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UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners:

California Independent System Operator Corporation

Docket No. EL02-45-000

ORDER DENYING PETITION FOR REVIEW

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1. This order denies the California Independent System Operator Corporation's (ISO) petition for review of an arbitrator's award that granted Pacific Gas & Electric Company's (PG&E) claim for reimbursement of \$14,172,337.08, the amount PG&E paid to the ISO for ancillary services during the period between April 1998 and April 1999.
2. This order benefits customers because it clarifies the ISO's duties and obligations under its Open Access Transmission Tariff (ISO Tariff), and reaffirms the Commission's policy of relying on alternative dispute resolution (ADR) procedures to more efficiently use limited time and resources.

BACKGROUND

3. PG&E initiated arbitration against the ISO pursuant to section 13.2.2 of the ISO Tariff claiming, among other things, that it improperly paid the ISO more than \$14 million in ancillary service charges during the period between April 1998 and April 1999. Specifically, PG&E argued that the ISO improperly procured ancillary services in connection with transactions scheduled on the California-Oregon Transmission Project (COTP) and on transmission facilities owned and operated by Sacramento Municipal Utility District (SMUD) and the Western Area Power Administration (WAPA) (collectively, the Bubble). PG&E asserted that these facilities were off-grid facilities that, while geographically located in the ISO control area, were not turned over to the ISO's operational control. PG&E maintained that since these facilities were not turned over to the ISO's control, they were not part of the ISO- controlled grid and not subject to the ISO Tariff, and thus the ISO was not entitled to assess ancillary service charges for transmission over them. In response, the ISO denied that PG&E was entitled to reimbursement of ancillary service costs, and also sought recovery from PG&E for additional ancillary service costs since May 1, 1999, including interest.

4. On December 13, 2001, the arbitrator issued a final order and award that granted PG&E's claim. The arbitrator framed the issue as whether the ISO had the requisite legal authority to impose upon PG&E charges for ancillary services in connection with transactions scheduled on the COTP and Bubble facilities. The arbitrator concluded that the ISO Tariff did not provide the ISO with authority to impose charges related to these transactions.
5. Specifically, the arbitrator found that the ISO Tariff provided the ISO authority to procure ancillary services only for the ISO-controlled grid, and the ISO-controlled grid did not include the COTP and Bubble facilities. The arbitrator also found that there was no language within the four corners of the ISO Tariff that authorized the ISO on the basis of its control area responsibilities to impose charges on scheduling coordinators for transactions that were within the control area but did not use the ISO-controlled grid.
6. The arbitrator concluded that the ISO Tariff language was strongly reinforced by the history of Amendment No. 2. The arbitrator stated that, if the ISO Tariff changes proposed by the ISO in its filing of Amendment No. 2 had been approved by the Commission, it would have resolved the issues which arose in this arbitration and there would have been no dispute. However, the arbitrator found that the Commission rejected the ISO's amendment in California Independent System Operator Corporation, 82 FERC ¶ 61,312 (1998) (March Order).
7. The arbitrator also considered other extrinsic evidence concerning the intent of the tariff provisions (e.g., discussions between the parties relating to scheduling COTP and Bubble transactions, as well as associated settlements and billing) and found that this evidence supported PG&E's position, rather than the ISO's claim. The arbitrator noted that the evidence showed that PG&E had agreements in place with, e.g., SMUD, that included ancillary service self-provision arrangements concerning COTP and Bubble transactions. Regarding the ISO's contention that PG&E was the scheduling coordinator for COTP and Bubble transactions and thus subject to the obligation to pay for ancillary services procured by the ISO, the arbitrator reviewed the extrinsic evidence and concluded that PG&E was the scheduling coordinator under the ISO Tariff for transactions on the ISO-controlled grid, but was not with respect to COTP and Bubble transactions.
8. Furthermore, the arbitrator considered the ISO's alternative basis for the legal authority that there was an exception to the filed rate doctrine, i.e., that utilities are entitled to recover the actual costs they incur when they have failed to file the necessary rate information, and found no support for the proposition.

9. The arbitrator also rejected the ISO's assertion that PG&E was time-barred from contesting the validity of the charges. The arbitrator found, as a factual matter, that PG&E did not discover the billing treatment being given the disputed charges until April 1999, and taking into account further findings the arbitrator found no basis on which to conclude that PG&E was deficient in not discovering these facts earlier and that PG&E's invocation of the dispute procedures was timely. The arbitrator concluded that it was neither fair and equitable, nor consistent with controlling legal standards as to the ISO's Tariff authority, to find that PG&E should bear the cost of the ISO's exercises of judgment regarding how the ISO should meet its responsibilities as a control area operator. Finally, the arbitrator denied the ISO's counterclaim, concluding that the ISO did not have the legal authority to impose ancillary services charges for COTP and Bubble transactions.

PETITION

10. On January 4, 2002, the ISO filed a petition with the Commission to initiate a proceeding for review of the arbitrator's final order and award, and asserts that the arbitrator improperly granted PG&E's claim. The ISO states that it is entitled to Commission review of the award under section 13.4 of the ISO Tariff, and also petitions the Commission to establish a procedural schedule for such review. The ISO states that its petition presents fundamental issues concerning the ability of a control area operator to fulfill its responsibility to maintain the reliability of the electric system within its control area, but fulfills its ancillary services obligations with regard to loads served by facilities that are not under its operational control but are owned by municipal utilities. The ISO explains that, although the COTP and the Bubble facilities are not part of the ISO-controlled grid, they are part of the Western Systems Coordinating Council (WSCC) control area for which the ISO is the control area operator.

11. First, the ISO argues that the arbitrator erred in concluding that the references in the ISO Tariff to the ISO-controlled grid, rather than to the control area, limit the ISO's ability to recover from PG&E the costs of ancillary services procured in connection with schedules on facilities that are within the control area but not part of the ISO-controlled grid. Second, the ISO claims that the arbitrator erred in concluding the Commission's rejection of Amendment No. 2 to the ISO Tariff barred the ISO from recovering from PG&E the costs of procurement of ancillary services in connection with the COTP and Bubble transactions. Third, the ISO asserts that the arbitrator's conclusion that PG&E is not the scheduling coordinator for COTP and Bubble transactions under the terms of the ISO Tariff is not supported by the language of the ISO Tariff or by substantial evidence. Fourth, the ISO claims that the arbitrator's conclusion that the ISO did not properly take into account the self-provision of ancillary services in procuring ancillary services for

COTP and the Bubble transactions is erroneous. Fifth, the ISO claims that the arbitrator misinterpreted Commission and judicial precedent that would allow the ISO to recover its variable costs of procuring ancillary services for the COTP and the Bubble transactions even if the ISO Tariff did not authorize charges for those services. Sixth, the ISO contends that the arbitrator's conclusion that PG&E's claim for the period from April 1998 to April 1999 is not time-barred under the ISO Tariff is not supported by substantial evidence.

12. On January 25, 2002, the Commission issued an order establishing a schedule for submission of pleadings in Docket No. EL02-45-000. See California Independent System Operator Corporation, 98 FERC ¶ 61,047 (2002). The Commission stated that: (1) persons seeking to intervene could file interventions within 30 days of the date of the order; (2) 30 days from the date of the issuance of the order, the ISO and intervenors supporting the ISO could file initial briefs addressing the award and the ISO's appeal of the award; (3) 30 days from the date of the initial briefs, PG&E as well as intervenors supporting PG&E could submit reply briefs addressing the award and the ISO's appeal of the award; (4) 20 days thereafter, the ISO as well as intervenors supporting the ISO could file rebuttal briefs.

INTERVENTIONS AND BRIEFS

Interventions

13. On January 17, 2002, the Cogeneration Association of California and the Energy Producers and Users Coalition (Cogeneration Association) filed a motion to intervene. On January 23, 2002, PG&E filed a motion to intervene and protest. On January 24, 2002, Southern California Edison Company (SoCal Edison) filed a motion to intervene.

14. On January 25, 2002, the ISO submitted the evidentiary record of the arbitration proceeding in Docket No. EL02-45-000. On January 30, 2002, the California Electricity Oversight Board (California Board) filed a motion to intervene. On February 4, 2002, SMUD filed a motion to intervene. On February 6, 2002, the California Public Utilities Commission (California Commission) filed a notice of intervention. On February 14, 2002, the Northern California Power Agency (NCPA) filed a motion to intervene. On February 15, 2002, Turlock Irrigation District (Turlock) filed a motion to intervene. On February 25, 2002, San Diego Gas & Electric Company (SDG&E) filed a motion to intervene and to compel publishing the award decision in compliance with the ISO Tariff. On February 25, 2002, the California Department of Water Resources (California Resources) and the Arizona Public Service Company (Arizona Company) filed motions to intervene, and on February 25, 2002, the Transmission Agency of Northern California

(TANC), M-S-R Public Power Agency (M-S-R Power), Modesto Irrigation District (Modesto), and the California Cities of Santa Clara and Redding (Cities) filed motions to intervene.

Initial Briefs

15. On February 25, 2002, the ISO filed an initial brief arguing that section 2.5.1 of the ISO Tariff unambiguously directs the ISO to ensure adequate ancillary services not simply for the ISO-controlled grid but to maintain the reliability of the ISO-controlled grid and authorizes recovery of the associated costs from scheduling coordinators. In addition, the ISO adds that the ISO Tariff when read as a whole authorizes and requires the ISO to procure ancillary services for transactions within the control area and to recover such ancillary services costs from the scheduling coordinators whose schedules necessitate the procurement, if such transactions have the potential to affect the reliability of the ISO-controlled grid.

16. Furthermore, the ISO contends that Commission's policy that revenue responsibility should follow cost-causation compels the conclusion that those entities who are beneficiaries of the ISO's procurement of ancillary services should bear the costs of those ancillary services. The ISO also argues that under existing agreements PG&E is the scheduling coordinator, and under the ISO Tariff PG&E is responsible for the cost of the ancillary services procured by the ISO in connection with schedules on the COTP. Moreover, the ISO disputes the arbitrator's conclusion that the March Order supports PG&E's claim. The ISO maintains that the evidence does not suggest that the ISO was concerned with its ability to charge scheduling coordinators for costs incurred in connection with the COTP schedules, but was concerned with its ability to collect the grid management charge and ancillary services costs in connection with load that was not scheduled and where there was no scheduling coordinator.

17. On February 25, 2002, SoCal Edison filed an initial brief stating that it does not fully support any of the parties to the ADR proceeding, but argues that it should not bear the responsibility for paying for the ancillary services that the ISO procured for COTP and the Bubble transactions.

Reply Briefs

18. On March 27, 2002, SDG&E filed a reply brief stating that it supports the arbitrator's award. SDG&E states that the Commission should uphold the award because the arbitrator correctly found, based on the ISO Tariff and the March Order, that the ISO charges at issue are improper. SDG&E adds that this is a case of first impression

involving procedures for an appeal to the Commission provided in the ADR provisions of the ISO Tariff, and SDG&E notes that it has filed its own claim and demand for arbitration against the ISO under the ISO Tariff.

19. On March 27, 2002, TANC, Modesto, M-S-R Power, Cities, SMUD, the NCPA, and Turlock (collectively, Intervenor) filed a reply brief supporting PG&E, and requests that the Commission affirm the arbitration award. Intervenor argue that the Commission should give substantial deference to the findings and conclusions of the arbitrator, which were based on the factual assessment of the record evidence, and even if the Commission uses a de novo review, the arbitrator's award is legally sound. Intervenor assert that the arbitrator's award neither contravenes the public interest nor is in any other way inconsistent with statutory requirements.

20. They claim that the arbitrator correctly found that: (1) there was nothing in the ISO Tariff which authorizes the ISO to impose charges for transactions that are within the control area but do not use the ISO-controlled grid, notwithstanding the ISO's responsibility for reliability; (2) there was no extrinsic evidence which would allow the ISO Tariff to be read to encompass the costs at issue, including the history of Amendment No. 2 which would have expanded ISO control over non-jurisdictional facilities at issue here; (3) since PG&E is not the scheduling coordinator for COTP and Bubble transactions, the ISO has no authority to assess ancillary charges on those transactions; (4) the ISO's contractual obligations buttress the conclusion that the ISO's reliability arguments do not justify its claim of authority to assess the disputed charges; and (5) the arbitrator's analysis of these contracts conclusively establishes that the Intervenor had the right to self-provide ancillary services to support COTP and Bubble transactions consistent with WSCC criteria. Intervenor add that the ISO should be barred from raising the reliability issue now, because it was not raised before the arbitrator.

21. Intervenor maintain that, absent a tariff filing, the cost causation principles and exceptions to the filed rate doctrine cited by the ISO fail to support the ISO's authority to recover the cost of ancillary services. They assert that the Commission's ADR policy favors affirming the arbitrator's award. Finally, Intervenor state that SoCal Edison's brief exceeds the appropriate scope of review since it focuses on who, if not PG&E, should pay for the ancillary services.

22. On March 27, 2002, PG&E filed a reply brief arguing that the ISO's appeal is another attempt by the ISO to attempt to disregard the provisions of the ISO Tariff by imposing charges on PG&E for costs incurred in connection with transactions that did not occur on the ISO-controlled grid. PG&E argues that the Commission must afford

substantial deference to the factual findings of the arbitrator, including the finding that the PG&E never agreed to schedule COTP transactions as an ISO Tariff certified scheduling coordinator nor did PG&E ever agree to pay for any charges, including the ancillary services charges, related to those transactions. PG&E claims that section 2.5.1 of the ISO Tariff plainly does not permit the ISO to procure, and then assess charges for, ancillary services on off-grid transactions. Moreover, PG&E argues that the Commission's denial of Amendment No. 2 in the March Order made the restriction inherent in the already plain language of the ISO Tariff absolutely unambiguous, and that in the March Order the Commission clearly denied the ISO's attempt to expand the ISO's authority to include off-grid facilities.

23. On March 27, 2002, SMUD filed a supplemental reply brief in support of PG&E. SMUD agrees with the arbitrator's determination that the ISO lacks the authority to charge for ancillary services in connection with COTP and Bubble transactions. SMUD states that the Commission has ordered the ISO to honor existing transmission agreements, including various interconnection agreements that predate the ISO. In this regard, SMUD argues that, under an Interim Agreement with PG&E, SMUD has the right to self-provide ancillary services to support COTP and Bubble transactions, consistent with the operating standards and requirements of WSCC and North American Electric Reliability Council (NERC).

Rebuttal Briefs

24. On April 16, 2002, the ISO filed a rebuttal brief arguing that nothing in the briefs of PG&E, Intervenors, or SMUD contradicts the ISO's authority and obligation under the unambiguous terms of section 2.5.1 of the ISO Tariff to procure the ancillary services that are the subject of this proceeding in order to protect the reliability of the ISO controlled grid in accordance with applicable standards. Thus, the ISO asserts that the Commission should reverse the arbitrator's award.

DISCUSSION

Procedural Matters

25. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2003), the notice of intervention of the California Commission and the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

The Arbitration Award

26. The Commission has long recognized the value of parties seeking to resolve disputes through means other than formal litigation before the Commission, and thus has stated that 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 given that arbitration is a valuable way to avoid time-consuming and expensive administrative proceedings.¹ The ISO Tariff thus provides for arbitration and, specifically, Section 13 of the ISO Tariff provides the basis of an appeal of an arbitration award. Section 13.4.1 states that: "A party may apply to the FERC . . . to hear an appeal of an arbitration award only upon the grounds that the award is contrary to or beyond the scope of the relevant ISO documents, United States federal law, including, without limitation, the FPA, and any FERC regulations and decisions, or state law." In addition, Section 13.4.2 of the ISO Tariff states that: "The parties intend that FERC should afford substantial deference to the factual findings of the arbitrator."

27. We will uphold the arbitration award and deny the ISO's petition for review, as discussed below.

28. We agree with the arbitrator's analysis as discussed below. Section 2.3.1.1.1 of the ISO Tariff states that "The ISO shall establish a WSCC approved Control Area and control center to direct the operation of all facilities forming part of the ISO Controlled Grid, Reliability Must-Run Units and Generating Units providing Ancillary Services." Section 2.5.1 of the ISO Tariff states that "The ISO shall be responsible for ensuring that there are sufficient Ancillary Services available to maintain the reliability of the ISO Controlled Grid consistent with WSCC and NERC criteria." We find that the arbitrator properly concluded that ISO Tariff section 2.3.1.1.1 directs the ISO to establish a control area and control center to direct the operation of all facilities forming part of the ISO-controlled grid, and ISO Tariff section 2.5.1 authorizes the ISO to ensure the adequacy of ancillary services for the ISO-controlled grid and ancillary services, in turn, are defined to mean certain services needed to maintain the reliable operation of the ISO-controlled grid. The ISO Tariff states that the ISO is responsible for procuring ancillary services only for the ISO-controlled grid, and thus it may seek reimbursement of the costs of ancillary services from customers that use the ISO-controlled grid. The ISO Tariff does

¹E.g., Policy Statement Regarding Regional Transmission Groups, FERC Stats. & Regs. ¶ 30,976 at 30,877 (1993). See also *Cities of Anaheim, et al.*, 107 FERC ¶ 61,---- at P 33 (2004); *California Power Exchange Corporation*, 88 FERC ¶ 61,112 at 61,266 (1999).

not provide, as the ISO argues, that the ISO can apply those provisions beyond to off-grid transactions within the ISO control area.

29. Therefore, we agree with the arbitrator that the ISO Tariff limits the ISO's authority to procure ancillary services to ISO-controlled grid transactions, and that the arbitrator correctly concluded that the ISO Tariff does not authorize the ISO to impose upon PG&E charges for ancillary services in connection with COTP and Bubble transactions since they are not included within the ISO-controlled grid.

30. In fact, in the March Order, we effectively rejected the ISO's request to extend its authority to procure ancillary services to non-ISO-controlled grid transactions when we rejected the ISO's Amendment No. 2.² In this regard, we note that the arbitrator found that the Commission's decision in the March Order supported denying the ISO's claim; in the March Order the Commission, among other things, rejected the ISO's Amendment No. 2 which proposed to revise the ISO Tariff to create a new definition for the ISO control area distinct from the ISO-controlled grid. The ISO stated that adding this term would clarify that the ISO Tariff would apply to entities, such as municipal utilities, that own transmission facilities within the ISO control area but have not yet indicated an intention to join the ISO. In response, we found that the proposed changes were unjust and unreasonable because they would broadly expand ISO control over non-jurisdictional facilities which were not being transferred to the ISO's control, and also inconsistent with our prior orders and would impose additional obligations on participating transmission owners. We will not relitigate the merits of the March Order, which the ISO is essentially now attempting to do in its petition.

31. 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, and the arbitrator's finding that PG&E had agreements in place that included ancillary service self-provision arrangements for COTP and Bubble transactions, as well as the arbitrator's finding that PG&E was not a scheduling coordinator for COTP and Bubble transactions. We also uphold the arbitrator's factual finding that rejected the ISO's assertion that PG&E was time-barred from contesting the validity of the charges. The arbitrator found, as a factual matter, that PG&E did not discover the billing treatment being given the disputed charges until April 1999, and taking into account further findings the arbitrator found no basis on which to conclude

² March Order, 82 FERC at 62,238, 62,241.

that PG&E was deficient in not discovering these facts earlier and that PG&E's invocation of the dispute procedures was timely.

32. Regarding the ISO's argument that it procured ancillary services to maintain the reliability of the ISO-controlled grid, we agree with Intervenors that we need not address this argument because it was not timely raised. Indeed, we note that the ISO could have, but did not, present to the arbitrator specific evidence showing that it procured ancillary services to maintain the reliability of the ISO-controlled grid.³ We also agree with Intervenors that SoCal Edison's concerns regarding cost responsibility are beyond the scope of this proceeding.

33. Finally, we agree with the arbitrator and dismiss the ISO's cost causation argument as an exception to the filed rate doctrine since these principles are not relevant in the factual context presented here. The ISO simply has not shown that it has a right under a tariff or on equitable grounds to assess or recover the charges it seeks here.

The Commission orders:

The ISO's petition for review is hereby denied.

By the Commission.

Secretary

³In this regard, we note that section 13.4.2 of the ISO Tariff provides that "[n]o party shall seek to expand the record before the FERC . . . beyond that assembled by the arbitrator" except in two limited respects not present here. We consider the ISO's reliability-related argument to be inconsistent with this provision.

AMERICAN ARBITRATION ASSOCIATION

PACIFIC GAS AND ELECTRIC COMPANY,

Claimant,

vs.

CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CORPORATION,

Respondent.

Case No. 71 198 00711 00

CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CORPORATION,

Counter-Claimant,

vs.

PACIFIC GAS AND ELECTRIC COMPANY,

Counter-Respondent.

FINAL ORDER AND AWARD

I. INTRODUCTION

A. Procedural History

This Arbitration has been initiated by Pacific Gas & Electric Company ("PG&E") pursuant to the Dispute Resolution provisions of Article 13 of the FERC Electric Tariff filed by California Independent System Operator Corporation ("Cal ISO" or "ISO"). PG&E filed a Statement of Claim ("PG&E Claim") against Cal ISO under §13.2.2 of the Tariff in October 2000. Statements of Claim and Petitions to Intervene raising the same issues as the PG&E Claim were filed by the following entities: Modesto Irrigation District; Cities of Redding, Santa Clara, CA; M-S-R Public Power Agency and the Transmission Agency of Northern California; Sacramento Municipal Utility District ("SMUD"); and Turlock Irrigation District. Northern California Power Agency filed a Petition to Intervene but not a Statement of Claim. The Arbitrator's Pre-Hearing Order No. One made each of these entities a party to the Arbitration. On November 22, 2000, Cal ISO filed a Response and Counterclaim.

The subject matter of the dispute is whether Cal ISO has the requisite legal authority to impose upon PG&E certain charges for ancillary services in connection with transactions scheduled on the California Oregon Transmission Project ("COTP") and on transmission facilities owned and operated by SMUD and the Western Area Power Administration ("WAPA")

(collectively called "the Bubble"). Cal ISO imposed and collected over \$14 million in such charges until their collection was suspended in May 1999 as an outgrowth of this dispute and Cal ISO asserts the right to collect over \$40 million in additional such charges for the period following that suspension.

PG&E challenges Cal ISO's authority to impose such charges and seeks recovery of the amounts it has already paid and relief from any obligation to pay for the additional period. Cal ISO defends its authority for such charges, and its Counterclaim seeks recovery of the additional sum for the period following suspension of collection. The Intervenor is aligned with PG&E in denying Cal ISO's authority to collect these ancillary service charges.

On August 2, 2001, PG&E filed a Motion for Summary Judgment, seeking summary disposition of its Claim, and of Cal ISO's Counterclaim, without the need for further evidentiary hearing. In support of its Motion, PG&E proffered Declarations of certain persons and other materials. On August 24, 2001, Cal ISO filed its Opposition to that Motion, also attaching Declarations of certain persons and other materials. A properly noticed oral argument was held on the Motion.

In Pre-Hearing Order No. Five, the Arbitrator denied the Motion for Summary Disposition, ruling that the Tariff standard applicable to such Motions, found in §13.3.6 of the Tariff, had not been satisfied. However, the Arbitrator also ruled in that Order that the evidentiary hearing would be phased, pursuant to Rule 32(b) of the AAA Rules. In the first phase, evidence would be heard on "the decisional significance of the ISO's statements in its filing at FERC of Amendment No. 2 (FERC Docket Nos. EC96-19-015 and ER96-1663-016) and of FERC's ruling on that filing in light of those statements." Pre-Hearing Order No. Five at 14. The denial of the Motion was without prejudice to its renewal at the end of the first hearing phase. If not renewed or if made and denied, the second hearing phase would cover the remainder of the parties' presentations.

The hearing began on October 1, 2001, and proceeded as just described. In Phase I, PG&E presented testimony from two witnesses; the Intervenor presented one witness; and Cal ISO presented one witness. PG&E did renew its motion at the end of the first phase, but the Arbitrator denied it, again ruling that the rather stringent standard for granting summary disposition set forth in Tariff §13.3.6 had not been met and that a full presentation of evidence by all parties was warranted.

In the second hearing phase, PG&E presented further testimony from two witnesses in its direct case and two witnesses in its rebuttal case. The Intervenor presented testimony from six witnesses in their direct case and one witness in their rebuttal case. Cal ISO presented testimony from five witnesses.

Following the hearing, the parties filed initial and reply briefs. The arbitrator has reviewed the hearing transcripts, the exhibits admitted in evidence and the parties' briefs.

As noted at the outset, the dispute presented in this Arbitration is whether Cal ISO has the requisite legal authority to impose certain charges on PG&E for Ancillary Services in connection with COTP and Bubble transactions. PG&E seeks recovery of over \$14 million in billings for

such charges which it paid from the outset of Cal ISO operations until May 1999, when this dispute arose. Cal ISO asserts the right to retain that amount and, through its Counterclaim, seeks recovery of more than \$40 million in such charges which have accrued since billing of PG&E for the disputed items was suspended in May 1999. The Intervenor support PG&E's position on these issues, pointing out that if PG&E is liable for these amounts, it will seek to pass them through to Intervenor, for whose loads the COTP and Bubble transactions were needed.

B. Structure of the Order and Award

The outline of this Order and Award reflects the decisional structure followed by the Arbitrator in considering and deciding this matter:

1. The relevant Tariff language was considered within its four corners to determine whether it had a plain, unambiguous meaning.
2. The conclusions reached in the first step were then checked in light of a special circumstance presented here. The FERC, which is vested with authority to establish the Tariff language, had been asked by ISO prior to startup to amend the very Tariff language which is relevant here. The FERC Order addressing that Amendment No. 2 was considered, along with the representations made to FERC in pleadings which led to that Order. The Arbitrator's initial conclusions, based on the Tariff language alone were re-examined in light of that history at FERC.
3. In the event it might be needed if the appeal provisions of Tariff Article 13 were invoked, the Arbitrator considered and made findings and conclusions concerning the extrinsic evidence presented by the parties. This evidence covered discussions of the charges now in dispute, both in the period prior to startup and in the first year thereafter. The topic of Amendment No. 2 arises again in this context. Here, the focus is not on FERC's disposition of the filing, but on the status of discussions when the Amendment was filed and on the parties' understanding of FERC's action on it. The extrinsic evidence also covered the history of settlement, billing and payment of the disputed charges during that first year. This extrinsic evidence also includes consideration of the proper treatment here of a settlement filed at FERC with regard to the applicability of a certain five charges to COTP and Bubble transactions, referred to in the record and here as the GMC Settlement. The Arbitrator has set forth specific findings on the content of discussions and actions relevant to the dispute. In addition, he undertook a broader assessment of Cal ISO's

fundamental position on the disputed charges and findings and conclusions on that assessment are also set forth.

4. The Arbitrator then turned to the merits of two fallback arguments urged by Cal ISO: (a) there is a legal basis for the disputed charges even if they are not authorized by the Tariff; (b) PG&E's effort to recover the amounts it has paid for the disputed charges is time-barred by provisions of the Tariff.
5. The Arbitrator concluded with consideration of Cal ISO's Counterclaim.

II. THE MEANING OF THE TARIFF LANGUAGE

A. The Language on its Face

Consideration of Cal ISO's legal authority to impose the disputed charges must begin with the provisions of Cal ISO's FERC Tariff. As a FERC-jurisdictional utility, Cal ISO's threshold obligation with regard to imposing any charges is to demonstrate that they are authorized by a tariff on file at FERC. Montana-Dakota Utilities Co. 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). Although Cal ISO has also asserted an alternative basis for its legal authority to impose these charges (an analysis that will be addressed hereafter), its hearing presentation and briefs clearly recognize that the starting point must be the Tariff provisions.

1. Cal ISO's Position on the Tariff Language

Cal ISO points to a number of Tariff provisions as the basis for its authority, beginning with certain subsections of Tariff §§2.3 and 2.5. More specifically, the ISO refers to §2.3.1.1.1 which requires Cal ISO to "establish a WSCC approved Control Area and control center to direct the operation of all facilities forming part of the ISO Controlled Grid, Reliability Must-Run Units and Generating Units providing Ancillary Services." The definition of ISO Controlled Grid in Appendix A of the Tariff is:

"The system of transmission lines and associated facilities of the Participating TOs that have been placed under the ISOs Operational Control."

The COTP and Bubble facilities are in the Control Area operated by Cal ISO, but are not part of the ISO Controlled Grid.

Cal ISO then points to Tariff §2.3.1.2 (which requires Market Participants in the ISO Control Area to comply with ISO operating orders) and §2.5.2 (which requires that Ancillary Services meet ISO's Ancillary Service standards) as providing it with authority to ensure the

sufficiency of Ancillary Services throughout the Control Area with respect to quantity, quality and location.

Cal ISO then relies on Tariff §2.5.1, which provides in pertinent part as follows:

The ISO shall be responsible for ensuring that there are sufficient Ancillary Services available to maintain the reliability of the ISO Controlled Grid consistent with WSCC and NERC criteria. The ISO's Ancillary Services requirements may be self provided by Scheduling Coordinators. Those Ancillary Services which the ISO requires to be available but which are not being self provided will be competitively procured by the ISO from Scheduling Coordinators in the Day-Ahead Market, Hour-Ahead Market and in real time or by longer term contracts. The ISO will manage both ISO procured and self provided Ancillary Services as part of the real time dispatch. The ISO will calculate payments for Ancillary Services to Scheduling Coordinators and charge the cost to Scheduling Coordinators.

The term Ancillary Services used in Section 2.5.1 and throughout the Tariff is defined in Appendix A of the Tariff as follows:

Regulation, Spinning Reserve, Non-Spinning Reserve, Replacement Reserve, Voltage Support and Black Start together with such other interconnected operation services as the ISO may develop in cooperation with Market Participants to support the transmission of Energy from Generation resources to Loads while maintaining reliable operation of the ISO Controlled Grid in accordance with Good Utility Practice.

Referring to its Control Area operator responsibilities under WSCC and NERC standards, Cal ISO asserts that it must establish standards for Ancillary Services that maintain "Control Area Reliability." Cal ISO Initial Br., p. 5. Cal ISO's Initial Brief uses this capitalized term. Its Initial Brief further states that capitalized terms not otherwise defined are defined in Tariff Appendix A (the Master Definitions Supplement). Cal ISO Initial Brief, p. 1, fn. 1. However, this term is not defined in that Tariff Appendix. In support of its use of this term, Cal ISO refers to Tariff §§2.5.2.1 and 2.5.2.2. Section 2.5.2.1 calls upon ISO "to set the required standard for each Ancillary Service necessary to maintain the reliable operation of the ISO Controlled Grid. "Ancillary Services shall be based on WSCC Minimum Operating Reliability Criteria (MORC) and ISO Controlled Grid reliability requirements..." Section 2.5.2.2 calls upon the ISO Technical Advisory Committee to review periodically "the ISO Controlled Grid operation to determine any revision to the Ancillary Services standard to be used in the ISO Control Area..."

Cal ISO asserts that its Ancillary Service responsibilities, as spelled out in these Tariff sections, authorize it to procure Ancillary Services on the basis of Control Area reliability considerations. It then rests its Tariff authority to impose the disputed charges on the language of Tariff §2.5.1, set out above, which empowers it to procure Ancillary Services that it requires,

but that are not self provided, and to "charge the cost to Scheduling Coordinators." It offers further support in Tariff §11.2.3, from the Tariff article on Billings and Settlements. That Section covers Ancillary Services billing and cross-references §§2.5.27.1 to 4 and 2.5.28.1 to 4 with regard to calculation of the bill for each Scheduling Coordinator.

Building on its §2.5.1 authority to charge costs to Scheduling Coordinators, Cal ISO asserts that PG&E is a Scheduling Coordinator as that term is defined in the Tariff, having signed a Scheduling Coordinator Agreement dated December 9, 1997. PG&E Ex. 6. In pertinent part that Agreement provides:

The Scheduling Coordinator wishes to schedule Energy and Ancillary Services on the ISO Controlled Grid under the terms and conditions set forth in the ISO Tariff and the ISO Protocols.

* * * * *

The Scheduling Coordinator agrees that ... it will abide by, and will perform all of the obligations under the ISO Tariff and the ISO Protocols placed on Scheduling Coordinators in respect of all matters set forth therein including, without limitation, all matters relating to the scheduling of Energy and Ancillary Services on the ISO Controlled Grid....

Cal ISO points to PG&E's submission to Cal ISO of COTP and Bubble transactions, using a particular Scheduling Coordinator ID, which Cal ISO calls the separate COTP Scheduling Coordinator ID (COTP SC ID) and which PG&E calls the COTP Proxy ID. In each instance, Cal ISO and PG&E are distinguishing this COTP SC ID from the PG&E SC ID which PG&E uses for transactions using the ISO Controlled Grid, and as to which there is no dispute here on the charges imposed.

Cal ISO asserts that PG&E has a Scheduling Coordinator Agreement and that it schedules the COTP and Bubble transactions using a Scheduling Coordinator ID. Hence, says Cal ISO, PG&E is the Scheduling Coordinator for COTP and Bubble transactions. Thus under Tariff §2.5.1, Cal ISO asserts that PG&E can be charged that cost of Ancillary Services procured by Cal ISO for COTP and Bubble transactions.

Compressing Cal ISO's Tariff analysis to its essentials, Cal ISO is asserting the following: The Tariff makes Cal ISO the Control Area operator. The Control Area includes the COTP and Bubble facilities. The Tariff makes Cal ISO responsible for reliable Control Area operation and authorizes it to procure Ancillary Services needed to meet that responsibility. Cal ISO can make a determination as to Ancillary Services needed for all Control Area transactions, on both the ISO Controlled Grid and on the COTP and Bubble facilities. When it procures Ancillary Services it can charge the cost to Scheduling Coordinators. PG&E is the Scheduling Coordinator, as that term is defined in the Tariff, for COTP and Bubble transactions since it signed a Scheduling Coordinator Agreement and schedules COTP and Bubble transactions with Cal ISO using the COTP SC ID. Hence, Cal ISO is authorized to charge the cost of Ancillary

Services it procured for COTP and Bubble transactions to PG&E and PG&E is obligated by the Tariff and its Scheduling Coordinator Agreement to pay those charges.

2. The Arbitrator's Findings and Conclusions on the Tariff Language

The Arbitrator has first considered Cal ISO's analysis of the Tariff by examining the cited provisions within the four corners of the Tariff. Columbia Gas Transmission Corp., 27 FERC ¶61,089 (1984); see also United States v. Missouri-Kansas-Texas Railroad, 194 F. 2d 777, 778 (5th Cir. 1952). Cal ISO attempts to invoke the familiar administrative law legal principles calling for judicial deference to agency interpretations of their authority under governing statutes. Cal ISO suggests that its view of its Tariff authority should be given similar deference. The Arbitrator is familiar with the cases on agency deference. However, he knows of no authority for the proposition that a utility which files a tariff with a regulatory agency should be given deference with regard to its interpretation of the tariff language. Indeed, it is inconsistent with the basic notions of regulatory oversight that such deference should be afforded to a tariff-filing utility.

The Arbitrator finds and concludes that Cal ISO's position on its authority under the Tariff language, considered within its four corners, cannot be sustained. Tariff §2.3.1.1.1 directs Cal ISO to establish a Control Area and control center to direct the operation "of all facilities forming part of the ISO Controlled Grid" Tariff §2.5.1, which is central to ISO's analysis, authorizes the ISO to ensure the adequacy of Ancillary Services for the ISO Controlled Grid, not the Control Area. Ancillary Services themselves are defined to mean certain services needed to maintain reliable operation of the ISO Controlled Grid, not the Control Area. Scheduling Coordinator is defined to mean entities certified by ISO to undertake the functions specified in Tariff Section 2.2.6. With respect to the Ancillary Services function, §2.2.6.7 simply refers to providing "Ancillary Services" (i.e., by reference to reliability of the ISO Controlled Grid) in accordance with Section 2.5.1, which as noted above, refers to the ISO Controlled Grid, not Control Area. PG&E's Scheduling Coordinator Agreement with Cal ISO limits its scheduling obligations under the Tariff to matters relating to Ancillary Services on the ISO Controlled Grid. PG&E Ex. 6. No obligations with respect to non-Grid transactions are expressed. Thus, the authority to procure such Services and charge the cost to Scheduling Coordinators does not embrace transactions off the ISO Controlled Grid, such as COTP and Bubble.

As previously noted, the term Control Area Reliability, used by Cal ISO in its Brief, is not found in the Tariff. The Tariff Section referred to by Cal ISO in support of that term calls upon Cal ISO to set Ancillary Service standards needed "to maintain the reliable operation of the ISO Controlled Grid" Tariff §2.5.2.1. The only reference to ISO Control Area in the Tariff sections cited in that connection is in §2.5.2.2 which calls upon the ISO Technical Advisory Committee to undertake a periodic review of "the ISO Controlled Grid operation to determine any revision to the Ancillary Services standards to be used in the ISO Control Area."

Thus, the Arbitrator finds and concludes that the Tariff provisions on which Cal ISO relies for authority to impose charges related to COTP and Bubble transactions do not, on their face, arm Cal ISO with that authority. Cal ISO is undoubtedly, indeed concededly, the Control Area operator for a Control Area that includes the ISO Controlled Grid as well as the COTP and

Bubble facilities. However, the Tariff provisions defining its authority with respect to Ancillary Services procurement define its responsibilities not by reference to the Control Area, but with respect to the ISO Controlled Grid, which does not include the COTP and Bubble facilities.

The Arbitrator can find no language within the four corners of the Tariff that authorizes Cal ISO, on the basis of its Control Area responsibilities, to impose charges on Scheduling Coordinators for transactions that are within the Control Area but do not use the ISO Controlled Grid.

B. The Significance of FERC's Decision on Amendment No. 2

The Arbitrator's conclusion about the unambiguous meaning of the Tariff language is strongly reinforced by the history of Amendment No. 2. In the midst of negotiations with PG&E and the Intervenor concerning the treatment of COTP and Bubble transactions, Cal ISO sought approval from FERC for Tariff changes, including changes in the very sections on which it now relies. Those changes would have resolved the question of authority for charges for Ancillary Services with respect to COTP and Bubble transactions entirely in accordance with Cal ISO's present position.

Amendment No. 2 was filed by Cal ISO on February 25, 1998, five weeks before the start of ISO's operation, and in the midst of intensive, ongoing discussions with PG&E and Intervenor on the handling of COTP and Bubble transactions. In the Amendment, Cal ISO sought, among other things, to modify the language of a number of Tariff sections, including each and every one of the Tariff sections discussed above which used the phrase "ISO Controlled Grid."

Indeed, in its FERC submission, the ISO stated:

The ISO is filing amendments to a number of sections of the ISO Tariff, including the ISO Protocols and the *pro forma* Scheduling Coordinator Agreement, to clarify the distinction between the "ISO Controlled Grid" and the "ISO Control Area." These terms are *not* interchangeable, yet they are not precisely distinguished in the ISO Tariff. In some instances, the terms are either not applied appropriately or are ambiguous as to applicability. The ISO therefore proposes the addition of new defined terms in the ISO Tariff - "ISO Control Area" and "Existing Control Agreement" - along with certain consequential amendments to the ISO Tariff, including the ISO Protocols and *pro forma* Scheduling Coordinator Agreement.

Undoubtedly referring, at least in part, to the discussions on COTP and Bubble transactions which were ongoing at the time of the FERC filing, the ISO's proposed Amendment further stated:

This amendment will resolve several areas of misunderstanding regarding the obligations of Scheduling Coordinators with respect

to schedules for transactions into, out of, within, or through the ISO Control Area

To achieve these goals, Cal ISO proposed to insert in the Tariff a new defined term, "ISO Control Area." It then proposed to amend a number of Tariff Sections that use "ISO Controlled Grid," by substituting "ISO Control Area" and, in some instances, by referring to scheduling of Energy and Ancillary Services "into, out of, within, or through the ISO Control Area." PG&E Ex. 2, p. 7. A number of new sub-sections were proposed for addition to Tariff Section 2.4. PG&E Ex. 2, pp. 14-16.

A new proposed defined term, Existing Control Agreement, was proposed. PG&E Ex. 2, p. 32. It described agreements between Participating Transmission Owners, such as PG&E, and Non-Participating Transmission Owners, such as the Intervenors, as owners of COTP and Bubble facilities, covering facilities not on the ISO Controlled Grid, but in the Control Area. Using this defined term, the proposed new sub-sections of Tariff §2.4.4.6 would have effectively brought the non-participating transmission owners into the ISO's dispute resolution mechanisms with respect to, among other things, charges for Ancillary Services. PG&E Ex. 2, pp. 14-16.

The Amendment also proposed changes directly affecting the Tariff terms concerning Cal ISO's relationship with PG&E with respect to charges for COTP and Bubble transactions. Thus, Tariff §2.5.1 would have been amended to state that the ISO is "responsible for ensuring that there are sufficient Ancillary Services available to maintain the reliability of the ISO Control Area" (Emphasis added.) not the ISO Controlled Grid, as the unamended Tariff §2.5.1 provides. PG&E Ex. 2, p. 16. With this change, the ISO's authority under this Section to procure Ancillary Services it deemed necessary for the ISO Control Area and to charge Scheduling Coordinators for the cost would have embraced the COTP and Bubble transactions.

The pro forma Scheduling Coordinator Agreement, which is used as the PG&E/ISO Agreement would have been amended to provide that:

The Scheduling Coordinator agrees that:

- A. the ISO Tariff and the ISO Protocols govern all aspects of scheduling of Energy and Ancillary Services into, out of, within or through the ISO Control Area ...

* * * * *

- B. it will abide by, and will perform all of the obligations under the ISO Tariff and the ISO Protocols placed on Scheduling Coordinators in respect of all matters set forth therein including, without limitation, all matters relating to the scheduling of ... Ancillary Services into, out of, within or through the ISO Control Area ... [and] ongoing obligations in respect of ... billing and payments

PG&E Ex. 2, pp. 38-39.

If thus amended, the terms of the Scheduling Coordinator Agreement between PG&E and ISO would have obligated PG&E to pay the charges for Ancillary Services procured by the ISO for COTP and Bubble transactions.

In short, adoption by FERC of the Tariff changes proposed by Cal ISO in its filing of Amendment No. 2 would have resolved the issues which later arose in this Arbitration and there would have been no dispute. However, FERC did not accept any of the Amendment No. 2 proposals. It rejected the proposed Amendment in toto. California Independent System Operator Corp., Order Conditionally Accepting and Rejecting Proposed Amendments to the ISO Tariff and Protocols, 82 FERC ¶61,312 (1998). This Order is in this record as PG&E Ex. 3.

Beyond question Cal ISO understood, and brought to FERC's attention, the impact of the changes in the Tariff and the pro forma Scheduling Coordinator Agreement on its authority to impose charges for Ancillary Services. In both the Amendment, and in its cover letter to FERC, Cal ISO said:

Costs for Ancillary Services purchased from the ISO auction are included in the statement sent to the Scheduling Coordinator. Without a requirement that all Schedules be submitted in the requisite form through a Scheduling Coordinator, the ISO would not have ... the necessary contractual relationship by which to charge for Ancillary Services [U]nless an entity acts through a Scheduling Coordinator, should such an entity fail to self-provide Ancillary Services ... there would be no ... contract path by which to seek payment. [Emphasis in original.]

PG&E Ex. 1, pp. 8-9; PG&E Ex. 2, p. 5.

Further, there can be no doubt that FERC understood PG&E's role in connection with COTP and Bubble transactions as it presently operates under the unamended Tariff provisions on which Cal ISO now relies for its Tariff authority. In its Order rejecting the Amendment, FERC summarized the objections raised by opponents of the Amendment, which included PG&E and the intervenors. In doing so, FERC stated:

PG&E states that it is willing to continue in its role of accepting schedules for use of the Non-ISO controlled facilities at issue in Amendment No. 2 by serving as the collection point for schedules. PG&E would, in turn, provide the ISO with all of the schedule information that the ISO needs to perform its responsibilities as Control Area Operator.

PG&E Ex. 3, pp. 11-12.

FERC's discussion of its own basis for rejecting Amendment No. 2 is brief. However, its decisional language must, of course, be read and understood on the assumption that FERC had reviewed and understood the representations made to it in the filing and the oppositions. Indeed, its summary description of the parties' positions makes it clear that this is the case. PG&E Ex. 3, pp. 2-4, 9-12. FERC stated that ISO's proposed changes were "unjust and unreasonable

because they would broadly expand ISO control over non-jurisdictional facilities which are not being transferred to the ISO's control" (*Id.* at 12), i.e., the COTP and Bubble facilities, *inter alia*. FERC also pointed out that the proposed changes "would improperly impose additional obligations on Participating Transmission Owners." *Id.* PG&E is one of those Participating Transmission Owners.

However, the "additional obligations" to which FERC referred could not have included PG&E's role in accepting COTP and Bubble schedules and providing them to ISO. The opposition filed at FERC by TANC, also an Intervenor here, describes in detail the discussions between PG&E and Cal ISO concerning COTP transactions and spells out PG&E's refusal to be a Scheduling Coordinator, as that term is defined in the Tariff, with regard to COTP transactions. SMUD Ex. 2, p. 63, ¶127. Simultaneously TANC described the very role PG&E presently plays with regard to those transactions. *Id.* SMUD's pleading attached as an exhibit a letter from PG&E spelling out its position in precisely those terms. *Id.* With these representations before it, FERC's Order described the role that PG&E was willing to perform (PG&E Ex. 3, pp. 11-12) and directed it to continue in that role saying "we will require all public utilities involved to continue to cooperate fully with the ISO to achieve the necessary information flow that has evolved during the testing period." *Id.* at 12. The additional obligations FERC was unwilling to impose in this connection must have been additional payment obligations.

Cal ISO urges a different view of its Amendment No. 2 filing and FERC's decision concerning it. Cal ISO asserts, first, that the heart of the issues in Amendment No. 2 was the Grid Management Charge ("GMC"). Further, says Cal ISO, it filed Amendment No. 2 in an effort to establish a direct contractual relationship with Intervenor, through which it could impose Ancillary Services charges for COTP and Bubble transactions. Cal ISO was not concerned, it claims, with its contractual relationship with PG&E since it had the authority it required for COTP and Bubble transactions under the existing Scheduling Coordinator Agreement in the record here as PG&E Ex. 6.

The Arbitrator has carefully considered Cal ISO's position on Amendment No. 2. In deciding the two Motions for Summary Disposition made by PG&E and the Intervenor, the Arbitrator applied the standard of Tariff §13.3.6 to Cal ISO's position on Amendment No. 2 and concluded that it was not possible to rule that ISO's argument lacked a good faith basis in fact or law. The Arbitrator has now considered those arguments on the broader question as to their substantive merit.

It is certainly true that concern with the applicability of the GMC to non-ISO Controlled Grid transactions was a dominant concern in the filing and in FERC's decision. However, it was certainly not the only issue raised in the pleadings and in the FERC Order. Charges for Ancillary Services for such transactions were clearly put on the table by the ISO filing and by the oppositions to it. The "additional obligations" which the FERC recognized in its Order, and was unwilling to impose, certainly embraced not just the GMC, but the contract path for collecting Ancillary Services charges on non-Controlled Grid transactions and PG&E's refusal to become a Scheduling Coordinator, within the Tariff's reach, for COTP transactions.

Cal ISO's filing sought to amend the pro forma Scheduling Coordinator Agreement so that it would expressly extend to Ancillary Services in the Control Area and thus embrace COTP

and Bubble transactions. Cal ISO's intention was that the amended form of Agreement would be substituted for the Agreement with PG&E then in effect and still in effect today. Tr. 333-35; 396-97. Cal ISO's witness, Kyle Hoffman, was asked by the Arbitrator to reconcile this proposed change in the language of the Scheduling Coordinator Agreement with Cal ISO's argument that the unamended Agreement already covered COTP and Bubble transactions. Mr. Hoffman's response was that Cal ISO was simply trying to improve the basis on which PG&E could pass these charges through to COTP and Bubble participants. The Arbitrator did not find this rationale persuasive in light of PG&E's opposition to all of Amendment No. 2, including this change to the Agreement, and in light of TANC's representations to FERC, supported by PG&E's own letter, that PG&E was refusing in the ongoing discussions preceding the filing to act as Scheduling Coordinator, as defined in the Tariff, for COTP transactions. Moreover, as previously noted, the Arbitrator concludes that the language of the Agreement, on its face, does not extend PG&E's obligations to COTP and Bubble transactions. In these circumstances, the Arbitrator cannot credit Cal ISO's contention that (a) PG&E was already obligated to pay for Ancillary Services related to COTP and Bubble transactions; and (b) Cal ISO's objective in the Amendment No. 2 filing was limited to extending the Tariff's reach to COTP and Bubble parties other than PG&E.

Thus, the conclusions reached by the Arbitrator as to the extent of Cal ISO's authority under the language within the four corners of Tariff provisions are fully supported by the history of Cal ISO's attempt to amend that language and FERC's decision on that effort.

III. FINDINGS AND CONCLUSIONS ON EXTRINSIC EVIDENCE CONCERNING THE TARIFF'S PROVISIONS

Given the Arbitrator's finding and conclusion that the Tariff on its face does not give Cal ISO the authority to impose the disputed charges for Ancillary Services related to COTP and Bubble transactions, resort to extrinsic evidence in order to determine the Tariff's meaning is unnecessary as a matter of law. Columbia Gas Transmission Corp., 27 FERC ¶61,089 (1984). Nor does the Arbitrator have any authority to modify the Tariff provisions. Montana-Dakota Utilities Co., v. Northwestern Pub. Serv. Co., 341 U.S. 246, 251 (1951). However, the Arbitrator is aware that the dispute resolution procedures in Tariff Article 13 include the right to appeal an arbitration award to FERC or a court of competent jurisdiction. Tariff §13.4.1. The permitted grounds for appeal are "that the award is contrary to or beyond the scope of the relevant ISO Documents, United States federal law, including, without limitation, the FPA, and any FERC regulations and decisions, or state law." *Id.* These permitted grounds are substantially broader than the bounds for appellate challenge typically found in arbitration clauses. In such circumstances, the Arbitrator has determined that it is appropriate to review and consider the record and set forth here, for use if needed, findings and conclusions concerning the extrinsic evidence presented by the parties in this case. The record does contain such evidence since ISO argued that, if there was ambiguity in the Tariff language, extrinsic evidence supported its position. The Arbitrator closely considered this evidence as it was being presented at the hearing, weighing credibility issues where appropriate. In addition, he has undertaken a thorough review of the post-hearing briefs and record evidence following the hearing's conclusion.

A. Discussions Between the Parties on COTP and Bubble Transactions

As the date for the startup of ISO's operations approached, intensive discussions were taking place among ISO representatives, PG&E representatives, and Intervenor representatives on an important unresolved issue: the procedures for scheduling transactions on transmission facilities which would not be turned over to the ISO for operational control; and the imposition of charges by Cal ISO with respect to transactions on such facilities. The facilities involved, which were referred to in the record as non-ISO Controlled Grid facilities, included COTP and the Bubble, each of which was briefly described at the start of this Order. The discussions of charges certainly focussed principally on the GMC and the Grid Operations Charge (GOC). However, those discussions also included treatment of Ancillary Services, and charges therefor, for COTP and Bubble transactions. PG&E presented the testimony of one witness who participated in those discussions (Metague). Cal ISO's witnesses included three such participants (Fluckinger, LeVine and Graves) and one witness whose participation was largely in post-startup discussions (Hoffman). Two Intervenor witnesses had participated in those discussions and four other Intervenor witnesses testified concerning their understanding as to the relevant outcome of the discussions. Related discussions continued after startup.

In March, 1998, with Cal ISO startup just a few weeks away, the issues under discussion were unresolved. Cal ISO was still seeking to apply the GMC and GOC to COTP and Bubble transactions and PG&E and the Intervenors were resisting that effort. With respect to Ancillary Services for such transactions, representatives of PG&E and the Intervenors had described the existing arrangements for such services used in connection with PG&E's role as operator of its Control Area. Under those arrangements, the Intervenors were self-providing ancillary services pursuant to various agreements they had with PG&E. These included the Coordinated Operations Agreement (COA), which governed COTP, and various Interconnection Agreements covering other transmission facilities of Intervenors, which came to be known for present purposes as Bubble facilities. The COA and Interconnection Agreements between PG&E on the one hand and SMUD, NCPA, Santa Clara, Modesto Irrigation District, and Turlock Irrigation District, respectively, were made part of the record. ISO Ex. 2; SMUD Ex. 4; NCPA Ex. 3; SVP Ex. 1; TID Ex. 2. The pertinent contract covering self-provision by Redding was also an exhibit. Redding Ex. 1. In addition, an Interim Agreement and a Restated Interim Agreement between PG&E, SMUD and Cal ISO was also submitted. ISO Ex. 6; SMUD Ex. 3. This documentation shows that these entities had ancillary service self-provision arrangements in place in their dealings with PG&E concerning COTP and the Bubble.

In the discussions with ISO on charges for COTP and Bubble Ancillary Services, the ISO representatives were undoubtedly expressing the view that Ancillary Services charges should be assessed for COTP and Bubble transactions where such services were not self-provided, while, also undoubtedly, PG&E and Intervenors representatives were resisting imposition of those charges and pointing to the existing arrangements for self-provision. When pressed by ISO representatives as to what would happen if such self-provision did not, in fact, occur, the PG&E representative responded that if self-provision did not happen, PG&E and the Intervenors would be responsible for charges; PG&E then pressed to turn to other topics under discussion, e.g., the GMC. The Arbitrator has considered the testimony on this exchange and finds that PG&E's fundamental position on the subject was that self-provision would be present, and that its comment when pressed was in the nature of a negotiating response rather than a meeting of the

minds and agreement to pay COTP and Bubble Ancillary Services charges when incurred by Cal ISO.

Apart from these findings that the content of the discussions does not support a conclusion that agreement was reached, Cal ISO's presentation appears to rely on the oral exchange itself as an adequate basis for imposing the disputed charges. Even if such an agreement had thus been reached, the Arbitrator concludes it would not suffice to provide Cal ISO with the legally required authority to impose charges. Such an exchange must find expression in Tariff language that could reasonably be interpreted, in light of the oral exchange, to so state. An oral agreement would not suffice. See, e.g., Pacificorp Electric Operations, 60 FERC ¶61,200 at 1992 WL 430671 * 4 (1992).

Meanwhile, on February 25, 1998, Cal ISO made its Amendment No. 2 filing. Two weeks later oppositions to that Amendment were filed. PG&E's position in that Docket on acting as Scheduling Coordinator, as that term is defined in the Tariff, for COTP and Bubble transactions, has been described above. On March 27, 1998, the Commission issued its Order rejecting the changes proposed in Amendment No. 2. No evidence was offered by either party that the filing or FERC's Order was ever a direct topic in these discussions. PG&E, for its part, took the FERC Order rejecting Amendment No. 2 to vindicate its position that it could provide the scheduling information for COTP and Bubble transactions using the COTP SC ID and not be Scheduling Coordinator for those transactions, as that term is defined in the Tariff, and used in the Scheduling Coordinator Agreement. In other words, PG&E's staff believed that there would be no charges for Ancillary Services on COTP and Bubble transactions. Cal ISO's staff obviously believed there would be such charges since it pursued the billing and settlement practices to be described below.

In this same time frame, Cal ISO reached agreement with PG&E and others on treatment of the GMC and GOC and three other charges with respect to non-ISO Controlled Grid transactions. That agreement was filed with FERC as an Offer of Settlement on April 7, 1998. Cal ISO Ex. 1. Under it, the GMC, the GOC and charges for Black Start, Voltage Support and Unaccounted for Energy were not assessed on COTP and Bubble transactions. Under the express terms of the Offer of Settlement, it can only be regarded as the resolution of the dispute concerning the five just-enumerated charges covered by that agreement. The Offer of Settlement cannot be deemed to constitute approval or agreement by its parties to any other matters purportedly underlying the issues covered by the settlement. *Id.* at pp. 12-23, ¶27. Nor can it be relied on by its parties to assert or infer that the settlement of the issues covered has a precedential effect on any other substantive matter. *Id.* at pp. 13-14, ¶29. The settlement of the dispute about the GMC and the other four charges, therefore, cannot be regarded here as implying any sort of resolution concerning the other charges which were simultaneously under discussion, i.e., the Ancillary Services charges in dispute here.

Very little contemporaneous documentation of the pre-startup discussions was provided in the record. One set of notes of an internal Cal ISO meeting on March 20, 1998 not surprisingly appears to reflect the ISO position that Ancillary Services charges should apply. ISO Ex. 9. A second set of notes was proffered as notes of a meeting four days later between Cal ISO and PG&E representatives, although the Arbitrator finds the ISO witness' recollection concerning these notes unreliable and is not able to conclude that they reflect such a meeting.

ISO Ex. 10A. There is an apparent reference in them to Ancillary Services, with a possible indication that PG&E would pay for such services but the Arbitrator cannot reach any reliable conclusions on the basis of this document.

A draft COTP SC ID Scheduling Procedure prepared by Kevin Graves, an ISO witness was admitted in the record. ISO Ex. 20. This document was prepared contemporaneously with the notes in ISO Ex. 10A, i.e., on March 23 or 24, 1998. Mr. Graves had participated in the March 20 meeting reflected in ISO Ex. 9. This draft Scheduling Procedure was never put in place.

However, the Arbitrator notes that it contains the statements "All transactions scheduled by PG&E using the COTP SC_ID are such that no ISO charges should be calculated. The ISO will modify data in the ISO's Scheduling Infrastructure (SI) such that no charges will be calculated for the COTP SC_ID." ISO Ex. 20, p. 4. [Emphasis supplied.] It also states in an earlier section "PG&E will schedule this information through the WENET using the ISO's standard Templates provided that charges are not calculated and charges to PG&E for these transactions." ISO Ex. 20, p. 1. [Emphasis supplied.]

Mr. Graves testified that it was not his intent in drafting this language, which repeatedly referred to "no charges," to indicate that Ancillary Services charges would not accrue in these transactions. The Arbitrator does not find it necessary to determine whether he finds this statement credible. However, this document does provide significant support for the Arbitrator's conclusion that the communications taking place at this time on these charges, whether internal to Cal ISO or in discussions between the parties, were less than perfect. Thus, the few contemporaneous documents in the record are consistent with a finding that there was no meeting of the minds in the pre-startup discussions on treatment of Ancillary Services charges for COTP and Bubble transactions.

B. Post Startup Settlements and Billing

When Cal ISO began operations on April 1, 1998. Cal ISO had been fully informed through its discussions with PG&E and the Intervenor as to the nature of the arrangements in place for self-provision of Ancillary Services for COTP and Bubble transactions. Using the COTP SC ID, PG&E began its scheduling of COTP and Bubble transactions. After working out some initial technical issues, this scheduling was done through the ISO's Scheduling Infrastructure. PG&E did not submit self-provision schedules for Ancillary Services in connection with these COTP SC ID schedules. However, the self-provision arrangements with Intervenor which had been described to Cal ISO in the pre-startup discussions remained in place. Cal ISO's operational procedures were such that (a) Cal ISO made no direct effort, e.g., by phone or fax, to determine whether the self-provision procedures described to Cal ISO by the COTP and Bubble participants were in place; and (b) that Ancillary Services were procured by the ISO for these COTP and Bubble transactions. Cal ISO's billing and settlement systems picked up the cost of these Ancillary Services procured by ISO and assigned them to PG&E.

The extrinsic evidence proffered and relied on by Cal ISO included the history of the settlement and billing of those costs. The Arbitrator finds the facts as to that history are as follows: Using computer technology, Cal ISO provided PG&E with Preliminary Settlement

Statements for the COTP SC ID, as well as for the PGAE SC ID the SC ID used by PG&E for submitting schedules for transactions which used the ISO Controlled Grid). PG&E's Settlements staff spent ninety-nine percent of its time on the PGAE Preliminary Settlement Statements and only one percent on the COTP Preliminary Settlement Statements. This allocation of effort was based in part on PG&E's understanding that there would be no charges associated with the COTP SC ID, and in part on the fact that PG&E had the ability to challenge the Preliminary Settlement Statements within an eight-day period, while the Final Settlement Statements were not subject to a challenge process. Moreover, the Final Settlement Statements for the COTP SC ID were being driven to zero. PG&E's Manager of Settlements had been informed of FERC's decision rejecting ISO's Amendment No. 2 at the time it was issued. It was the understanding of PG&E's personnel involved in this settlements review process that this FERC Order confirmed PG&E's position that it would not incur charges for transactions on the non-ISO Controlled Grid.

On the Final Settlement Statements, the now-disputed charges for Ancillary Services, which had first appeared on the COTP SC ID Preliminary Settlement Statements, would appear on the PGAE SC ID Statement having been transferred there from COTP SC ID Preliminary Statements by Cal ISO through a manual process. These transfers on the PGAE Statements were overlooked by PG&E's settlement review personnel during the first year of Cal ISO operation and the invoices based on the PGAE SC ID Final Settlement Statements were paid by PG&E.

It should be noted that PG&E's Manager of Settlements, whose testimony was discussed above, was on maternity leave for a portion of Cal ISO's first year of operations. Having considered the testimony from both parties on this subject, the Arbitrator finds that, during the tenure of her substitute, he had noted charges on the COTP SC ID Settlement Statements and made inquiry about them with Cal ISO. The results of that inquiry were inconclusive, but PG&E's substitute Manager of Settlements was not informed that these charges were being transferred to the PGAE SC ID and charged to PG&E, a result he would have questioned, because he shared the PG&E understanding that no charges were to apply to COTP and Bubble transactions.

In April of 1999, PG&E's Manager of ISO Contracts, a peer manager of its Manager of Settlements, learned at a meeting with ISO that the COTP SC ID charges were being transferred to the PGAE SC ID statements and charged to and paid by PG&E. The Manager of ISO Contracts had been told by a Cal ISO representative prior to ISO startup that the GMC would not be applied to COTP and Bubble transactions, but other charges would apply. After this conversation, FERC's Order rejecting ISO's Amendment No. 2 had been issued. It was also her understanding that PG&E had repeatedly said that it would not undertake the scheduling function for COTP and Bubble transactions if any charges were to be incurred. Hearing the information in April, 1999 that PG&E has been incurring these charges caused surprise and dismay for the Manager of ISO Contracts since it was contrary to her belief as to the understandings which had been reached. She consulted with PG&E's Manager of Settlements, who had returned from maternity leave and was also unaware that these charges were being made to PG&E and paid.

Following up on this information, a process was initiated which ultimately led to the present dispute before the Arbitrator.

C. Cal ISO's Position that PG&E Must be Considered Scheduling Coordinator for COTP and Bubble Transactions

There is one thread that runs through Cal ISO's position on both the plain meaning of the Tariff language, and on its view of the extrinsic evidence demonstrating the intent of the Tariff. This is the contention that, for COTP and Bubble transactions, PG&E is the Scheduling Coordinator, as that term is defined in the Tariff, and used in the pertinent Tariff sections and the Scheduling Coordinator Agreement. This point is so central to Cal ISO's overall position that it merits the Arbitrator's direct focus here even though much of the Arbitrator's findings and conclusions which touch on it have already been stated.

Cal ISO points out that PG&E has signed a Scheduling Coordinator Agreement. PG&E Ex. 6. It further points out that PG&E submits the COTP and Bubble transactions through the ISO's Scheduling Infrastructure using the COTP SC ID. Cal ISO points out other entities that have only one Scheduling Coordinator Agreement and use more than one SC ID on which they schedule Grid and non-Grid transactions. ISO Ex. 11, 12, 13. As a Scheduling Coordinator, submitting COTP SC ID Schedules, says ISO, PG&E must be regarded as the COTP Scheduling Coordinator, subject to the obligation set forth in Tariff §2.5.1 to pay for Ancillary Services procured by ISO for COTP schedules. Further, says ISO, when PG&E agreed to submit the COTP schedules using the COTP SC ID, it agreed to pay for charges imposed on such schedules other than the five charges covered by the GMC Settlement. Finally, Cal ISO urges that FERC rejected PG&E's effort to extricate itself from its obligations as Scheduling Coordinator under the Tariff for COTP schedules when it rejected PG&E's proposal to amend the Coordinated Operations Agreement (COA) which governs PG&E's functions as operator of the COTP. ISO Ex. 2. All of these arguments except the last one have already been addressed.

First, the Arbitrator has concluded that the language of the Tariff provisions and of the Scheduling Coordinator Agreement addresses transactions on the ISO Controlled Grid and does not authorize charges for non-ISO Controlled Grid transactions in the Control Area operated by ISO. Second, the Arbitrator has noted PG&E's express position in connection with Amendment No. 2 that it was not willing to act as Scheduling Coordinator, as defined in the Tariff, for COTP transactions. FERC's requirement, while rejecting Amendment No. 2, that PG&E act as the conduit to Cal ISO for such transactions indicates FERC's acceptance of the position PG&E described to it. The Arbitrator has found no basis for a conclusion that, in pre-startup discussions, PG&E agreed to assume the obligations of a Tariff-defined Scheduling Coordinator for COTP and Bubble transactions.

This leaves Cal ISO's final point on this question, i.e., FERC's Orders rejecting PG&E's effort to amend the COA. Pacific Gas and Electric Company, 93 FERC ¶61,322 (2000); rehearing denied, Pacific Gas and Electric Company, 94 FERC ¶61,204 (2001). These Orders are in the record as ISO Exs. 4 and 5, respectively. The Arbitrator has determined above that, in its ruling rejecting ISO's Amendment No. 2, FERC understood that PG&E was not willing to be Scheduling Coordinator under the Tariff for COTP scheduling. Given this understanding, the Arbitrator concludes that FERC's choice of language in rejecting PG&E's proposed amendment of the COA, i.e., its reference to PG&E's effort "to assign its scheduling coordinator duties and responsibilities" (PG&E Ex. 5, pp. 7-8), cannot be regarded as a recognition that PG&E is the COTP Scheduling Coordinator, as defined in the Tariff, for COTP. Indeed, there is every reason

to conclude that FERC chose its words carefully in this COA Order to make its ruling on the COA proposed amendment consistent with its disposition of Amendment No. 2.

In short, the Arbitrator finds and concludes that PG&E is a Scheduling Coordinator under the Tariff for transactions on the ISO Controlled Grid, but is not in that status with respect to COTP and Bubble transactions.

This conclusion concerning PG&E's status as a Scheduling Coordinator under the Tariff renders moot Cal ISO's further contention that it has not been shown that the ISO has ever waived its right under the Tariff and the Scheduling Coordinator Agreement to impose charges on PG&E for Ancillary Services with respect to COTP and Bubble transactions. Since no such right has ever arisen, there is no need for a showing that Cal ISO has not waived it.

IV. CAL ISO'S ALTERNATIVE BASIS FOR LEGAL AUTHORITY

At the hearing, and in its brief, Cal ISO urges a fall back position should the Arbitrator conclude, as he has, that Cal ISO does not have authority under the Tariff to impose the disputed CORP and Bubble charges. Cal ISO argues that there is an exception to the filed rate doctrine, i.e., that "utilities are entitled to recover the actual costs they incur even when they have failed to file the necessary rate information." ISO Initial Brief, pp. 29-30. In support of this purported legal principle, Cal ISO cites Central Maine Power Co., 56 FERC ¶61,200 (1991); Central Hudson Gas & Electric Corp., 61 FERC ¶61,089 (1992); Pacificorp Electric Operations, 60 FERC ¶61,292 (1992); Coastal Oil & Gas Corp. v. FERC, 782 F. 2d 1249 (5th Cir. 1986); and Transcontinental Gas Pipe Line Corp. v. FERC, 998 F. 2d 1313 (5th Cir. 1993).

The Arbitrator has reviewed and considered each of these decisions. They provide no support whatever for the proposition asserted by Cal ISO on the basis of them. Indeed, they lead precisely to the opposite conclusion. The three FERC decisions cited do not address the possibility of cost recovery in the absence of a tariff filing. They represent instances in which FERC was insisting on the need for such filings. The subject being addressed by FERC was the proper exercise of the discretion granted it by §205 of the Federal Power Act (FPA) (16 U.S.C. §824(d)) to waive the notice requirements of the statute with regard to such tariff filings. In each instance addressed in those cases, the utilities involved had submitted the agreements involved as tariff filings under §205 of the FPC, albeit after service under those agreements had begun.

The utilities were not asking to impose charges not authorized by a filed tariff. Rather, they were seeking the waiver of notice requirements needed to achieve acceptance of the filing so that the agreements could become filed tariffs authorizing the charges. The Commission's discussion of permitting recovery of certain costs incurred was in the context of the conditions it would impose upon grant of a waiver of the notice requirement for tariff filings, not a ruling that such costs could be recovered in the absence of a filed tariff.

Perhaps most pertinent here is an observation by FERC in the Pacificorp Electric Operations order, supra, 60 FERC ¶61,292, 1992 WL 430671 * 4. Of course, the underlying premise of this entire argument presented by ISO is the assumption that in this proceeding there has been a ruling that there is no tariff on file authorizing the disputed charges. In its brief on this argument, Cal ISO specifically cites to Pacificorp and relies "on the 'oral understanding' that

PG&E would Schedule the COTP transactions [and] pay for Ancillary Services procured by ISO when such services were not self-provided” ISO Initial Brief at 32. Yet, we find FERC emphatically stating in Pacificorp “We cannot allow utilities ... to evade their statutory filing responsibilities by operating under unfiled ‘oral understanding’ rather than filed agreements.” Pacificorp Electric Operations, supra, 60 FERC ¶61,292; 1992 WL 430671 * 4.

Similarly, the Coastal and Transco cases were not situations creating exceptions to the filed rate doctrine. In each instance, the Court was reviewing the Commission’s handling of situations in which the regulated entity had not complied with its obligations under filed tariffs or certificates of public convenience and necessity. The Court rulings dealt with limitations on the Commission’s authority to impose penalties, not with a utility’s right to impose charges in the absence of a filed tariff.

The fallback argument justifying recovery of certain costs in the absence of a filed tariff is without basis in law and is rejected by the Arbitrator.

V. THE ARGUMENT THAT PG&E’S CLAIM IS TIME-BARRED

Cal ISO offers one further fallback argument should the Arbitrator rule that the disputed charges are not authorized by the Tariff. This is the assertion that the ISO Tariff provisions preclude PG&E from contesting the validity of those charges because it did not do so in a timely manner. ISO Initial Brief at 34-36.

The Arbitrator has made a factual finding above, having considered all the record evidence on the subject, that PG&E did not discover the billing treatment being given the disputed charges until April of 1999. Taking into account all of the further findings as to the understanding of the parties, respectively, concerning the treatment to be accorded such charges and the rationale for PG&E’s conduct of the billing and settlement review process, the Arbitrator finds no basis on which to conclude that PG&E was deficient in not discovering these facts earlier.

In urging this point, Cal ISO relies on the FERC’s rulings in November, 1999, and March of 2000 on certain Tariff changes, put in place on ISO’s initiative, concerning procedures for disputing changes on Final Settlement Statements. See Tariff §11.6 and 11.7; California Independent System Operator, 89 FERC ¶61,229 (1999); and California Independent System Operator, 90 FERC ¶61,315 (2000). On the basis of these provisions added to the Tariff in 2000, and FERC’s observations in accepting them, Cal ISO asserts that PG&E’s present claim is time-barred. The Arbitrator concludes that this assertion must be rejected. In accepting the Tariff changes, FERC stated:

The ten-day final bill validation period does not represent a ‘statute of limitations’ ... since the tariff provides Scheduling Coordinators with the ability to bring a dispute before the ISO Governing Board at any time. This existing provision will better serve PG&E [which had sought making the settlement re-Run provision retroactive] as well, as it allows PG&E to challenge a billing dispute at any time

California Independent System Operator, *supra*, 89 FERC ¶61,229; 1999 WL 1411328 at * 9.

Thus, in accepting the Tariff revisions on disputing changes on Final Settlement Statements, FERC was careful to preserve existing Tariff rights under Article 13. Having found, as a factual matter, that PG&E was not deficient in learning of the disputed charges before April 1999, PG&E's invocation of the dispute procedures in Article 13 of the Tariff was certainly timely and within the bounds recognized by the Commission in accepting the Tariff changes in its 1999 and 2000 orders cited above.

VI. CONCLUSIONS ON WEIGHING COMPETING EQUITIES IN THE DISPUTE

In reaching the findings and conclusions stated in this Order and Award, the Arbitrator has been mindful of Cal ISO's assertions concerning its responsibilities as operator of the Control Area which includes not only the ISO Controlled Grid, but also the COTP and Bubble facilities. Cal ISO argues that it incurred the disputed costs in the good faith discharge of its responsibility to maintain reliability of the Control area. It asserts that it has incurred these costs and should be able to recover those costs from somebody and that PG&E is the logical candidate. Cal ISO is unquestionably operator of that Control Area. As such, it has responsibility to satisfy NERC, WSCC and MORC reliability standards. The Arbitrator finds on the basis of the record evidence, though, that Cal ISO is not alone in having that responsibility and further finds as follows.

PG&E and the Intervenors also have obligations to meet NERC and MORC standards. The obligations these entities had in place under their existing agreements concerning COTP and Bubble facilities were undertaken, in part, to satisfy that responsibility. Cal ISO was informed of those arrangements in the discussions preceding startup of its operations.

It was within Cal ISO's judgment to determine what was required by its responsibility as operator of a Control Area wider than that which PG&E operated using the ancillary service self-provision arrangements in place with Intervenors. Cal ISO had knowledge of those arrangements. Because of the manner in which PG&E provided COTP and Bubble scheduling information through Cal ISO's Scheduling Infrastructure, Cal ISO exercised its judgment to operate on a basis that did not take into account these existing arrangements. It was further Cal ISO's judgment to procure, in these circumstances, additional Ancillary Services related to COTP and Bubble schedules.

Finally, it was also Cal ISO's judgment to pursue the course of action it took in this regard knowing the content of its Tariff language and knowing the action which FERC had taken on the pertinent Tariff language when it rejected Amendment No. 2.

The Arbitrator concludes that it is neither fair and equitable, nor consistent with controlling legal standards as to Cal ISO's Tariff authority, to find that the PG&E should bear the cost of these exercises of judgment as to how Cal ISO should meet its responsibilities as Control Area operator. It was the structure put in place by the decision to revamp the California electric industry and to create and vest Cal ISO with its Control Area responsibilities that led to these added costs for COTP and Bubble related ancillary services. The Arbitrator concludes that

spreading those costs across all participants in that structure is not unreasonable in such circumstances. It is, of course, not within the scope of the Arbitrator's authority in this arbitration to require that result. However, the Arbitrator records his conclusion in that regard as a factor in rejecting Cal ISO's claim that it should prevail, in part, because the costs it seeks to recover were the product of the discharge of its responsibility as Control Area operator to satisfy certain applicable standards.

VII. CAL ISO'S COUNTERCLAIM

Finally, there is Cal ISO's Counterclaim. The Arbitrator has concluded that Cal ISO did not have the legal authority to impose the disputed Ancillary Services charges for COTP and Bubble transactions from April 1998 through April 1999 which PG&E seeks to recover through its claim in this arbitration. It follows that, for the same reasons, Cal ISO's Counterclaim is denied. This renders moot the dispute as to whether Cal ISO had ever agreed to forego recovery of those charges if its view of its authority to impose them prevailed. Again, for possible use if this Award is appealed under Article 13, the Arbitrator has considered the record evidence on that dispute and finds that Cal ISO had agreed only to suspend billing of those charges during pendency of this Arbitration and had not consented to forego pursuit of collecting those charges if Cal ISO's view of their legality prevailed.

ORDER AND AWARD

On the basis of the findings of fact and conclusions of law stated above, the Arbitrator makes the following Award:

1. PG&E's Claim is granted. Cal ISO shall reimburse PG&E in the amount of \$14,172,337.08 in costs for procuring Ancillary and other services in connection with COTP and Bubble scheduling information submitted to Cal ISO by PG&E during the period from March 31, 1998 through April 30, 1999. Such reimbursement shall be paid with interest calculated in accordance with the definition of Interest in Appendix A to the ISO Tariff, Sheet No. 325.
2. Cal ISO's Counterclaim is denied in its entirety.
3. The Arbitrator's Award on the Statements of Claim filed by Modesto Irrigation District, The City of Redding California, the City of Santa Clara, California, the M-S-R Public Power Agency, the Transmission Agency of Northern California, Turlock Irrigation District and the Sacramento Municipal Utility District is subsumed in the Arbitrator's Award in paragraph 1, above, on PG&E's Claim since each of these Statements of Claim sought the identical relief requested by PG&E.
4. The administrative fees and expenses of the American Arbitration Association ("the Association") shall be borne by PG&E and Cal ISO pro rata. The compensation and expenses of the Arbitrator in this Arbitration shall be borne pro rata by each side in the dispute, with the portion borne by the PG&E side allocated pro rata among PG&E and the Intervenors, all of whom sought relief identical to PG&E's Claim. Thus, Cal ISO shall bear fifty percent of such compensation and expenses. The remaining fifty percent shall be borne in equal portions by PG&E and the Intervenors, i.e., SMUD, Modesto Irrigation District, Northern California Power Agency, Transmission Agency of Northern California, the City of Redding California, the City

of Santa Clara, California, M-S-R Public Power Agency, and Turlock Irrigation District. These Association fees and expenses and the compensation and expenses of the Arbitrator total \$119,682.18. Therefore, Cal ISO shall pay to PG&E the sum of \$5,419.63, representing PG&E's share of deposits previously advanced the Association. Cal ISO shall pay to SMUD the sum of \$5,419.63, representing SMUD's share of deposits previously advanced the Association. Cal ISO shall pay to TANC and Modesto Irrigation District the sum of \$617.84, representing TANC's and Modesto's share of deposits previously advanced the Association. Cal ISO shall pay to NCPA the sum of \$5,419.63, representing NCPA's share of deposits previously advanced the Association. Cal ISO shall pay to Turlock Irrigation District the sum of \$5,419.63, representing Turlock's share of deposits previously advanced the Association. Cal ISO shall pay to the Association the sum of \$10,698.31 representing amounts still due the Association and/or the Arbitrator. City of Redding, California, City of Santa Clara, California, and M-S-R Public Power Agency shall be jointly and severally liable to pay to the Association the sum of \$4,183.94 representing amounts still due the Association and/or the Arbitrator.

5. Each of the aforementioned parties to the Arbitration shall bear its own costs and fees.

IT IS SO ORDERED:

Dated: December 13, 2001

George A. Avery
Arbitrator