UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	**)** **)**	**Docket No. ES00-____-___**

APPLICATION OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION FOR AUTHORIZATION UNDER SECTION 204 OF THE FEDERAL POWER ACT TO ISSUE SECURITIES

The California Independent System Operator Corporation ("ISO") respectfully requests, pursuant to Section 204 of the Federal Power Act and Part 34 of the Federal Energy Regulatory Commission's ("Commission's") regulations thereunder, that the Commission authorize the ISO to issue bonds in an amount not to exceed $295,000,000.

I. BACKGROUND AND REASONS FOR FILING

The proceeds from this bond offering will be used for two purposes. First, approximately $263,000,000 of the bond proceeds will be used to refinance the ISO's existing debt with a lower cost form of credit enhancement, allowing the ISO to save an anticipated $1 million to $2 million over the life of the bonds.

The ISO's November 14, 1997 filing[1] requested Commission approval to issue up to $260,000,000 in long-term bonds; the Commission granted the

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1 *California Independent System Operator Corporation's Application Under Section 204 of the Federal Power Act for an Order Authorizing the Issuance of Securities*, Docket No. ES98-9-000.

request.[2] This amount was later increased to $310,000,000 in a filing dated March 13, 1998,[3] which the Commission also approved.[4] The ISO issued a total of $301,400,000 in long-term bonds in May 1998, resulting in 1998 Series A, B, C, and D variable-rate demand bonds. The ISO's first amortization payment in April 1999 brought the outstanding amount of these bonds down to $282,500,000. The proceeds from this bond issuance were used to retire the ISO's start-up financing provided by the ISO Restructuring Trust, provide for working capital, and provide funds for capital expenditures for future years.

Because the ISO was a new entity without a stand-alone credit rating, it was required to obtain credit enhancement to sell these bonds. The ISO obtained such credit enhancement through a direct-pay letter of credit with a reputable bank. Since it commenced operations, the ISO has established a credit history and, accordingly, it has become possible for the ISO to receive a stand-alone credit rating. Consequently, the ISO has reexamined its credit structure and has determined that it is feasible for the ISO to replace its existing letter of credit with bond insurance and a liquidity line of credit, providing significant overall cost savings over the life of the bonds. The ISO is proceeding with a plan to refund its existing bonds and to reissue new bonds backed with the bond insurance effective March 1, 2000.

2 *See California Independent System Operator Corporation*, 81 FERC ¶ 62,220 (1997).

3 *Amendment to the California Independent System Operator Corporation's Application Under Section 204 of the Federal Power Act For an Order Authorizing the Issuance of Securities*, Docket No. ES98-9-001.

4 *See California Independent System Operator Corporation*, 83 FERC ¶ 62,039 (1998).

A secondary purpose of the bond offering is to obtain additional funding for capital expenditures for the years 2000 and 2001. A total of $30,000,000 in new funding is requested. Approximately $8 million to $10 million will be allocated toward meeting year 2000 capital expenditures, with the balance for use in 2001 or beyond. In November 1999, the ISO's Board of Governors approved a year 2000 capital budget of $40.1 million. The ISO has identified internal funding of approximately $32 million that can be used, with the balance requiring outside funding, hence the need for this additional debt issuance. The internal funding consists of Grid Management Charge ("GMC") collections into the ISO's operating reserve above the 15% requirement identified in the ISO's GMC formula, and remaining funds on hand from the ISO's 1998 bond issuance of approximately $16 million.

The ISO is not requesting that any changes be made to the GMC formula currently in effect. Additionally, the ISO is not requesting any changes to its most recent GMC filing made on December 15, 1999, which resulted in a proposed year 2000 GMC of $.8300/MWh. The amortization of the debt resulting from the planned March 1, 2000 debt issuance will differ slightly from the amortization of the ISO's current debt; however, the amount is not significant enough to require a change in the ISO's GMC. This is because the amortization of the increased amount of this borrowing will effectively be deferred until 2001, and the marginally higher overall interest expense in 2000 will be funded from the ISO's Operating Reserve.

II. INFORMATION REQUIRED BY 18 C.F.R. § 34.3

As required by Section 34.3 of the Commission's regulations, 18 C.F.R. § 34.3 (1999), the ISO provides the following information:

(a) Applicant's official name and principal business address.

California Independent System Operator Corporation
151 Blue Ravine Road
Folsom, California 95630

(b) State of incorporation and principal place of business.

The ISO was incorporated in the State of California on May 5, 1997. The ISO provides transmission service over the facilities that comprise the ISO Controlled Grid, which are principally located within the State of California.

(c) The name, address and telephone number of the person at the ISO authorized to receive notices and communications regarding this application.

William J. Regan, Jr.
Chief Financial Officer
California Independent System
Operator Corporation
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Tel: (916) 351-4450
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The ISO requests that notices regarding this filing also be sent to:

Kenneth G. Jaffe
Scott P. Klurfeld
Bradley R. Miliauskas
Swidler Berlin Shereff Friedman, LLP
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Washington, DC 20007
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Counsel for the California Independent
System Operator Corporation

(d) Requested action date.

The ISO respectfully requests that the Commission act by February 15, 2000, to permit the planned March 1, 2000 issuance date.

(e) Description of the securities to be issued.

1. Type and nature of the securities.

The securities to be issued are tax-exempt, variable-rate demand bonds. The bonds will bear interest in one of several modes, either at a daily, weekly, or monthly rate. Initially, the ISO will issue the bonds to bear interest at a weekly rate. The bonds will be amortized over 8 years, with principal payments scheduled to result in level overall annual debt service. The ISO will also have in place an interest rate swap to result in a net fixed rate for the ISO. The interest rate swap will cover approximately 2/3 of the outstanding bonds. Accordingly, the ISO will have net floating rating interest exposure with regard to about 1/3 of the total issuance.

2. Amount of securities.

The amount of securities is not to exceed $295,000,000. The attached pro forma schedules are based on an issuance amount of $289,600,000, which is the ISO's current estimate of the total issuance.

3. **Interest or dividend rate.**

The bonds will bear interest at a floating rate. The overall debt cost to the ISO is expected to be in the range of 4.5% to 4.75%.

4. **Dates of issuance and maturity.**

The bonds will be issued on March 1, 2000, and will be amortized to approximately 2008. Increasing annual principal payments will be made over time, resulting in level overall debt service to the ISO.

5. **Institutional rating, estimated future rating, or an explanation of why the securities are not rated**

The ISO is in the process of finalizing stand-alone credit ratings with two rating agencies. The ISO has secured an "A2" rating from Moody's Investors Service and expects to secure a rating of "A" or better from Standard & Poor's. In addition, the bonds themselves will have a credit rating based on the overall structure including bond insurance.

(f) The purpose for which the securities are to be issued.

The securities are issued primarily to refinance existing outstanding debt. In addition, new funding of $30 million will be obtained to finance year 2000 and 2001 capital expenditures.

(g) State applications.

No application with respect to this issuance is required to be filed with any state utility regulatory body. As is necessary for the issuance of tax-exempt debt, the bonds will be issued through a conduit issuer, the

California Infrastructure and Economic Development Bank. The ISO filed its application for issuance through this body on December 27, 1999. The ISO's 1998 bond issuance was conducted through the California Economic Development Financing Authority, a predecessor to the above entity.

(h) Facts relied upon to show that the issuance is lawful and necessary.

This transaction is being executed primarily to restructure existing debt, with the objective of generating an overall cost savings for ratepayers. As discussed above, depending on the final costs for bond insurance, a liquidity line of credit, and other transaction costs, the ISO anticipates saving $1 million to $2 million over the life of the bonds. The proceeds derived from this cost savings may be used to fund necessary capital improvements or to reduce the GMC.

The ISO's Board of Governors has not yet adopted a resolution with respect to this bond issuance. This resolution is scheduled for presentation and adoption at the January 2000 meeting. Once the ISO Board of Governors adopts the bond issuance, the ISO will forward copies of the adopting resolutions to the Commission. The ISO requests that the Commission accept this filing with the understanding that these additional materials will be provided as soon as practicable.

(i) Statement of bond indentures and/or other limitations on issuance of debt.

The bond indenture on the ISO's new debt will contain terms similar to those regarding its 1998 issuance. The 1998 bonds are secured by a pledge of all operating revenues. The agreement with the letter of credit provider for the ISO's existing debt provides for a limitation of additional indebtedness not to exceed $75,000,000. While this agreement will be terminated upon the execution of agreements for the ISO's new debt, it is anticipated that agreements with the bond insurer and liquidity provider will contain similar restrictions on the issuance of additional debt.

(j) Summary of rate changes.

The ISO does not anticipate that any changes to the rate filed on December 15, 1999 will be necessary due to the issuance of this debt. In December 2000, the ISO will make its normal filing for the annual GMC to incorporate budgeted operating costs and the new debt amortization schedule.

(k) Form of notice.

A Form of Notice is attached hereto and an electronic version in WordPerfect format has been included with this filing.

III. INFORMATION REQUIRED BY 18 C.F.R. § 34.4

In support of this application, the ISO submits the following exhibits:

Exhibit A — The Articles of Incorporation of the California Independent System Operator Corporation, dated May 5, 1997

Exhibit B — Resolutions adopted by the ISO Board of Governors authorizing the initial 1998 bond issuance. The ISO Board's

January 2000 resolutions will be provided as described in Section II(h) of this filing.

Exhibit C	Official Statement for the 1998 California Economic Development Financing Authority Variable Rate Demand Revenue Bonds (California Independent System Operator Project)
Exhibit D	Projected Pro Forma Balance Sheets for the twelve months ending December 31, 1999 (data contained in the "Before Transaction" column), and for the twelve months ending December 31, 2000 (data contained in the "After Transactions" column); and Schedule of Pro Forma Adjustments to Section 35 Filing, dated December 15, 1999
Exhibit E	Projected Pro Forma Income Statements for the twelve months ending December 31, 1999 (data contained in the "Before Transaction" column), and for the twelve months ending December 31, 2000 (data contained in the "After Transactions" column)
Exhibit F	Projected Pro Forma Statement of Cash Flows for the twelve months ending December 31, 1999 (data contained in the "Before Transaction" column), and for the twelve months ending December 31, 2000 (data contained in the "After Transactions" column); and calculation of interest coverage

IV. REQUEST FOR EXEMPTION FROM OR, IN THE ALTERNATIVE, WAIVER OF, THE REQUIREMENTS OF 18 C.F.R. § 34.2(a)

With respect to the ISO's proposed bond issuance, 18 C.F.R. § 34.2(b)(4) provides an exemption from the competitive bid and negotiated placement requirements of 18 C.F.R. § 34.2(a). The exemption applies to securities to be issued "in support of or to guarantee securities issued by governmental or quasi-governmental bodies for the benefit of the utility."

A governmental entity, the California Infrastructure and Economic Development Bank, is to issue the bonds for the benefit of the ISO. The ISO has selected J. P. Morgan Securities, Inc. to act as underwriter of the bonds. The

ISO is confident that the underwriter's fee that J. P. Morgan is to charge represents an attractive option relative to other alternatives in the market.

Should the above exemption be deemed not to apply to the proposed bond issuance, the ISO respectfully requests a waiver of the requirements contained in 18 C.F.R. § 34.2(a). The ISO believes the waiver should be granted for the following reasons:

1) *Transaction Costs*: This transaction is primarily a restructuring of the ISO's outstanding debt in order to enhance the security structure, reduce the cost of credit enhancement, and increase flexibility. J. P. Morgan, the underwriter of the original issuance of debt in 1998, indicated at that time that ongoing credit enhancement costs and financial flexibility could be improved once the ISO established a sound operating history. Consequently, J. P. Morgan has proposed enhancements to the existing debt structure and has offered to execute the restructuring at a reduced rate. The proposed underwriter's discount for the transaction is estimated to be under $1 per $1,000 of debt, which is approximately half of the industry standard for similar transactions.

2) *Variable Rate Debt*: The refunding and new money debt that the ISO will be issuing through the California Infrastructure and Economic Development Bank will be weekly adjustable tax-exempt variable rate bonds. The initial underwriting, to be managed by J. P. Morgan, will produce an interest cost to be in effect for only one week. The actual

interest rates thereafter will be reset on an ongoing basis as determined by at least two and as many as three remarketing agents (including J. P. Morgan), as part of a continuation of the competitive process established in 1998. Therefore, given the type of debt being issued, there would be no additional benefit in having multiple *initial* underwriters. In fact, additional underwriters would result in increased costs to the ISO. A competitive pricing advantage will be realized by the ISO through the ongoing repricing, on a weekly basis, of the outstanding securities by competing remarketing agents.

V. SERVICE OF DOCUMENTS

The ISO has served copies of this transmittal letter and all attachments on the California Public Utilities Commission, the California Energy Commission, and the California Electricity Oversight Board. In addition, the ISO is making the transmittal letter and attachments available to all California market participants by posting them on the ISO Home Page, www.caiso.com.

VI. SUPPORTING DOCUMENTS

In addition to this transmittal letter and the exhibits described above in Part III, this filing is supported by a draft notice of this filing, suitable for publication in the Federal Register (Attachment A), together with a diskette in WordPerfect format containing that notice in electronic form.

VII. CONCLUSION

WHEREFORE, the ISO respectfully requests that the Commission take the following actions with respect to this application:

- authorize the ISO's proposed bond issuance in the amount of $295,000,000;
- grant the appropriate exemption from or, in the alternative, waiver of, the requirements of 18 C.F.R. § 34.2(a), concerning the methods by which securities are to be issued; and
- issue its order authorizing the above requests by no later than February 15, 2000.

Respectfully submitted,

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President and Chief Executive Officer
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