO Tariff. (Exhibit No. SMUD 5, hereafter “Ex. SMUD-5” and Exhibit No. SMUD 16, hereafter “Ex. SMUD-16”).

By way of further background, there are two important matters to address at the outset surrounding the central dispute here. First, there was an earlier AAA arbitration

(Case No. 71 198 00711 00) in 2000-2001 concerning COTP and Bubble charges from the CA ISO to PG&E, but involving different charges under the Tariff (other than MOO) -- so-called "ancillary services." The arbitrator in that case issued a comprehensive 22-page, single-spaced award in December of 2001 which addressed some, but certainly not all, of the issues presented in the instant arbitration. (Ex. SMUD-16). That arbitration has been referred to in this case as "COTP I".

In this arbitration--sometimes referred to as "COTP II" -- there was a great deal of controversy and dispute about the application of that earlier arbitration to this case. PG&E and the Joint Intervenors maintained that the earlier arbitration is very much applicable and, in large part, controls the results. CA ISO argued the opposite. That important, underlying controversy is addressed at length and resolved as part of the analysis in this award.

CA ISO sought review of that earlier COTP I arbitration award at FERC under the Tariff (see the paragraphs at the end of this subsection of the award for further discussion of FERC's review powers under the Tariff) and that agency has issued three separate decisions or orders, to date, on the appeal/review of COTP I: Order Denying Review, 107 FERC 61,152 ("May 10 Order")(2004); Order Denying Rehearing , 111 FERC 61,078 ("April 18 Order") (2005); and an Order Granting Rehearing For Further Consideration, ("June 17 Order") (2005). [The April 18 FERC order is a formal exhibit (Exhibit No. SMUD 17, hereafter "Ex. SMUD-17) here.] Importantly, the parts of the arbitrator's decision in COTP I arguably applicable to this case have been fully upheld by FERC in its orders, as further addressed later in this award.

Finally, with respect to the COTP I arbitration award and the subsequent FERC orders, it should be noted that the applicable DRP provision in the Tariff specifically provides that an arbitrator “may consider relevant decisions in previous arbitration proceedings.” (Ex. Arb-2, Sec.13.3.11.1). As will be seen, this award has done just that, where appropriate.

A second supplemental background matter to note is the right of appeal to or review of this award, or any arbitration award, by FERC under the Tariff. An arbitrator deciding a CA ISO Tariff case must keep that framework fully in mind, as the responsibility to properly interpret and apply FERC precedent is a significant overlay to the usual, and already imposing, obligations of an arbitrator to render a fair and just award, within the law, based on all of the record evidence and all arguments. Specifically, the Tariff provides that when an appeal to FERC is taken from an arbitration case, the agency will “afford substantial deference to the factual findings of the arbitrator” and, except for limited exceptions, the agency will not permit expansion of the record created in the arbitration. (Ex. Arb-2, Section 13.4.2).

In fact, that is precisely what the agency did in its review of the arbitrator’s award in COTP I, in fleshing out the DRP Section 13.4.2 review provision. FERC explicitly recognized, in upholding the COTP I arbitrator’s award, the “value of parties seeking to resolve disputes through means other than formal litigation before the Commission... and it is desirable and appropriate, if otherwise consistent with the public interest, for the Commission to adhere to the results of a binding arbitration award... .” (May 10 Order at 8, emphasis added).

This arbitrator was very much aware of this unique legal and procedural construct as he undertook his responsibilities here. This award attempts to fully honor the important principles embodied in that Tariff framework, recognizing the reliance that FERC must, and will, place on this award and the extensive record that has been created in this arbitration. As will be seen later, the arbitrator here allowed an expansive (but proper) record to be created so FERC would have everything possibly relevant and necessary for any subsequent review by it under the Tariff. And this award is explicit in explaining the weight applied to crucial parts of the record in order to provide a complete foundation for FERC, if required.

III. Legal Framework: The FERC Tariff

The starting point for the analysis here must be the Tariff as it is the applicable rate schedule upon which the charges at issue arise and is the “controlling law”, in effect. Thus, the consideration of the CA ISO’s legal authority to impose the disputed charges must start with the provisions of the Tariff, itself.

As the arbitrator in COTP I quite properly noted in his 2001 award: “As a FERC-jurisdictional utility, CA ISO’s threshold obligation with regard to imposing charges is to demonstrate that they are authorized by a tariff on file at FERC. Montana –Dakota Utilities C. v. Northwestern Public Service Co, 341 U.S. 246, 251-52 (1951); Maine Public Service Co. v. FERC, 579 F. 2d 659 (1st Cir 1978).” (Ex. SMUD-16 at 4). This oft-stated, and important, principle must apply in this case as well. There was no real dispute among the parties on this essential concept. As CA ISO stated on brief: “If the ISO lacks authority under rates on file with the Commission, the ISO cannot bill PG&E.” (CA ISO IB at 45).

The parties also agreed at oral arguments that the applicable Tariff language on each of the three separate MOO Charges is virtually identical with respect to the three components (Emissions, Startup and Minimum Load) and that there is no substantive difference in the language of the components, for purposes of the analysis. (Orals Tr. at 1050-1052). The crucial language, for one of the components, is as follows in full:

2.5.23.3.6.1 Obligation to Pay Emissions Cost Charges

Each Scheduling Coordinator shall be obligated to pay a charge which will be used to pay the verified Emissions Costs incurred by a Must-Offer Generator as a direct result of an ISO Dispatch instruction, in accordance with this Section 2.5.23.3.6. The ISO shall levy this administrative charge (“Emissions Cost Charge”) each month, against all Scheduling Coordinators based upon each Scheduling Coordinator’s Control Area Gross Load and Demand within California outside of the ISO Control Area that is served by exports from the ISO Control Area. Scheduling Coordinators shall make payment for all Emissions Cost Charges in accordance with the ISO Payments Calendar. (emphasis added).

Again, all agree the other two charges involved (standby and minimum load) embody the same fundamental requirements.

Many of CA ISO’s arguments in this case focused on the “based upon” language above in the relevant Tariff sections and that will be addressed in this award. The key fact, though, is that the Tariff’s explicit language is unequivocally clear that it is Scheduling Coordinators (hereafter “SCs”, or “SC” in the singular) upon whom MOO Charges are to be levied and it is SCs only who are obligated to and do make payments, accordingly.

The essence of the dispute here, then, came down to whether it can be concluded definitively that PG&E is an SC for purposes of transactions on the COTP or the Bubble as it relates to MOO Charges, regardless of upon what such charges are “based”. It is

interesting to note that CA ISO's sole witness in the case, Mr. Fuller, appeared to concede and concur in this point that charges can only be imposed on SCs. (Tr. 823).

To the extent that PG&E is not an SC, billing to it under the Tariff for such transactions would be improper by definition. On the other hand, if PG&E is an SC for any reason, then CA ISO's theory of the case would be correct and the billing here would be proper. Unfortunately, there is no precise language in the Tariff providing a totally clear answer and there is great disagreement between the parties on the question. That is what the arbitration is about and, thus, that debate underlies the thrust of the analysis in this award.

IV. Legal and Factual Conclusions and Analysis

A. Introduction and Overall Summary of Result

Once again, under the applicable legal framework, it was ultimately CA ISO's threshold obligation to establish that it has the authority to impose the disputed charges. It was the concomitant duty of this arbitrator under the Tariff to evaluate whether such lawful authority credibly exists. While, at times, the parties may not have framed the central issue this way, (see e.g CA ISO RB 1-3), that had to be the approach to the analysis.

In an attempt to establish its case, CA ISO put forward a series of intricate, in-depth arguments for which it found support largely in several important FERC decisions rendered over recent years in often complex and hotly contested cases involving various aspects of Tariff implementation and administration. Those CA ISO positions are simplified and addressed at length beginning in the immediately following subsection of this decision.

That is then followed by an analysis of the key positions of PG&E and Joint Intervenors, as to why no such authority indeed exists, either factually or as a matter of law, to impose MOO Charges on COTP/Bubble transactions.

A word is in order as to why the analysis and conclusions on the CA ISO's position were presented first. This was not a comment on, or reflection of, the allocation of the burden of proof in this arbitration, which indeed was carried out in accord with the usual allocation in civil and regulatory litigation (and as the parties concurred in oral arguments was proper). Rather, this award has been so organized because it is logical, in that CA ISO had the ultimate obligation to establish the basis of the authority to bill the charges at issue. In light of that, it made sense to present the analysis of the validity of the theories/arguments of CA ISO as to the existence of such authority before addressing the arguments of PG&E and Joint Intervenors as to why such authority does not, and cannot, exist independent of the CA ISO positions.

In the end, after balancing all of the facts on the record and the arguments, this arbitrator was more persuaded by the case established by PG&E and Joint Intervenors, for the multiple reasons that follow. The intricate "web" of arguments that CA ISO weaved was indeed creative and comprehensive, but ultimately called for impermissible speculation or conjecture on the part of the decision maker, did not stand up fully to close inquiry in all respects and, in the end, did not establish that the authority to bill the charges at issue is clear enough to support their imposition. When all is said and done, the arguments and evidence of PG&E and Joint Intervenors proved more definitive and persuasive.

However, the arbitrator acknowledges that in coming to this ultimate result, it was necessary, at times, to engage in difficult interpretation of arguably ambiguous FERC decisions, rendered over many years, touching upon related issues. If a regulatory appeal is taken from this award/decision, which all parties seemed to predict would occur, and the agency has a different view of its own precedent than that presented here because it has the institutional advantage of insights that could not be gleaned fully from its earlier written decisions, as understood by this experienced arbitrator and/or the expert witnesses appearing before him here, then so be it. It appears FERC will have an opportunity to do that. Of course, this award and the analysis could not predict, or be expected to have predicted, if FERC and its Commissioners may have such insights. This award could only be based on the written words in existence as applied to the facts adduced.

It also should be noted at the outset that a number of the arguments presented, from all parties, urged the arbitrator to take into account allegedly inconsistent positions/statements made in historic pleadings in an array of earlier regulatory proceedings, as compared to positions ultimately taken in this arbitration. In fact, a number of exhibits or pleadings apparently were introduced and referenced in briefing solely for that purpose.

It would have taken numerous additional pages of this award to lay out the multiple claims of such argument inconsistency, analyze each as to their individual probity, and then it probably would have been impossible to reach any definitive conclusion as to any, if not all, of them. In reality, it appeared overall that most of these inconsistency arguments just reflected vigorous and good advocacy on very complex matters in this case and/or in those earlier proceedings.

In any event, the arbitrator was unimpressed, in nearly all instances, by the claims of advocacy inconsistency as probative of the real issues at hand. The award's conclusions had to be based on the record created and, most importantly, the fair and thorough analysis of the relevant legal/regulatory precedent. Therefore, this award has made little mention of the numerous inconsistency claims, except in a few isolated incidences where they had some meaningful probative impact on the outcome of a specific issue involved.

B. Evaluation of CA ISO Arguments on Why PG&E is an SC for the MOO Charges as to COTP/Bubble Transactions

1. A Starting Point?: If Not PG&E, Then Who?

In setting the stage for its key arguments based on the Tariff, related agreements, and FERC orders, CA ISO explicitly raised a threshold “condundrum” (its counsel’s words at oral argument, Orals Tr. 1045) as follows: who is to be billed for the MOO Charges on COTP/Bubble transactions, if not PG&E? (Orals Tr. 1044-1048). CA ISO’s briefs also raised this concept. As counsel for CA ISO emphasized at the end of the case: “[I]t’s a simple question....If PG&E is not the Scheduling Coordinator to bill, then who is....?” (Orals Tr. 1044).

CA ISO insisted that this proposed inquiry was not part of an overall “equitable” argument to support its basic position in the case, (Orals Tr. 1041-1042), and the arbitrator accepted that (even though at times CA ISO urged that this case involved PG&E’s attempt to get a “free ride”). After all, this decision could not be based on such “equities”, but rather had to rest on the Tariff’s language and FERC’s historic interpretations of it. (See Section IV.B.3.b. below for further discussion of the application of equitable principles in a different context).

However, this award could not totally ignore, without comment, this CA ISO issue of “who to bill, if not PG&E”. Simply put, it was not, and could not have been, the place of this award/decision to even consider that question. If, as this decision has concluded, PG&E is not the proper entity (SC) to be billed the MOO Charges as to the COTP/Bubble transactions, then the question of what happens alternatively was not for this case, particularly where there was no adequate record on the subject.

While the arbitrator suspected there may be other ways for CA ISO to seek the recovery of the apparently legitimate costs involved if not from PG&E in the manner here (and PG&E very well may be responsible for some significant portion under such a mechanism because of its relative size), this arbitrator did not have any jurisdiction under the Tariff, or a record available, to factor it into his decision in any way. Presumably, if the CA ISO conundrum is to be answered ever, then it must be for FERC (and/or another arbitrator) in another context.

2. The Heart of the Matter: The Tariff, the RPTOA and Opinion 463-A

Prior to considering CA ISO’s theories on why its position is correct and its interpretation of the Tariff and FERC precedent construing it and related agreements is proper, there was one other preliminary issue that needed to be addressed. That was the question of whether CA ISO had to be accorded any special deference in interpretation of its “own” tariff and earlier FERC decisions under it, as well as related agreements, as compared to the positions/views of any other party.

The simple answer is no. That is the law that must apply and, and in any event, CA ISO appeared to have conceded the point, (Orals Tr. 1085), which it apparently pursued with some vigor in the COTP I arbitration. In case there was any remaining

question, however, this topic was fully disposed of in the COTP I arbitrator's award, when it noted: "it is inconsistent with the basic notion of regulatory oversight that such deference should be afforded to a tariff-filing utility." (Ex. SMUD 16 at 7, emphasis added). This award fully concurs and adopts that analysis.

Having disposed of that, this award turns to the heart of CA ISO's fundamental position that PG&E is indeed an SC which can be billed MOO Charges on COTP/Bubble transactions. The thrust of CA ISO's position seemed to have two key components or central themes when all of its arguments were simplified to the base components.

First, CA ISO maintained that when FERC approved inclusion of the MOO Charges in the Tariff in the first place in 2001, (San Diego Gas & Elec. Co., 97 FERC 61,293), FERC made it clear that such charges are to be allocated to "all users of the transmission system, i.e. all Demand within the ISO Control Area and all Demand within California that is served by exports from the ISO Control Area" for any and all grid charges. (CA ISO IB at 3,7-8). Put simply, CA ISO's first position appeared to be that FERC ruled specifically that it is proper to bill for any load on the grid; whether or not a COTP or Bubble transaction is involved or whether PG&E is an SC. In light of that, CA ISO, in essence, argued further that the COTP I decisions are irrelevant to this case because that earlier arbitration involved different charges (Ancillary Services).

This initial argument of CA ISO has several inherent weaknesses and ultimately was neither persuasive nor provided the required authority to clearly support application of the MOO Charges as urged here.

First, a thorough reading of the MOO Charges decision(s) did not reveal any language that would fairly lead to a conclusion that FERC intended to have that decision carry forward as far as CA ISO urged.

Most importantly, to accept this initial theory of CA ISO, one would have had to conclude that the SC language in the MOO Charge sections of the Tariff was, in effect, irrelevant and superfluous. The Tariff is clear that it is SCs who are to be billed. While it can be agreed that those billings should be determined by “demand for energy within the ISO Control Area” etc., the Tariff is still clear as to who gets billed—and it is only SCs. Therefore, whether PG&E is an SC for purposes of MOO Charges as to transactions on COTP/Bubble was still a critical determination and that requirement of the Tariff could not be sidestepped or, in effect, written out of it. Surely FERC did not intend to do that when the MOO Charges were instituted in 2001. At least there was no indication to that effect in its orders or on the face of the language of the Tariff as approved.

Finally on this point, Joint Intervenors pointed out persuasively that the charges assessed in this case were actually billed based on COTP and Bubble transactions and not on load or demand as CA ISO’s urged. (Orals Tr. 1028). That fact tended to detract from the thrust of CA ISO’s first argument, as well.

CA ISO then moved on from the argument, above, that the Tariff itself (from the time the MOO Charges were approved) permits application of MOO Charges as to COTP/Bubble transactions because of the billing determinant (or demand) language. The second thrust of its “authority” to bill here attempted to persuade that, in effect, PG&E indeed is an SC for MOO Charges as applied to COTP/Bubble transactions. (It is

interesting to note that this argument is made after CA ISO attempted to “write” the SC language “out of” the Tariff, in effect, by its first argument.)

CA ISO’s second key argument was that its authority to bill the MOO Charges as done in this case arises, in effect, from the context of entirely separate charges from MOO-- the Generation Management Charges (“GMC”)—and how those other charges flow from the so-called Responsible Participating Transmission Owner Agreement (“RPTOA”), as interpreted by FERC’s Opinion 463-A. [The RPTOA is both Exhibit No. CA ISO 24, hereafter “Ex. ISO-24”, and Exhibit No. PG&E 1, Exh. 3, hereafter “Ex. PGE-1, Ex.3”; Opinion 463-A is Exhibit No. CA ISO 7, hereafter “Opinion 463-A”]. As counsel for CA ISO said at oral arguments: “In this case, the RPTOA is what makes PG&E the Scheduling Coordinator.” (Orals Tr. at 1092).

Specifically, CA ISO maintained that: “in Opinion 463-A, the Order on Rehearing in the 2001 Grid Management proceeding, the Commission ruled that PG&E is the Scheduling Coordinator for the ISO to bill for GMC Control Area Services Charges allocated to the Control Area Gross Load of Governmental Entities whose Loads are served by COTP transactions.” (CA ISO IB 20). CA ISO then argued, in this case, that the RPTOA and Opinion 463-A’s interpretation of it as to the GMC extends fully and completely to MOO Charges. In essence, then, CA ISO argued the RPTOA has permitted what it was seeking here, since the time the RPTOA came into existence in 1997.

Not surprisingly, this claim of CA ISO, which turned out to be its central one, evoked a vigorous debate in this case about the RPTOA, Opinion 463-A and their application in this case. (See PG&E IB 11-17; JI IB 8-10).

On the whole, this second key argument of CA ISO was not persuasive, ultimately. There were numerous reasons for this. First, no specific language in Opinion 463-A or any related documents indicated that its holding on GMC charges is to apply in the MOO Charges setting here. Rather, even CA ISO acknowledged that its reliance on Opinion 463-A is based on the “logic”, not the language, of Opinion 463-A as applied to the case at hand. However, this arbitrator could not conclude the “logic” so extends.

In reaching this result, the arbitrator was very persuaded by the fact that there was language in the GMC sections of the Tariff, being interpreted in Opinion 463-A, that permitted those charges (as opposed to MOO Charges) to be billed to an “other appropriate party”, in addition to an SC. (Exhibit No. CA ISO 24, hereafter “Ex. ISO-24”). Significantly, that “other appropriate authority” language as to GMC is not found in the MOO Charges context in the Tariff. Again, the MOO provisions in the Tariff have only SCs as permissible billing entities.

Moreover, a close reading of the Initial Decision of the Administrative Law Judge in the GMC case, (Exhibit No. CA ISO 15, hereafter “Ex. ISO-15”), made it clear that the GMC case specifically excluded application of the GMC charges to the COTP or Bubble transactions. While there was a great deal of debate here as to whether that was the case when all is said and done that Initial Decision had to be interpreted to say that, and it was not established that FERC disagreed on its review there.

In addition, CA ISO conceded in the GMC case (in contrast to its position here in one of the inconsistencies that does make a difference) that the then-pending COTP I case (before it was decided and CA ISO lost the issue) would be controlling of whether it could impose any charges on the COTP or Bubble. (Ex. PG&E-2 at 15).

Further, if FERC had meant in Opinion 463-A to be ruling that indeed the CA ISO could bill MOO Charges (as well as GMC) as to COTP/Bubble transactions based on the “logic” of that opinion, as CA ISO urged here, surely FERC would not have ruled, as it did, in May 2004, only four months after Opinion 463-A was issued (when it upheld the arbitrator’s decision in COTP I) that PG&E is not the SC in regard to the COTP and the Bubble. One has to assume that when FERC rules, it has full knowledge of its earlier decisions and their full implications. If the “logic extension” argument CA ISO urged to be derived from Opinion 463-A was correct, then it would be hard to see how it would not have been raised and disposed of in the COTP I decisions. [It also is important to note that all of the agreements and FERC decisions/cases upon which CA ISO relied on, even beyond Opinion 463-A, predated the COTP I decision. (See also Section IV.C.2. herein)].

To accept CA ISO’s RPTOA and Opinion 463-A “logic extension” argument, even if the significant reservations above had not been reached, one would still have needed to come to a conclusion that indeed PG&E is an SC under that agreement to permit application of the MOO Charge billings here. And, by the terms of the RPTOA, that is not the case.

The RPTOA’s language is clearly limiting in scope. It states that PG&E will be the SC for transactions under the contracts listed in the agreement’s Appendix A, exclusively; that is for Existing Contracts of the Existing Rightholders. (Ex. PGE-1, Ex. 3 at 1, Whereas Clause E). For ISO to have authority through the RPTOA to bill PG&E as an SC, the Coordinated Operations Agreement (“COA”), (Exhibit No. SMUD 19, hereafter “Ex. SMUD-19”), governing PG&E’s relationship to the COTP through 2004, would have to have been listed in RPTOA Appendix A. It was not and CA ISO, in effect,

did not dispute that here. (Exhibit No. PGE 8 at JP-ISO-3-11, hereafter “Ex. PGE-8). It is important to note that the arbitrator’s decision in COTP I, in essence, reached a similar conclusion based on the RPTOA’s coverage through the COA. (Ex. SMUD-16 at 17-18).

Finally, it is important to note that the MOO billings in dispute here ended in December of 2004 when the COA terminated. If those charges were not tied to the COA in the first place, why would CA ISO have needed to end them when the COA terminated? That query was never adequately answered here, further undermining CA ISO’s second key argument.

Thus, one cannot find sufficient support in the RPTOA or Opinion 463-A to conclude that PG&E is an SC that can be charged for COTP/Bubble transactions, as CA ISO maintained. CA ISO did attempt to create a theory that the Existing Rightholders language in the RPTOA really should be construed to cover the concept of “Governmental Entities”. Joint Intervenors, particularly, characterized this position as an “invention”.... “out of whole cloth” and a “diversion and obfuscation”. (JI RB at 5-6). In the end, CA ISO’s theory to that effect did appear to be a “legal fiction” and was not adequately supported, factually or legally, and ultimately did not make logical sense in light of the express language of the RPTOA and its historic interpretations by FERC.

There also is testimonial evidence in the record of this arbitration (as there was in COTP I) on the RPTOA and the meaning of Opinion 463-A that supported the conclusions above on the meaning of the RPTOA, as interpreted by Opinion 463-A and its argued extension to the case at hand. As detailed at length in Section IV.C. 2., below, of this award, there was an extensive dispute in this case about the use of such testimonial evidence. That issue is fully addressed in that later section of this award. In light of that

subsequent discussion, however, this award has concluded that some weight can and should be applied to such testimony and that has application on this RPTOA and Opinion 463-A issue.

The testimony of PG&E's witness Mr. Bray, which was not rebutted factually by CA ISO, was persuasive and credible. That testimony clearly explained why Opinion 463-A did not cover COTP/Bubble matters. (Ex. PGE-2). Similarly, the testimony of PG&E witness, Ms. Eschbach, was persuasive and credible that PG&E's intent in entering into the RPTOA was to be the SC only for contract listed in Appendix A of the RPTOA. (Ex. PGE-1). Ms. Eschbach also testified in support of the proposition that for ISO to have authority through the RPTOA to bill PG&E here as SC, the Coordinated Operations Agreement (COA"), which governed PG&E's relationship to the COTP through 2004, would have to be listed in RPTOA, Appendix A. And, CA ISO admitted that the COA was not so listed. (Ex. PGE-8).

While none of this testimony extrinsic to the Tariff or FERC opinion language was dispositive of the ultimate issues here, it did provide almost totally unrebutted support to buttress the interpretations and legal conclusions that undermined CA ISO's theory as to from where its required authority was derived.

There are a number of additional reasons that this award concludes that CA ISO's "theory" that the RPTOA and Opinion 463-A provided it with the requisite authority here had to fail, in the end.

CA ISO's reliance on the "behind-the-meter" analogy from the Opinion 463-A case as applied here appeared misplaced. As SMUD's witness, Mr. Jobson established, behind-the-meter load is distinct and separate from COTP and Bubble. (SMUD-1).

Additionally, both PG&E and Joint Intervenors pointed out that despite the authority that CA ISO asserted it finds in Opinion 463-A to bill GMC charges for COTP/Bubble transactions, for which PG&E relayed information as the proxy SC, it has done no such billing in fact. (See Ex. PG&E-3, Att. 1 and Ex. SMUD-18). PG&E and Joint Intervenors argued that this undermined the credibility of CA ISO's overall position on the RPTOA and Opinion 463-A extending to MOO Charges. While CA ISO attempted to explain this "non-billing" of GMC away, the arbitrator did find it of some value (not determinative but supportive, again) in that it made the CA ISO's construct here, as to the RPTOA and Opinion 463-A, appear a bit "strained". If the GMC decisions were so clear from day one (eight years ago, when the GMC was approved) why haven't the GMC charges been applied? In effect, that was an open question when this case ended.

The failure to bill GMC was more compatible, as a conceptual matter, with the conclusions above that Opinion 463-A did not reach the application of charges to COTP/Bubble transactions and, therefore, the GMC case history does not support CA ISO's claim that it can impose MOO Charges on PG&E for the COTP or Bubble.

CA ISO's theory that the RPTOA, as interpreted by Opinion 463-A, should have dictated the result here also was conceptually "debunked" a bit, when one took into account the Scheduling Coordinator Agreement ("SC Agreement"). (Ex. PG&E -1, Ex. 2). The SC Agreement is a companion, intricately interrelated agreement with the RPTOA, in that the RPTOA implemented the obligations of PG&E under the SC Agreement for Existing Rightholders. And, in fact, the COTP I decision of FERC explicitly concluded that it found no authority under the SC Agreement to bill PG&E for

COTP/Bubble transactions scheduled by PG&E as the “unique scheduling coordinator.” (Ex. SMUD-17; April 18 Order at 6, fn. 8; see also JI IB at 7, fn 7).

Based on all of the above, one could not reasonably conclude that either the RPTOA or the principles in Opinion 463-A, as CA ISO urged, were readily transferable to the case at hand. The RPTOA and Opinion 463-A just do not provide the clear and convincing authority required to support the MOO Charges that CA ISO sought to impose here under the Tariff. Contrary to CA ISO’s claim at oral arguments: the RPTOA is not what makes PG&E the SC.

3. Other CA ISO Theories/Arguments

In addition to the two key arguments above, CA ISO made a number of other miscellaneous and diverse arguments to support its position. Because of their nature, several of these are disposed of in a more abbreviated form than the analysis above.

a. Collateral Attack and Seeking Exemption

CA ISO argued that PG&E’s claims here are “impermissible collateral attacks” on FERC orders in earlier cases. (CA ISO IB 11). The gravamen of this claim appeared to be that PG&E’s claims seek the “same relief” it sought in the GMC litigation, described above, namely: “an exemption from Must Offer Charges for Load served by off-grid schedules.”

To support this proposition, CA ISO laid out extensive legal authority on brief on the proper application of collateral estoppel and res judicata principles in contexts such as this. (CA ISO IB 11-15). For the reasons that follow, the arbitrator did not believe those extensively briefed principles have any application under the circumstances at hand.

First, this award has already explained at length why GMC, in effect, is not the same case as the one here. Second, CA ISO's underlying characterization of the issue here—that PG&E is seeking an “exemption” from MOO Charges-- was just plain wrong and baseless, from this arbitrator's perspective. In fact, the issue here, as noted on several occasions herein, had to be: is CA ISO authorized to make the MOO Charges? CA ISO, therefore, was incorrect when it maintained that “it is indisputable that the same arguments could have been raised and brought to FERC in the fall of 2001, when the Intervenors were seeking an exemption.” (CA ISO IB at 21). As laid out above, that was not the issue in 2001 and to characterize it as such is plain incorrect.

b. Reliability and Equities

In a number of places in its briefs, CA ISO seemed to be suggesting that a ruling should have been made in its favor here because the MOO Charges were introduced for reliability purposes during the California energy crisis. (See e.g. CA ISO RB at 3, noting: “The Arbitrator must first determine whether... to give COTP blanket immunity from charges that relate to reliability of the transmission system.”).

This argument was never fully fleshed out by CA ISO and no evidence was presented on it, but the plea appeared to be one of an equitable or a “sympathy” nature. It is hereby rejected as any basis for concluding CA ISO has the authority to bill MOO Charges for COTP/Bubble charges. First, this case had to be decided on the facts and the applicable law and not the equities, as pointed out at an earlier point. Second, the arbitrator in the COTP I case (addressed at length in Section V.C.2. below) specifically rejected a very similar reliability argument and FERC did not depart from that on review. (See Ex. SMUD-16 at 18-19; 20-21 and May 10 Order at 10). Third, no evidence was

offered by CA ISO to be a foundation of an equitable claim. Finally, as noted in Section IV.B. 1. above, there indeed may be a mechanism available to protect these reliability interests, but that was not an issue for this case.

C. Evaluation of PG&E and Joint Intervenors Arguments in Support of a Lack of Authority for MOO Charges as to COTP/Bubble Transactions

1. Introduction

PG&E and the Joint Intervenors made a lengthy series of arguments in order to establish that CA ISO does not and cannot have the legal authority to bill MOO Charges on COTP/Bubble transactions. As contrasted with the key arguments of CA ISO, which relied to a great degree on principles that need to be extrapolated as a matter of “logic” from previous FERC orders, PG&E and Joint Intervenors relied, in many instances, on the very language of the Tariff at issue and FERC authority addressing the matters at stake here. That was an important distinction and went a long way to explaining why, on balance, PG&E’s and Joint Intervenors’ position was clearer, more definitive and ultimately persuasive.

The key arguments of PG&E and Joint Intervenors seemed to fit best into three broad categories as addressed in Sections IV.C.2.,3., and 4., below: (1) the applicability of the COTP I decisions here; (2) supporting testimonial evidence adduced at hearings; and (3) PG&E as a unique proxy scheduling coordinator.

Coupled with the successful rebuttal of CA ISO’s arguments in the proceeding, as addressed in Section IV. B. above, these affirmative positions of PG&E and Joint Intervenors and a few other miscellaneous arguments (see Sections IV. C. 2-5, below), on balance, were ultimately persuasive and fully supported the conclusion here that the

billing of the MOO Charges as to COTP/Bubble transactions under the presented circumstances is unauthorized and improper.

2. COTP I Arbitration Award and FERC's Three Orders Affirming

PG&E and Joint Intervenors maintained from the very beginning of the case that the decision of the arbitrator and FERC's order upholding it in the COTP I case were controlling here. Specifically, PG&E urged that FERC's "two COTP I orders affirmed that the ISO has no authority to charge PG&E as the SC for the COTP or Bubble. In those orders [FERC] affirmed all of the findings of the Arbitrator in COTP I, including the explicit findings that (i) the ISO only has authority to bill in accordance with the Tariff and (ii) PG&E is not the SC for COTP or Bubble." (PG&E IB 17-18).

This award has already, in effect, addressed CA ISO's position that the COTP I precedent was not applicable here because the issue there and here were "totally different", concluding that this position was not persuasive under the facts and circumstances of this arbitration. CA ISO also may still disagree with the results in COTP I (and even be prepared to go to Federal Appeals Court for review when FERC finally disposes of a pending clarification request), but this arbitrator, in this context, had no choice but to apply the COTP I precedent where it is relevant. In part, the Tariff dictates that. (See DRP Section 13.3.11.1).

As noted earlier, the Tariff specifically requires that billing of the MOO Charges be to an SC and paid by an SC. Therefore, the issue of whether PG&E is an SC for COTP/Bubble transactions, which is the issue here, must be answered. And, this award concludes that in the COTP I litigation, FERC clearly established in its May 10 and April

18 orders that, indeed, PG&E is not an SC in that context. Therefore, that result must control here.

The rulings by the arbitrator and by FERC in COTP I and their application here could not be any clearer. As FERC specifically ruled in its second order on the matter:

In the May order we agreed with the arbitrator's finding that there is no basis to conclude that PG&E was an ISO Tariff defined Scheduling Coordinator for the COTP/Bubble transactions...The ISO has not convinced us we mis-interpreted our prior decision. (April 18 Order at 6, section 21, emphasis added).

This arbitrator was unable to find any limitations on these conclusions of FERC in COTP I, despite the fervent pleas of CA ISO. There is nothing in the multiple orders upon which CA ISO bases its theories to indicate FERC had any intention of permitting charges such as MOO, to apply to COTP/Bubble transactions, in contravention of the COTP I series of decisions. Critically, nothing in the COTP I orders indicates that FERC thought PG&E's status for COTP/Bubble transactions (not an SC) depended on the types of charges involved, which is a key underpinning of CA ISO's case, as discussed earlier.

While this award could have expended paragraphs detailing the basis of the COTP I arbitrator's decision (and FERC's resulting affirmance) and the specific rulings there on many of the arguments made in the instant case, that was both unnecessary and would have been repetitive. [An example of this would be the so-called Amendment 2 issue, pursued in both contexts (see Ex. SMUD-16 at p. 8)]. It is enough to say that the analysis in the COTP I arbitrator's award, and its FERC affirmation, was thorough and persuasive and applied here for the reasons posited throughout.

Interestingly, for what it is worth, SCE (which withdrew from this arbitration on March 29, 2005, from the CA ISO side of the case) participated in the COTP I case and seemed to indicate in a motion it filed there (which is an exhibit to the case at hand) that

COTP I indeed is dispositive of this case. (Exhibit No. CA ISO 12, hereafter “Ex.ISO-12”). While CA ISO attempted to explain this away (CA ISO RB at 28), the arbitrator found that explanation confusing and not consistent with the language on the face of SCE’s papers.

One of the essential reasons that the COTP I arbitrator, and FERC on review, concluded that PG&E is not a Tariff-certified SC to whom charges such as the ancillary or MOO Charges can be billed is that PG&E actually is a “proxy scheduling coordinator” (using the “proxy SC ID” as discussed in Sections IV.C.3. and 4, below) and not the Tariff defined SC for COTP and Bubble transactions. In the case at hand, it was unequivocally clear that PG&E relayed the information to ISO for the billing that underlay MOO Charges using this proxy SC ID. And, as was the case in COTP I, there is no language permitting MOO Charges when there is no SC and there is no basis, whatsoever, to assess charges on the proxy SC ID.

As noted earlier, CA ISO attempts to distinguish application of the apparently clear principles, reaffirmed by FERC on several occasions in COTP I, by arguing that there is a distinction between the kinds of charges involved in COTP I—ancillary services “off-grid” and those involving MOO—“on grid”, like GMC. Once again, such a distinction is not supportable under the facts presented in this case or in light of the GMC charge decision of FERC and the COTP I rulings of FERC. FERC neither drew such distinction or left room for the same in its multiple COTP I orders. And, this is particularly so where the first COTP I order came only four months after the GMC decision, as noted above.

3. Testimonial Evidence

If the FERC precedent discussed above had not been enough, standing by itself, then PG&E and Joint Intervenors also made an ultimately persuasive evidentiary presentation in the case to support the conclusion that PG&E is not an SC for billing MOO Charges on COTP and Bubble transactions.

Throughout the case (in its May 6, 2005 Motion to Strike, at hearing, and in post-hearings briefing), CA ISO vigorously objected to any reliance being placed in this award on that testimony and/or any weight being attached to it for purposes of the analysis and outcome of this matter. The essence of CA ISO's opposition on this point consistently was that the issues here involve purely legal matters and/or interpretations of FERC tariffs and decisions. Consequently, CA ISO maintained that it is only for this arbitrator--the ultimate decision maker—to make those interpretations and legal judgments. Moreover, CA ISO claimed that any testimony by non-lawyers on those questions must be rejected and have no weight attached to it. In addition, CA ISO attacked the use of excerpts from the COTP I record (as included as exhibits to testimony of PG&E's witnesses) on basically the same grounds, as well as irrelevancy.

This essential challenge of CA ISO to the witnesses and exhibits presented here by PG&E and Joint Intervenors was initially the subject of the May 19, 2005, Order on CA ISO's Motion to Strike, as well as its April 8, 2005 motion and the order concerning official notice. In rejecting the argument at that earlier point, this arbitrator drew conclusions that are still very applicable to the use of and reliance upon such expert testimony in this final award.

When all is said and done, the arbitrator is not convinced that he cannot and should not rely in any way, as CA ISO urges, on the testimony and exhibits of PG&E's and Joint Intervenors' witnesses because they involve impermissible legal opinion or testimony.

First, it was far from clear here that purely legal issues were involved. For example, there certainly appeared to be a factual (or at least mixed) issue of what is a Scheduling Coordinator under the MOO Charges Tariff provision.

Second, as stated in the May 19 order in this proceeding on the Motion to Strike testimony filed by CA ISO:

[T]he Arbitrator is not convinced that the testimony CA ISO wants stricken is purely legal opinion or testimony. At best, it is a "mixed bag" of technical and legal material, involving interpretations of a tariff, contracts, a previous arbitration award and FERC decisions. There is ample legal precedent at FERC and in the courts, as delineated by PG&E and SMUD in their pleadings, that "[t]he interpretations of tariffs and legal documents is not always a question of law" and that testimony such as that involved here "may be useful in interpreting the instruments which must be construed in this proceeding." Trans Alaska Pipeline System, 52 FERC 63,022 at 65,022 at 65,037 (1990). Order at 5).

It was somewhat helpful in reaching the ultimate decisions here to consider that testimony and materials concerning the interpretation of complex Tariff provisions and FERC decisions. Interpreting such tariffs and FERC decisions cannot be looked at as pure law—as many technical, operational and expert aspects are involved. And the witnesses presented by PG&E and Joint Intervenors (particularly Ms. Eschbach, Mr. Bray and Mr. Judson) clearly are "experts" in such matters, having negotiated and administered a number of the agreements involved and been responsible for implementing FERC orders with respect to them for years.

Surely, CA ISO cannot be maintaining that no weight whatsoever should be attached to such extrinsic and expert evidence concerning Tariff and FERC decision interpretations. After all, it is CA ISO who urged at numerous points on brief that one of the important tasks the arbitrator needs to undertake here is to divine the “intent” of FERC. For example, at page 6 of its Initial Brief, CA ISO urges that: “The effect of PG&E’s and Intervenors’ arguments, if accepted, would be simply to negate the Commission’s clear intent.”

Thus, if part of the job for the arbitrator here was to discern FERC’s intent in arguably vague technical language and orders interpreting it, how can there be something wrong with relying, to a limited degree, on experts, such as those presented by PG&E and Joint Intervenors here in order to divine FERC’s intent and meaning? After all, these are experts with years of experience in implementing and applying the Tariff to real world circumstances from a business, technical and operational perspective.

Moreover, it is interesting to note that the DRP provisions of the Tariff, which must be applied in this arbitration context, do not indicate that such evidence/testimony should be ignored. Section 13.3.8 specifies the type of evidence the arbitrator should reject in a Tariff dispute case: that which is “irrelevant, immaterial, unduly repetitious, or prejudicial or privileged.” And, the testimony here involves none of that. It might be technical and, even “quasi-legal” in places, but it was presented by experts intimately familiar with the Tariff and the circumstances. That made it well worth considering to assist this arbitrator.

In addition, it is worth noting also that, even if one accepted that only purely legal issue were involved here as CA ISO maintained, the Tariff itself does not require that

only lawyers can be arbitrators in cases such as this. DRP Section 13.3.1.1 only requires arbitrators who are “qualified”, with no restriction as to profession. Thus, consultants, engineers, or transmission experts, like the witnesses in this case, could serve as arbitrators and make all of the required decisions on the issues here. So, if CA ISO were correct that when solely legal issues are involved non-lawyers cannot be opining upon or deciding the issues, why doesn’t the Tariff make that concept clear, even in the qualifications of arbitrators.

The COTP I case also is helpful on this extrinsic evidence issue. There, the arbitrator found such extrinsic evidence (in fact some of it identical there and in this case) helpful in making his determinations, which also are important, in effect, to make in this arbitration. (SMUD-16). Critically, FERC explicitly upheld reliance on such extrinsic supporting evidence in its review of the COTP I arbitration award and, in effect, actually relied upon it, itself. As FERC noted: “Following the ISO Tariff, we also give substantial deference to the arbitrator’s factual findings that considered the extrinsic evidence relating to the meaning of the ISO Tariff provisions in dispute.” (May 10 Order at 9, emphasis added). That is compelling here.

A word is in order, however, on the weight this arbitrator attached in the end to that testimony. It was not conclusively used to arrive at the ultimate result here and the arbitrator has not even used it as the essential support of his ultimate legal conclusions. The arbitrator believes it was a somewhat valuable supplement to support the legal arguments of PG&E and Joint Intervenors. As noted in COTP I, the arbitrator did analyze similar testimony and found it persuasive. (Ex. SMUD-16 at 12-15). Ultimately, it serves the same purpose for this award.

Having addressed the limited use to which this arbitrator ultimately applied the testimony, it is still important to briefly summarize its thrust because it was persuasive as support of certain conclusions. And, the arbitrator indeed closely evaluated that evidence and weighed its credibility.

In essence, PG&E's witnesses established (and it was uncontested by testimony from CA ISO) that PG&E was never willing to be an SC for COTP/Bubble transactions by presenting evidence on how the proxy SC ID designation came into existence in the first place and what was intended all along. (See Ex. PGE-1 and Ex. PGE-2). These witnesses provided their independent recollections as to that, acknowledging there was no language in the Tariff or any other formal agreement embodying all of that, but that the extrinsic evidence corroborated the logical meanings of the Tariff, agreements and applicable FERC decisions.

The witnesses also provided, by way of attachment, key portions of the record from the COTP I case, (See Ex. PGE-1, Exhs 1A-T), to many of the same points. Indeed, that incorporated evidence from the COTP I arbitration was part of that upon which the arbitrator there relied in arriving at his conclusion that PG&E is not an SC for COTP/Bubble transactions, in general—the basic conclusion upheld by FERC explicitly on two occasions. (See Section IV.C. 2.). Indeed, on one of those occasions, FERC noted (clearly reviewing the COTP I record) that it “understood that PG&E was not willing to be a scheduling coordinator under the ISO Tariff for COTP and Bubble transactions. Therefore, we continue to uphold the arbitrator’s conclusion...” (April 18 Order at 6, emphasis added). Surely, if FERC could base a previous decision, in part, on such extrinsic evidence, this arbitrator should be able (if not required) to do the same here.

One more matter should be addressed on the extrinsic testimonial topic here. CA ISO elected not to present any witnesses of its own in rebuttal to those of PG&E and Joint Intervenors. While that was a calculated risk that CA ISO was free to take, particularly in light of its overall position here that only legal issues were involved and expert testimony was not permissible and unnecessary, that does not mean that the award was not permitted to place some limited weight on it in reaching its conclusions.

4. Unique Proxy Scheduling Coordinator—the Interim Agreement

PG&E and Joint Intervenors also presented a third key argument (at times, blended into its other two) that, rather than being an SC as defined in the Tariff, PG&E actually is a unique “intermediary” or “proxy scheduling coordinator”(using a “proxy SC ID) as to transactions on the COTP and Bubble for MOO Charges. This concept was introduced in the preceding section of this award, and formally embodied in the so-called Interim Agreement (“Interim”), (Ex. SMUD-28), which was entered into in 1998 by CA ISO, PG&E and SMUD. As Joint Intervenors explained on brief, that agreement establishes that “PG&E will act as the specialized ‘proxy scheduling coordinator’ for COTP and Bubble transactions... Thus, the Interim Agreement memorializes the parties’ understanding that PG&E is not the SC for COTP and Bubble transaction schedules, rather the ‘proxy scheduling coordinator for same, which have a special ‘COTP ID’ identification to distinguish them.” (SMUD IB at 3-4).

As noted in the preceding subsections, there was ample evidence on the record and precedent in the COTP I orders reflecting a similar concept that PG&E is not an SC as required in the MOO Charges section of the Tariff. As noted above, Ms. Eschbach explained the history of that on the record here.

Nevertheless, CA ISO seemed to argue that the fact that PG&E submitted COTP and Bubble information under the proxy SC ID in the format requested by the ISO (the format used by true SCs) that, somehow, converted it into an SC for purposes of MOO Charges as to COTP/Bubble transactions. Not only does such a theory fly in the face of the COTP I precedent and logic, there was no evidence presented to support the factual underpinning for that. In fact, CA ISO's sole witness, Mr. Fuller, specifically indicated, (Tr 863-864), he had no understanding of the effect of the proxy SC arrangement. As Joint Intervenors pointed out on brief, (JI IB at 11), "indeed Mr. Fuller's opinion that the mere fact of an entity submitting a schedule to the ISO made it a full-fledged SC was offered without knowledge and consideration by him of the details of the Interim Agreement". This award finds that persuasive and attaches some weight to it.

Thus, it seemed hard to find anything—either record evidence or definitive decisional authority as laid out in PG&E's or Joint Intervenors' three key arguments --to support a proposition that PG&E is, or can be, an SC under the MOO Charge Tariff provisions, as it must be for those charges to be authorized and permissible.

5. Other PG&E and Joint Intervenors Arguments on Authority

At a number of places, PG&E and Joint Intervenors argued that CA ISO's position should be rejected because it has had "multiple bites at the same apple"—to establish that charges can be visited upon PG&E for COTP/Bubble transactions. Examples of this included PG&E's and Joint Intervenors argument on the so-called Amendment 2 issue (See Section IV.C. 2. above).

While these "three... four, or five strikes and you are out" arguments are indeed interesting and colored some of this arbitrator's perception of certain CA ISO positions,

such arguments ultimately did not prove dispositive in any way. The arbitrator viewed such arguments just as he viewed CA ISO's collateral estoppel argument (See Section IV. B. 3. a., herein) and all of the parties' claims of position inconsistency (see Section IV.A., herein). Ultimately, such arguments are not at the heart of the matter and determination. Thus, precious little space or time needed to be consumed on them here, but it should be noted that it did seem that many of the claims/arguments here have been raised before and disposed of on multiple occasions.

4. If CA ISO is Right, the Result is "Absurd"

A final argument that Joint Intervenors, particularly, made against CA ISO's fundamental position did have some surface appeal and deserved mention. Joint Intervenors maintained that if CA ISO is correct that it can bill MOO Charges, but not Ancillary Services (per the COTP I decisions), on COTP/Bubble transactions, then there would be an "absurd" outcome because the result would be that for the same transactions over COTP, PG&E is SC for some charges but not for others. (JI RB at 2, 9; Orals Tr. at 1029). Joint Intervenors noted that such an outcome would be unprecedented and "completely novel (if not foreign) to the California ISO marketplace and the ISO Tariff provisions and practice." (JI RB at 9).

Such a disparate and inconsistent result for different charges on COTP transactions would not be inherently improper or determinative of the overall result in this arbitration. However, it is at best curious (even if not "absurd), somewhat persuasive and indeed well may place CA ISO's overall theories on somewhat "shaky ground".

CA ISO did not make a meaningful attempt to rebut the charge-application inconsistency would be "unheard of in the California markets and unprecedented", as

Joint Intervenors claimed. That failure reinforced that there might be something to the argument. Critically, FERC has not indicated to date anywhere, contrary to what would result from CA ISO's positions here, that the agency wants to create such a precedent of inconsistency of types of charges under the Tariff. Surely, then, it could not have been the place of this award to do that.

D. The SMUD Post-June 2002 Issue

After June 18, 2002, SMUD became its own control area and PG&E ceased being an SC for SMUD, as indicated in the FERC order and the underlying ISO filing accepting changes to the RPTOA to reflect that [Exhibit No. CA ISO 26, hereafter "Ex. ISO-26" (Order, 101 FERC 61,065) and Ex. SMUD-6]. It should be noted that, by logical definition because of the relative size of SMUD and its transactions, that the MOO charges to PG&E as SC for SMUD after June 18, 2002, make up the bulk of the \$14.4 million disputed charges to PG&E between 2001 and the end of 2004. (see JI IB at 12, fn. 16).

Based on the analysis elsewhere in this award that CA ISO has never been authorized to bill PG&E as an SC on COTP/Bubble transactions, it probably would have been unnecessary to reach this issue of SMUD's being SC for SMUD after June 18, 2002. At oral arguments, there seemed to be general concurrence on that. (Orals Tr. at 1009). And, in framing this SMUD issue in its reply brief, [see CA ISO RB at 1 (item 2)], CA ISO seemed to explicitly concede the same point by its use of the "if" concept. Thus, this award concurs that there appears to be no need to reach the issue.

Nevertheless, CA ISO pursued a number of "alternative theories" as to why it was proper to bill PG&E for SMUD transactions after the June 2002 date. That engendered a

great deal of argument and debate here between SMUD and CA ISO, while PG&E largely “stood aside” on that. Because this issue appeared moot in light of the other conclusions of law and fact herein, this award only touches upon those alternative theories of CA ISO on this point, in case it would be helpful to FERC in the event of an appeal.

First and probably most importantly, CA ISO did not provide any real credible authority for the proposition that PG&E serves as an SC for SMUD, at all, after June 18, 2002. CA ISO’s sole witness at hearing, Mr. Fuller, was unable (or unwilling) to marshal any evidence (or knowledge for that matter) to support the authority for such billing, (see JI IB at 10-11), and such persuasive support did not appear elsewhere in CA ISO’s case.

Second, it would appear that FERC’s order and the CA ISO filing at the agency accepting changes to the RPTOA to reflect the change of SMUD’s control area status and the termination of PG&E as an SC for SMUD (with regard to Existing Contracts) clearly establishes that there was no authority for CA ISO to assess PG&E MOO Charges associated with SMUD transactions after June 18, 2002. (Ex. ISO-26 and Ex. SMUD-6). PG&E’s role as SC for SMUD under the RPTOA, if it ever existed, ended on June 18, 2002. That is how the RPTOA operates, as discussed in earlier sections of this award.

CA ISO’s other arguments on this subject of the treatment of SMUD after June 18, 2002, are not persuasive, either. Both the “exports” and “wheeling through” issues are convoluted at best and were not supported adequately in the record.

Finally, as to this issue, the arbitrator’s view of CA ISO’s rationale and arguments for its position, including the exports and wheeling through points, was shaped by one of the “inconsistent position” arguments that did deserve mention. SMUD attached to its

reply brief, and explained at oral arguments, a copy of a data request response filed by CA ISO early in this arbitration. (JI RB, Att. E). In there, CA ISO apparently unequivocally stated, through counsel, “PG&E ceased to be the Scheduling Coordinator for SMUD on June 18, 2002.” While that discovery submission was not made part of the record here and CA ISO attempted to explain it away in a number of ways, the arbitrator does believe it has some value here. It could not, and would not, be used to establish the fact that CA ISO conceded the ultimate point. But, its existence did call into question many of the creative arguments fashioned by CA ISO on this SMUD post- June 2002 matter. It did not dictate the outcome that is laid out earlier, but it did undermine the arguments forwarded by CA ISO on the issue.

There was one last point to address on the SMUD post-June 2002 issue. CA ISO made a somewhat unclear argument at pages 48-49 of its reply brief that if this award concluded that PG&E is not the SC for SMUD after 2002, then somehow this award needed to “make clear” that this “does not relieve PG&E of its responsibility to ... ensure” an alternative party agrees to the obligations. PG&E expressed some well-placed confusion on this “guarantor” concept. (PG&E RB at 19-20). This award has not adopted the CA ISO “guarantor” suggestion/position. It was unclear and totally unsupported in the record. It also appears to have been presented too late in the case, if the arbitrator fully understands its thrust.

V. Allocation of Costs

On brief, PG&E urged that this arbitration award, in accord with ISO Tariff Section 13.3.14, “order the ISO to bear 100% of all costs associated with this Arbitration.” (PGE IB at 22, emphasis added). Joint Intervenors “deferred” to PG&E’s

position and brief on this issue. (JI IB at 20). To the contrary, CA ISO maintained on brief that costs should be shared pro rata under the allocation language in the Tariff, as has been the case throughout the pendency of the arbitration. (CA ISO IB at 49).

A quantification of “all costs associated with the Arbitration” was not to be found in the record here, but it would not be unreasonable to assume that if this additional remedy were to be ordered, as PG&E requested, a total amount in the multiple hundreds of thousands of dollars would be potentially involved, taking into account AAA fees, arbitrator charges/expenses, as well as the overall litigation costs of the multiple parties in this complex and lengthy matter.

The legal standard for awarding costs is clear under the Tariff and by its explicit language places complete discretion in the arbitrator on this subject. “If the arbitrator determines that a demand for arbitration or response to a demand for arbitration was made in bad faith, the arbitrator shall have discretion to award the costs of the time, expenses, and other charges of the arbitrator to the prevailing party.” (IBR 1 at 280, emphasis added). It must be noted initially that this Tariff language only allows allocation of arbitrator costs, and not “all costs associated with this Arbitration” as requested by PG&E.

The Tariff provides neither a definition of “bad faith”, nor a criterion for interpreting those words. Also, as counsel for all parties acknowledged at the final oral arguments, there is no legal precedent on this Tariff language and its interpretation. (Orals Tr. at 949 and 1068). Therefore, this allocation issue appeared to be a question of first impression.

PG&E maintained that CA ISO demonstrated the required bad faith because, among other things, it “never had any legal basis to impose the charges on PG&E.” (PGE IB at 22, emphasis added). CA ISO, on the other hand, did not believe “any of the parties acted in bad faith” and was not seeking a 100% allocation, despite the fact that “costs of this arbitration have been needlessly escalated by shifting legal positions and by the filing of legal opinion testimony... .” (CA ISO IB at 49).

On this issue, the arbitrator rules in favor of the CA ISO and orders that the unquestionably significant costs be allocated pro rata, as AAA has been doing throughout the proceedings. Simply put, the arbitrator has concluded that CA ISO did not exhibit any bad faith which would be required to have hundreds of thousands of dollars in costs imposed on it, as urged by PG&E.

As detailed in the discussions in the preceding sections of this award, CA ISO’s arguments in the arbitration were not frivolous, at all. This lengthy award amply established that the questions presented were not clear cut. After all, very competent and experienced counsel in matters such as this handled the litigation for these sophisticated parties. The arbitrator did not observe anything but “good faith” and honorable actions by CA ISO or its counsel throughout the course of the proceedings. That applied to counsel of all parties, as well.

The fact that the summary dismissal stage, involving complex issues and interpretations of FERC legal precedent, took months to unfold (including a lengthy in-person oral argument at the end) and resulted in a 19-page order by the arbitrator, and the fact that the parties, after four days of evidentiary hearings, took 175 pages to fully argue

and brief the key legal issues here was proof, indeed, that there were very viable and legitimate arguments on each side.

While, at times, this arbitration may have presented arguably unusual and unnecessary controversy and contention on all sides, as well as intricately constructed arguments, that never rose to a level of bad faith actions by any party or counsel.

Thus, this award concludes that, by logical definition, the pursuit of viable legal arguments, as here, and the existence of the close questions on complex issues, are inconsistent with the required exhibition of bad faith. Since the arbitrator cannot reach a conclusion that bad faith was exhibited, PG&E's allocation request is rejected and CA ISO's position on pro rata allocation of costs is approved.

VI. Conclusion and Final Orders

Based on all of the determinations above, CA ISO is hereby ordered to adjust billings to PG&E to reflect a full refund of all MOO Charges for transactions on the COTP and the Bubble through the close of the record (\$14,319,378.14), as well as any and all additional and/or associated amounts reflected in PG&E settlement statements, at any time after the close of the evidentiary record. CA ISO shall make all final, required adjustments to the bills of PG&E fully within 30 days of this award, unless stayed by any proper action pursuant to the Tariff, or agreement of the parties. Since neither PG&E nor the Joint Intervenors requested that any interest attach to the ordered refunds and the Tariff does not provide for that, none is ordered.

In addition, and in accordance with the conclusion on the allocation of costs request of PG&E in the preceding section of this award, the costs associated with the arbitration are to be shared pro rata. This is as specified in DRP Section 13.3.14 of the

CA ISO Tariff and as provided in the November 4, 2004 Order on Initial Allocation of Costs-Case Order No.2-Supplement in this proceeding. Accordingly, the final pro rata sharing and/or accounting for such costs shall be implemented by AAA as necessary and be consistent with the AAA's allocation and billing in place in this arbitration since the last of the five departing parties (TID) formally withdrew on April 22, 2005, leaving PG&E, CA ISO, SMUD, TANC, MID and Redding remaining to be allocated pro rata shares.

In conjunction with this conclusion and final order, an additional issue raised in the case must be addressed. On brief, CA ISO urged that in the event the arbitrator "issues an Award granting relief to PG&E, the CA ISO believes that it would be advisable for the Arbitrator to retain jurisdiction until the filing of an appeal of the Award with the Commission [FERC] or 60 days after the issuance of the first Preliminary Settlement Statements reflecting the Award, whichever comes first." (CA ISO IB at 49). This suggestion apparently was designed to deal with any questions that might arise with respect to the finalization of the charges and refunds involved. PG&E opposed this proposal, at oral arguments, largely on the grounds that such a step is unnecessary. (Oral Tr. 945-949). Joint Intervenors opposed the proposal, as well. (Orals Tr. 1022-1023).

Despite some surface appeal to potentially retaining jurisdiction to "help the parties out" and/or for the efficient administration of justice, the arbitrator declines to do so. First, CA ISO very well may have fully abandoned the request at oral argument. (Orals Tr. 1076). Second, the arbitrator is not convinced that he has the authority under the Tariff to do it. DRP Sections 13.3.10 and 13.3.11 appear to contemplate a single, and truly final, award or decision and there is no language in the Tariff suggesting continuing

jurisdiction or issuance of any subsequent order, along the lines envisioned by CA ISO. Third, it does not appear that such continuing jurisdiction is necessary in this case. It is hoped that the parties can amicably work out what appear to be relatively uncomplicated calculation matters or, if not, FERC is the likely place the matter ultimately will be resolved.

Thus, CA ISO's continuing jurisdiction request on brief is not adopted. This award and decision are indeed final, for purposes of the DRP. This arbitrator's jurisdiction and duties are at an end under the Tariff, at this time.

By way of further final orders, CA ISO also is reminded of an additional obligation in DRP with respect to this award. Section 13.3.11.2 requires that "a summary of the disputed matter and the arbitrator's decision shall be published in an ISO newsletter or electronic bulletin board and any other method adopted by the ISO ADR Committee." In addition, any or all parties filing a notice of appeal of this award with FERC are reminded of the obligation under DRP Section 13.4.3.1 that a copy of such notice(s) shall be provided to the arbitrator, in addition to all other recipients. The dual Tariff obligations noted in this paragraph shall be implemented as to this award.

Respectfully Submitted and So Ordered,

s/Robert P. Wax

Robert P. Wax, Esq.
Arbitrator

West Hartford, CT.
September 30, 2005