UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
and Nora Mead Brownell.

Mirant Delta, LLC and Mirant Potrero, LLC, Complainants, v. California Independent System Operator Corporation, Respondent.	Docket No. EL01-35-000
San Diego Gas & Electric Company, Complainant, v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange, Respondents, et al.	Docket No. EL00-95-005 Docket No. EL00-95-012
California Independent System Operator Corporation	Docket No. ER01-1877-000 Docket No. EL00-95-030 Docket No. EL00-98-029
Operational Audit of the California Independent System Operator	Docket No. PA02-1-000
California Independent System Operator Corporation	Docket No. RT01-85-000
Pacific Gas and Electric Company	Docket No. RT01-83-000
San Diego Gas & Electric Company	Docket No. RT01-82-000

Docket Nos. EL01-35-000, et al.

Southern California Edison Company Docket No. RT01-92-000

ORDER CONCERNING GOVERNANCE OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION

(Issued July 17, 2002)

1. The California Independent System Operator Corporation (CAISO) is a public utility as defined in section 201(e) of the Federal Power Act (FPA),[1] and its transmission services and sales for resale of electric energy in interstate commerce (i.e., its operation of imbalance energy markets) are within this Commission's exclusive jurisdiction. In light of the recommendations in a January 25, 2002 independent consultant's audit report on the CAISO and other factors associated with the recent California energy crisis, we make several findings with respect to the future governance of the CAISO and order the CAISO to take certain actions. We find that the continuation of the existing Board will hamper the ability of the CAISO to implement the CAISO's market redesign proposal,[2] and thus this Commission's ability to ensure non-discriminatory transmission services and just and reasonable rates in the West. This is because the State-controlled Governing Board of the CAISO (Board) is not capable of operating its interstate transmission facilities on a non-discriminatory basis. The Board continues to be in non-compliance with our December 15, 2000 order, establishing remedies for the California electricity markets,[3] and Order No. 888,[4] governing independent system operators. The Board, as presently

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[1]See 16 U.S.C. § 824(e).

[2]The CAISO's market redesign proposal is being addressed concurrently with this order. See California Independent System Operator Corporation's Comprehensive Market Redesign Proposal, Docket No. ER02-1656-000 (2002).

[3]See San Diego Gas & Electric Company, et al., 93 FERC ¶ 61,294 (2000) (December 15 Order), order on reh'g, 97 FERC ¶ 61,275 (2001) (December 19 Order), appeal filed sub. nom. California ex rel. Lockyer, 9th Cir. No. 01-71944 (2001), reh'g denied, 99 FERC ¶ 61,160 (2002) (May 15 Order).

[4]See Order Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, 61 Fed. Reg. 21,540 (1996), FERC Stats. & Regs. ¶ 31,036 (1996), order on reh'g, Order No. 888-A, 62 Fed. Reg. 12,274 (1997), FERC Stats. & Regs., Regs. Preambles January 1991-June 1996 ¶ 31,036 (1997), order

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constituted, does not meet the independence requirement of Order No. 2000,[5] governing regional transmission organizations (RTOs).[6]

2. Because of these problems with the current Board, we direct the CAISO, following the procedures discussed below, to adopt a two-tier form of governance by January 1, 2003. The top tier will consist of an independent, non-stakeholder Board, while the lower tier will consist of an advisory committee (or committees) of stakeholders, which may recommend options to the Board, and an advisory committee of the California Electricity Oversight Board (Oversight Board), which will serve as the state of California's (State) and its agencies' representative in advising the Board.[7] The top tier will have sole decision-making authority in all matters.

3. We do not issue ths directive lightly. Given the severe problems (e.g., price volatility) in California and Western energy markets in 2000-2001, it is critical that the Western interstate transmission grid, including the California portion of the grid, be operated in a coordinated, non-discriminatory manner that leads to the most efficient use

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[4](...continued)
on reh'g, Order No. 888-B, 62 Fed. Reg. 64,688, 81 FERC ¶ 61,248 (1997), order on reh'g, Order No. 888-C, 81 FERC ¶ 61,046 (1998), aff'd in part sub nom. Transmission Access Study Group v. FERC, 225 F. 3d 667 (D.C. Cir. 2000), cert. granted, 69 U.S.L.W. 3574 (Nos. 00-568 (in part) and 00-809) and cert. denied, id. (No. 00-800) (U.S. Feb. 26, 2001).

[5]See Regional Transmission Organizations, Order No. 2000, 65 Fed. Reg. 809 (Jan. 6, 2000), FERC Stats. & Regs. ¶ 31,089 (1999), order on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (Mar. 8, 2000), FERC Stats. & Regs. ¶ 30,092 (2000), review pending sub nom. Public Utility District No. 1 of Snohomish County, Washington, v. FERC, Nos. 00-1174, et al. (D.C. Cir.).

[6]On June 1, 2001, the CAISO, see Docket No. RT01-85-000 (2001); Southern California Edison Company (SoCal Edison), see Docket No. RT01-92-000 (2001); San Diego Gas & Electric Company (SDG&E), see Docket No. RT01-82-000 (2001); and Pacific Gas & Electric Company (PG&E), see Docket No. RT01-83-000 (2001), made RTO filings pursuant to the Commission's directives in San Diego Gas & Electric Company, et al., 95 FERC ¶ 61,115 (2000) (April 26 Order). In this order, we act on the independence aspect of the CAISO's RTO filing. We will act on other aspects of that filing in a later order.

[7]See, e.g., Order No. 2000 at 31,073 (stating that the dominant governance model for ISOs is a two-tier form of governance).

of electric energy resources in the Western region. Events of the last two years have demonstrated all too well the regional, interstate nature of the Western grid. At times, disruptions in historical trading patterns between California and neighboring states and flaws in California's market design and institutions, among other things, have contributed to a reduction of electricity supplies and an increase in electricity prices, to varying degrees, in all Western states. We acknowledged the reciprocal energy relationship of Western states in our orders adopting price mitigation for California and the other states in the Western Electricity Coordinating Council.[8] The only real, lasting solution to these current problems is to promote, rather than undermine, the same type of regional cooperation, reflecting natural markets, that the Commission is promoting in other regions of the country.[9]

4. The current operation of the California transmission grid serves only to prolong, if not exacerbate, the conditions that led to the California energy crisis and the ripple effects of that crisis on other Western states. Transmission owners are reluctant to turn over operational control of their facilities to the CAISO. Accordingly, the CAISO's transmission grid must be operated by entities independent from power market participants and undue parochial influences. In the long-run, energy customers will be protected only if we eliminate disincentives to adding new supply and transmission capability in California.[10]

5. However, we recognize the difficult transition to a competitive market that California, in particular, is undergoing and the immediate tasks facing the CAISO. We therefore emphasize that our directives provide the State the opportunity to advise the new independent Board by directing the creation of an advisory committee that will consist of the Oversight Board.

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[8]See April 26 Order, 95 FERC ¶ 61,115; San Diego Gas & Electric Company, 95 FERC ¶ 61,418 (2001). In addition, the Commission's Staff examined historical trading patterns, according to which California and other Western states have relied on imports during periods of peak energy demand, in market reports issued on November 1, 2000 and February 1, 2001.

[9]See, e.g., PJM Interconnection, L.L.C., 96 FERC ¶ 61,061 (2001); GridSouth Transco, LLC, et al., 96 FERC ¶ 61,067 (2001).

[10]A recent Government Accounting Office report (GAO Report) states that developers have been deterred from investing in the California market, resulting in less new generation and, in turn, less supply. See Restructured Electricity Markets: Three States' Experience in Adding Generating Capacity, GAO REP. NO. 02-427, at 30-32 (May 2002).

6. We issue this order at this time for several reasons. The Commission was reluctant to take further action on the issue of independence when energy prices were exceptionally volatile in California. Moreover, as the Commission-initiated Operational Audit of the California Independent System Operator (Audit Report) recognizes, the present Board's ability to manage through the crisis was an improvement on the prior Board.[11] In addition, the Commission wanted to avoid any undue additional pressure on the CAISO management (Management), which was performing its job as well as could be expected under the circumstances,[12] and any uncertainty regarding its decision-making process during that period. However, prices have become more stable in California. More importantly, the Audit Report[13] has revealed significant problems concerning the independence of the current Board. Given the Commission's directives in a concurrent order[14] that redesign aspects of the markets operated by the CAISO, this is an appropriate time to address critical independence issues that have important ramifications for these markets.[15] Further, while price stabilization has been caused in part by actions taken by

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[11]See Audit Report at 25-26, Docket No. PA02-1-000 (2002) (stating that the original Board was "very effective until the crisis hit in mid-2000"); id. at 30 (stating that "[t]he current [Board] served its purpose during the recent crisis"). The Audit Report was contracted for following the Commission's request, on October 9, 2001, for a proposal to conduct an audit report of the CAISO, covering the period between October 2000 and October 2001. An independent consulting firm issued the Audit Report on January 25, 2002.

[12]As the Audit Report notes, it was "impress[ive] how well the organization functioned under the incredible stress placed on it." See Audit Report at 10.

[13]See generally Audit Report.

[14]See See supra note 2.

[15]In the December 19 Order, the Commission made the following statement concerning the time that it would issue an order concerning the CAISO's governance structure:

> There are a number of pending proceedings that implicate the ISO's current governance structure and the extent of its independence. The context for approaching ISO governance has changed dramatically since issuance of the December 15 Order. The Commission finds it more appropriate to address governance issues in the context of these other, more recently filed

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the Commission, it has also been caused by more unpredictable, less controllable factors such as weather conditions. For all these reasons, we take advantage of this opportunity to address the independence problem now so that we can help restore confidence in the California markets and thus attract the infrastructure investment needed to provide a long-term solution to California's supply deficiency.

Background

7. The Commission initially authorized the establishment of the CAISO in orders issued on November 26, 1996[16] and December 18, 1996.[17] On October 30, 1997, the Commission issued an order authorizing the CAISO to commence its operations.[18] In that order, the Commission evaluated the CAISO's proposal in light of the ISO principles established in Order 888, including Principle No. 1, which concerns governance and independence. The Commission stated in that order that the Board "will affect matters within the Commission's exclusive jurisdiction, [and] that the Commission must eliminate any unduly discriminatory provisions that relate to the Governing Boards that will oversee jurisdictional activities. . . ."[19]

8. On November 1, 2000,[20] the Commission proposed specific remedies to address dysfunctions in California's wholesale bulk power markets, including a proposed remedy

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proceedings. In addition, a Commission-initiated operational audit of the ISO is currently underway. Therefore, the arguments and concerns raised herein will be addressed in a future order.

97 FERC at 62,228-29.

[16]See San Diego Gas & Electric Company, et al., 77 FERC ¶ 61,204 (1996).

[17]See Pacific Gas & Electric, et al., 77 FERC ¶ 61,295 (1996).

[18]See Pacific Gas & Electric, 81 FERC ¶ 61,122 (1997).

[19]Id. at 61,450.

[20]See San Diego Gas & Electric Company, et al., 93 FERC ¶ 61,121 (2000) (November 1 Order), order on reh'g, December 19 Order, 97 FERC ¶ 61,275 (2001), appeal filed sub. nom. California ex rel. Lockyer, 9th Cir. No. 01-71944 (2001), reh'g denied, May 15 Order, 99 FERC ¶ 61,160.

concerning the governance structure of the CAISO.[21] Specifically, we determined that the then-existing Board, which consisted of 26 members that were chosen from various stakeholder groups, was having "such difficulty reaching decisions on the complex and divisive issues confronting it that it has become ineffective."[22] We further concluded that Board members were coming under "undue pressure from various sources," and, as a result, the Board was not functioning in an independent manner.[23] Therefore, the November 1 Order proposed that the then-serving Board be replaced with an independent, non-stakeholder Board, effective 90 days after the date of that order.[24] We further proposed a transition mechanism in which the CAISO's chief executive officer (CEO) would select an independent consultant, who would, in turn, prepare a slate of candidates from which the then-existing Board members would pick a nine-member Board.[25]

9. After reviewing comments on the proposals in the November 1 Order, we issued the December 15 Order, in which we made revisions to certain aspects of the November 1 Order proposal, including the requirement that the existing stakeholder Board be replaced with a non-stakeholder Board whose members are "independent of market participants."[26] In addition, noting "the complex jurisdictional issues involved and the benefits of avoiding litigation," we called for "further on-the-record procedures to discuss with California representatives the selection process for the new ISO Board."[27] Pending those discussions, the Board was to turn over decision-making power and operating control to Management by January 29, 2001, with the Board members then serving as a stakeholder advisory committee until the new Board was seated.[28] The CAISO's bylaws were to become null and void, as of January 29, 2001, to the extent they were inconsistent with

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[21] See November 1 Order, 93 FERC at 61,362-65.

[22] Id. at 61,363. In addition, in the November 1 Order, we found that the PX stakeholder Board had become ineffective and proposed that it also be replaced with an independent, non-stakeholder Board, effective 90 days after the date of that order. See id.

[23] Id.

[24] See id. at 61,364.

[25] See id.

[26] December 15 Order, 93 FERC at 62,013.

[27] Id.

[28] See id. at 62,013-014.

the directives in the December 15 Order.[29] We also stated that "if no consensus is reached regarding an acceptable means to select new CAISO Board members [by April 29, 2001], then the procedures proposed in the November 1 Order will be carried out."[30]

10. The on-the-record CAISO Board proceeding established under the December 15 Order did not occur because of several actions at the State level. On January 18, 2001, the Governor of California (Governor) signed a bill passed by the California State Legislature (ABX1 5) that authorized the replacement of the then-existing Board with a five-member, non-stakeholder Board appointed by the Governor, subject only to confirmation by the Oversight Board, a California state agency.[31] This State law states that members may not be "affiliated with any actual or potential participant in any market administered by the Independent System Operator."[32] The law further describes that the Oversight Board "shall require the articles of incorporation and bylaws of the Independent System Operator to be revised" to reflect the new governance structure and "shall make filings with the Federal Energy Regulatory Commission as the Oversight Board determines to be necessary."[33] In addition, the law provides that "the Independent System Operator may not enter into a multistate entity or a regional organization as authorized in Section 359 unless that entry is approved by the Oversight Board."[34]

11. The Governor nominated five California residents to the Board: the California Secretary of Business, Transportation, and Housing; a senior advisor to the Governor; an attorney with the Utility Reform Network; an attorney with a California law firm, who was also a former chair of the Oversight Board; and the president of the Silicon Valley Manufacturing Group.[35] The Oversight Board confirmed the Governor's nominees on January 23, 2001. That same day, the California Attorney General filed a complaint in Sacramento County Superior Court to compel the 26 stakeholder members of the Board to

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[29]See id. at 62,014.

[30]Id.

[31]See CAL. PUB. UTIL.§ 337(b) (West 2001).

[32]Id. § 337(b).

[33]Id. § 337(d).

[34]Id. § 352.

[35]See Press Release from Office of the Governor of California, Governor Davis Names Members of the CAISO Board (Jan. 24, 2001) at http://www.governor.ca.gov.

resign immediately. Those stakeholder members resigned on January 25, 2001, and the five individuals selected by the Governor assumed control of the Board.[36] The Governor subsequently signed an executive order (E.O. D-23-01) that directed the new Board to revise certain provisions of the CAISO tariff to reflect the recommendations of the Oversight Board.[37]

12. On January 17, 2001, the Governor issued an emergency proclamation giving the California Department of Water Resources (DWR), which is a department of the State government that reports directly to the Governor, authority to enter into arrangements to purchase power.[38] DWR began purchasing under this authority the next day. The California State Legislature has since passed legislation authorizing and appropriating funds for such purchases.[39] DWR has purchased substantial amounts of capacity and energy in the CAISO's imbalance market and has entered into long-term contracts for electric energy to serve retail load in California. As a result of these activities, DWR is now the largest purchaser of energy in the California wholesale market.

13. In our April 26, 2001 order on prospective price mitigation for the CAISO's markets,[40] we conditioned price mitigation on the CAISO and the California investor-owned utilities (IOUs) filing an RTO proposal by June 1, 2001.[41] As stated above, see supra note 5, these parties filed an RTO proposal on June 1, 2001.

14. Finally, as mentioned above, on January 25, 2002, an independent consulting firm filed its Audit Report with the Commission, in which it makes recommendations to the Commission concerning prospective improvements that can be made to help the CAISO in effectively fulfilling its responsibilities to operate the transmission system under its

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[36]The CAISO failed to file amended bylaws, pursuant to the requirements of section 205 of the Federal Power Act (FPA), 16 U.S.C. § 824d (1994), to reflect the changes made to its Board until April 26, 2001.

[37]See Cal. Exec. Order No. D-23-01 (Feb. 8, 2001).

[38]See Proclamation, Cal. Gov. (Jan. 17, 2001).

[39]See CAL. WATER CODE § 80,104 (West 2001).

[40]See April 26 Order, 95 FERC ¶ 61,115.

[41]See id. at 61,362.

control and administer certain real-time energy markets.[42] First and foremost, we address the Audit Report's recommendations concerning the independence of the CAISO.[43] As the Audit Report finds "[o]ne of the lynch pin [sic.] issues that needs to be resolved is the governance of the CAISO . . . [u]ntil it is resolved, there is no hope for a comprehensive solution"[44] for the problems in California. Accordingly, we will address the remaining Audit Report recommendations after an independent Board is seated on January 1, 2003.

15. The Audit Report finds that the current Board "has served its purpose" but is not "the appropriate governing body going forward."[45] According to the Audit Report, "[d]espite the best intentions of the new [Board] to be fair and independent, the net result

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[42]The Audit Report does not address the merits of whether the formation of the current Board was legal and appropriate. However the Audit Report states that "[r]egardless of the legality of the Governor naming [the Board], the almost universal reaction of the industry was that the CAISO was no longer independent. From that time on, suppliers, [load serving entities] and other control areas assumed that all the actions of the CAISO were directed and/or approved by the Governor's office or his appointees." Audit Report at 30.

[43]The Audit Report states that it would "be impossible to implement all recommendations over the same time frame. Therefore, these recommendations would need to be prioritized." Id. at 4. In addition, the Audit Report maintains that "[n]ot all recommendations can be implemented by FERC. Many will require cooperation and actions by various California regulators and agencies." Id.

[44]Id. at 9.

[45]Audit Report at 30.

of their inception was a loss of independence by the CAISO."[46] Therefore, the Audit Report recommends that:

> As with the original Stakeholder Board, the recent Governor's Board, has had a finite life, which must come to an end. The first step to resolving the many problems at the CAISO, in particular the perception of independence from the State, and the California energy industry more generally, is to create an independent, 'corporate type' of Board of Governors which consists of qualified professionals that do not have any financial or political ties to any of the parties. In conjunction with the establishment of a new Board, a Stakeholder Advisory Committee must be formed to address and resolve complex issues based on input from all parties.[47]

The Audit Report states that the approach it puts forth for selecting a new, independent Board "can be modified in many respects, however, [it] caution[s] that it must ultimately result in a [Board] that is independent in the eyes of all stakeholders and the management and employees of the CAISO."[48] Furthermore, the Audit Report finds that such a Board,

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[46]Id. at 31. The Audit Report finds that "[u]ltimately the real test of how effective the Governor's Board was are the results of its tenure. . . . [T]he overall results have led to a series of major problems." Id. at 31. Furthermore, according to the Audit Report:

> "[o]ne measure of the effectiveness of [the current Board] is the view by virtually all of the officers at the CAISO that the current [Board] is not independent or effective on long-term issues. They identified the following as evidence of the lack of independence and effectiveness: Pressure to provide [DWR] personnel with access to the operating floor and key market information. The lack of significant or meaningful long-term planning. The lack of progress on ongoing projects such as the Congestion Management Reform. A general lack of understanding of some complex issues that need to be addressed. Discontinuance of formal Board committees such as the Audit Committee."

Id. at 31.

[47]Id. at 36.

[48]Id.

which has "no stakeholder affiliations or pre-dispositions[,] will be able to restore the confidence of all market participants in the even-handness of the [CA]ISO."[49]

Instant Pleadings

16. Pleadings concerning the governance directives of our December 15 Order have been filed in the following Docket Nos.: EL01-35-000; EL00-95-005 and EL00-95-012; ER01-1877-000, EL00-95-030, and EL00-98-029; PA02-1-000; and RT01-85-001, RT01-83-000, RT01-82-000, and RT01-92-000. Because of the overlap in the issues raised, this order addresses all these pleadings.[50]

A. Docket No. EL01-35-000

17. On February 6, 2001, Mirant Delta, LLC and Mirant Potrero, LLC (jointly Mirant) filed a complaint against the CAISO arguing that the December 15 Order preempted ABX1 5; thus, the Governor's selection of Board members was invalid. Mirant also argues that four of the five members selected by the Governor fail to meet the independence requirement of the December 15 Order, because two have close business ties to energy consumer interests and two are State employees. Therefore, Mirant requests that the Commission take the following actions: (1) replace the current Board with a truly independent one; (2) until a new Board is seated, require the current Board to obtain preapproval before taking any action pursuant to the CAISO tariff; and (3) declare all prior actions taken by the current Board as voidable and, thus, allow Mirant to withdraw from its participating generator agreement.[51]

1. Notice of Filing and Responses

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[49] Id. at 37.

[50] To the extent that this order discusses specific aspects of the independence requirement of Order No. 2000, we find that the CAISO has met those requirements for the purposes of qualifying for RTO status.

[51] Mirant's complaint also seeks enforcement of creditworthiness requirements and a direction to the CAISO to collect payment from defaulting Scheduling Coordinators. These issues have been addressed in California Independent System Operator Corporation, et al., 94 FERC ¶ 61,132 (2001); California Independent System Operator Corporation, et al., 95 FERC ¶ 61,024 (2001); and California Independent System Operator Corporation, et al., 98 FERC ¶ 61,335 (2002). Therefore, we dismiss this portion of Mirant's complaint as moot.

18. Notice of Mirant's complaint was published in the Federal Register on February 15, 2001, 66 Fed. Reg. 10,494 (2001), with comments, protests, and motions to intervene due on or before February 26, 2001.

19. The following parties filed timely unopposed motions to intervene and comments in support of the complaint: Duke Energy North America, LLC and Duke Energy Trading and Marketing, LLC (jointly Duke); Enron Power Marketing, Inc. (Enron); Morgan Stanley Capital Group Inc.; Puget Sound Energy, Inc.; Reliant Energy Power Generation, Inc. and Reliant Energy Services, Inc. (jointly Reliant); Western Power; and Williams Energy Marketing and Trading Company (Williams). Dynegy Power Marketing, Inc. (Dynegy) filed a motion to intervene in support of the complaint two days out of time.

20. These intervenors make the following arguments: the seating of the current Board is unlawful because the CAISO did not first file revised bylaws with the Commission to reflect the change in composition of its Board; the current Board is now effectively an instrumentality of the State, which is unjust because the Board has been acting in a manner preferential to State interests and detrimental to interstate markets; the current Board members lack adequate knowledge of the industry; now that DWR is making capacity and energy purchases, the State is itself a major participant in the market and therefore the Governor-appointed Board, consisting of two current State employees, is not independent of market participants, thus violating not only the December 15 Order but even California's own ABX1 5; and the Governor's issuance of E.O. D-23-01 indicates that California is attempting to extend its control of the CAISO beyond its appointment of the Board.

21. The CAISO filed a timely answer. The Oversight Board filed a timely unopposed motion to intervene in opposition to the complaint. The California Public Utilities Commission (CPUC) filed a notice of intervention and request for summary rejection or, in the alternative, a protest and request for hearing.

22. The CAISO and the CPUC argue that Mirant's challenge to the Board is not ripe because the CAISO has not filed amended bylaws to reflect the new governance structure. The CPUC also states that because the CAISO is a creature of California law, the State has the right to define the structure of its Board. The CAISO argues that Mirant has failed to provide any evidence that the actions of its new Board were illegal or unreasonable, and thus, these actions should not be voidable. The CAISO also argues that it would be an administrative impossibility to seek preapproval from the Commission on all actions its Board takes pursuant to the CAISO Tariff. Mirant filed an answer to the CAISO's answer.

23. The following parties filed timely unopposed motions to intervene raising no substantive issues: Calpine Corporation; Exelon Generation Company; Pacific Gas and Electric (PG&E); PPL EnergyPlus, LLC and PPL Montana, LLC; and the Sacramento Municipal Utility District. The Northern California Power Agency (Northern Power) filed a motion to intervene raising no substantive issues one day out of time.

2. Discussion of Procedural Matters

24. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2000), the CPUC's notice of intervention and the timely, unopposed motions to intervene of the parties listed above serve to make them parties to this proceeding. We find good cause to grant the late, unopposed motions to intervene of Northern Power and Dynegy, given the early stage of the proceeding, their interest in the proceeding, and the absence of any undue prejudice or delay. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2000), generally prohibits an answer to an answer, unless otherwise permitted by the decisional authority. We are not persuaded to allow Mirant's answer to the CAISO's answer and, accordingly, will reject it.

B. Docket No. EL00-95-005

25. On January 16, 2001, the CAISO, the Oversight Board, and the Western Power Trading Forum (Western Power) each filed a request for rehearing of the governance provisions of the December 15 Order.

26. The CAISO seeks rehearing and stay of the requirement that the Board surrender authority to Management by January 29, 2001. The CAISO argues that such a move could place a "cloud" over the CAISO's corporate authority and, therefore, disrupt arrangements with lenders.

27. The Oversight Board argues that the December 15 Order should be revised to allow the State to restructure the Board subject to subsequent Commission review. The Oversight Board argues that because the CAISO was expressly created by California law, California has the right to amend its restructuring law to change the governance structure of the CAISO without prior Commission approval.

28. Western Power argues that it is inappropriate to allow California any significant role in the selection of a new Board. Western Power states that the new Board must operate free from State influence in order to ensure that all market participants are treated fairly.

C. Docket No. EL00-95-012

29. Docket No. EL00-95-012 is the proceeding in which the Commission accepted comments on a market monitoring and mitigation plan for the California wholesale electric power market.[52] Coral Power, LLC and Enron, jointly, and Williams and the Electric Power Supply Association (EPSA), individually, filed comments arguing that the Board is illegitimate and requesting that the Commission take action to enforce the governance directives of its December 15 Order. These parties argue that the Board has become a partisan advocate for the State and must be replaced with an independent Board. They also argue that pursuant to judicial and Commission precedent all filings made by the CAISO should be rejected as legal nullities.

D. Docket Nos. ER01-1877-000, EL00-95-030, and EL00-98-029

30. On April 26, 2001, the CAISO filed amended bylaws that reflect the changes made to its Board.

E. Docket Nos. RT01-85-000, RT01-83-000, RT01-82-000, and RT01-92-000

31. As mentioned above, on June 1, 2001, the CAISO, SoCal Edison, and SDG&E, jointly, and PG&E, individually, filed RTO proposals in compliance with the April 26 Order.[53] The CAISO, SoCal Edison, and SDG&E assert that the existing Board meets the independence requirement of Order No. 2000 for five reasons.[54] First, these parties argue that ABX1 5, which created the new governance structure, bars members of the Board from being affiliated with market participants. Second, these parties argue that under State law and the CAISO bylaws, each member has a fiduciary responsibility to represent solely the interest of the CAISO. Third, these parties state that the CAISO's code of conduct requires all members to disclose their financial investments in any entity engaged in generation, transmission, marketing, or distribution of electricity. Fourth, these parties assert that the Board operates under an open meeting policy. Fifth, these parties state that members are monitored and subject to fines for misbehavior. The CAISO, SoCal Edison, and SDG&E do not address the concerns about the level of state control of the Board that petitioners have raised in the dockets discussed above, beyond simply asserting in a

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[52] See San Diego Gas & Electric Company, 96 FERC ¶ 61,254 (2001).

[53] We will address aspects of these filings other than governance in a separate order.

[54] See CAISO/SoCal Edsion/SDG&E June 1 filing at 19-21 and App. at 6-7.

footnote that the State is not a market participant notwithstanding DWR's involvement in the CAISO markets.[55]

32. PG&E acknowledges that questions have been raised about the independence of the Board and expresses concern that the Commission have adequate assurances that the CAISO is truly independent. PG&E also notes that the CAISO is faced with the challenge of operating under sometimes conflicting State and federal laws. Thus, PG&E urges the Commission to work with the state, as envisioned in the December 15 Order, to develop a consensus on how a new Board should be selected.[56]

1. Notice of Filing and Responses

33. Notice of the CAISO's filing was published in the Federal Register on May 17, 2001, 66 Fed. Reg. 27,497 (2001), with comments, protests, and motions to intervene due on or before May 25, 2001.

34. The Oversight Board filed a timely unopposed motion to intervene in support of the CAISO. The Oversight Board asserts that the current Board is independent of market participants and that, although the process for seating the Board differed from that contemplated in the December 15 Order, the result is consistent with that order. The Oversight Board further states that while the Commission has authority to determine whether the governance of the CAISO satisfies the independence criterion of Order No. 888, the Commission does not have authority to dictate the governance of a corporation organized under state law. Thus, according to the Oversight Board, if the Commission was to conclude that the new Board failed Commission independence standards, then its option would be to rescind the CAISO's tariff rather than disband the Board.

35. Dynegy, Enron, EPSA, Mirant, NRG Power Marketing, Inc., Reliant, Williams, and Western Power filed timely unopposed motions to intervene and protest. The protests reiterate the arguments made against the current Board in Docket Nos. EL01-35-000 and EL00-95-012. Timely unopposed motions to intervene raising no substantive issues were filed by the City and County of San Francisco (jointly San Francisco), Duke, and Northern Power.

36. The Transmission Agency of Northern California (TANC) filed timely comments in which it requests the establishment of a stakeholder advisory committee to ensure that

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[55] Id. App. at 7 n.21.

[56] See PG&E June 1 filing at 7-8.

stakeholders' views are communicated on a regular and timely basis to the Board. PG&E made a filing in which it indicated it would address the merits of the CAISO's proposal in its June 1 RTO filing.

2. Discussion of Procedural Matters

37. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2000), the timely, unopposed motions to intervene of the parties listed above serve to make them parties to this proceeding.[57]

E. Docket No. PA02-1-000

38. On January 25, 2002, the Commission issued a notice of the filing of the Audit Report and invited comments on the list of specific recommendations and findings contained in it.[58] The CAISO states that "it does not offer any comments on the future structure and function of its Governing Board, nor the timing for creating a new Board."[59] The CAISO maintains that these matters are for federal and state policymakers to decide. Nevertheless, the CAISO notes that the existing Board functioned effectively during the recent crisis and provided a stable platform from which Management could perform its day-to-day responsibilities. In addition, the CAISO states that, although independence is critical to establishing trust in an organization, the Audit Report fails to address how states can have a legitimate and meaningful role in governance in the future.

39. San Francisco supports the CAISO's comments that there is a need and legitimate interest for the State to be involved in the role of the Board. The CPUC states that, although the governance and independence issues are certainly important, they are secondary to the need to reform the CAISO's market structures to provide a clearer, narrower mission for the CAISO and a foundation for potential competitive markets going forward.

40. The Oversight Board believes that the current Board continues to serve its purpose and, in fact, functions as an appropriate governing body consistent with the requirements

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[57]These petitioners were already parties to this proceeding by virtue of having been granted intervention in other subdockets of Docket No. EL00-95-000.

[58]See 67 Fed. Reg. 4714 (2002). The CAISO was to file comments on or before February 15, 2002. All other comments were to be filed on or before March 1, 2002, and these commenters were allowed the opportunity to respond to the CAISO's comments.

[59]CAISO's Comments at 11.

of California law pertaining to nonprofit, public benefit corporations. In addition, the Oversight Board states that the present Board functions much more like a corporate board of directors than the prior stakeholder Board. The Oversight Board maintains that Management implements the policies without day-to-day micromanagement on the part of Board members, which often occurred under the prior stakeholder Board. The Oversight Board believes that the concern about independence is much more a matter of perception than reality and reflects the stakeholders' interest in eliminating any State role with respect to the CAISO.

41. The Oversight Board has no objection to the formation of a formal stakeholder committee to make recommendations and/or to educate the Board concerning how proposed CAISO policies might affect particular interests; however, the stakeholder committee must be a manageable size (unlike the prior stakeholder Board) and should focus on ensuring that the Board is well-informed of the potential consequences of its decisions.

42. Western Power, Powerex Corp. (Powerex), Independent Energy Producers Association (Independent Producers), EPSA, California Municipal Utilities Association (California Municipal), Mirant, TANC, Duke, and Reliant maintain that the resolution of the independence issues that plague the CAISO is a threshold matter that must be addressed before there can be any effective comprehensive market reforms in Western wholesale power markets. They argue that there is an inherent conflict between the CAISO being controlled by the State and the State's role as the dominant purchaser in the CAISO's markets. These commenters state that the CAISO can only reestablish leadership and trust with market participants through an independent Board. They maintain that the Commission should recognize that it will be very difficult, if not impossible, to build confidence in the CAISO's current market design, let alone prospective changes to that design, unless the CAISO has an independent Board and a formal stakeholder process that takes into account the concerns of all market participants. In addition, they state that the Commission's reluctance to address the independence of the CAISO has been surprising in light of the importance that the Commission places on independence in Order No. 2000 and in its orders addressing the merits of proposed RTOs.

43. These commenters support the Audit Report's recommendation to establish a new and independent Board, along with a formal stakeholder committee. According to them, the Audit Report supports the conclusion that the CAISO is in appearance and reality an instrument of the State and, as such, fails to satisfy the core principal underlying the formation of both ISOs and RTOs (i.e., independence from market participants).

44. Western Power, Independent Producers, Powerex state that at the same time that the CAISO acknowledges that the Board's independence is critical to establishing trust in the market, the CAISO also argues that it must maintain a role in the governance of the Board in order to protect the public interest. These commenters maintain that the CAISO's response reveals a fundamental misunderstanding of its legitimate role in the marketplace; instead of being an independent and nondiscriminatory operator of the interstate transmission system, the CAISO seeks, first and foremost, to represent the needs of California retail customers, as perceived by elected and appointed State officials.

45. Mirant states that once the independent Board is established, the process should not get "bogged down" in the politics of establishing a formal stakeholder committee; therefore, the absence of a formal stakeholder committee should not deter proceeding with market redesign once an independent Board is seated.

46. California Municipal has concerns about the proposal in the Audit Report that the CEO of the CAISO should be on the Board. Because of the number and complexity of technical issues that come before an independent Board, California Municipal states that the CEO will have an inordinate amount of influence over the Board's decisions, eroding the necessary separation between the Board and Management. California Municipal also notes that the CAISO's independence is not assured simply by installing a disinterested Board, because there is an inherent conflict in a market structure that places a procurement obligation on the independent grid operator and, thereby, puts the grid operator in a potentially adversarial position to market participants.

47. With regard to the stakeholder process, Dynegy states that it and other stakeholders have previously urged the Commission to hold a series of technical conferences (like the one held on September 24-25, 2001 in Folsom, California) where the Commission's staff can facilitate discussions and, thereby, help rehabilitate the stakeholder process.

1. Discussion of Procedural Matters

48. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2000), the timely, unopposed motions to intervene of the parties listed above serve to make them parties to this proceeding. We find good cause to grant the CPUC's late notice of intervention, given the early stage of the proceeding, their interest in the proceeding, and the absence of any undue prejudice or delay.

III. Discussion of the CAISO's Independence and Governance Issues

49. With regard to the composition of the current Board, the Commission concludes that the CAISO is not sufficiently independent to operate its interstate transmission facilities on a non-discriminatory basis. Furthermore, the Commission finds that the Board, as currently constituted, poses a barrier to the implementation of market redesigns that are necessary to rehabilitate the CAISO and Western markets. We also find that the current Board conflicts with our December 15 Order and Order Nos. 888 and 2000.

50. The primary problem with the existing Board is the extent to which it and, in turn, the CAISO are controlled by the State. Since the Governor signed ABX1 5 into law, all of the Board members have been selected by the Governor and serve at his pleasure, subject only to the confirmation of the Oversight Board.[60] Not only did the State fail to engage in a collaborative process with the Commission to establish an election process that would ensure the creation of a governance structure that is free from undue influence of any stakeholder, it established a decision-making process that is heavily influenced, if not completely dictated, by one stakeholder(i.e., the State).

51. State control of the CAISO is problematic for several reasons. In light of the redesign of the California energy markets that is required by prior Commission orders[61] and the Commission's efforts to create seamless wholesale energy markets in the West, we find that the Board's lack of independence presents a significant impediment to a well-functioning Western energy market. It will be difficult, if not impossible, for the current Western energy market to foster badly needed infrastructure development and maintain just and reasonable prices unless the CAISO has an independent Board and a formal stakeholder advisory process that takes into account the concerns of all market participants.

52. As discussed above, the GAO recently issued a report detailing how State control of the CAISO has resulted in the impression that the CAISO will not provide equal treatment to market participants.[62] In particular, the GAO Report states that developers in new generation in California are concerned that the DWR receives favorable treatment

[60]Under the current governance structure, if the Governor is dissatisfied with the Board, he can select a new Board, or new members, and direct the state Attorney General to file suit to compel the resignation of the current Board. Consequently, the Board is akin to an executive agency in the State government.

[61]See December 19 Order, 97 FERC ¶ 61,275.

[62]See GAO REP. NO. 02-427, at 30.

from the CAISO.[63] According to the GAO Report, "[t]his concern continues because the state has so much potential influence over the market, which raises the risk of entering the market for independent developers."[64] Furthermore, as the Audit Report states, market redesign may be "somewhat premature" without the independence issue being resolved,[65] because "[t]he current Board, in its caretaker role, does not appear inclined to address [] long term issues. Many of these issues will require in-depth work by stakeholder groups and then, careful, informed consideration by the [Board]."[66] With regard to one of the market redesign proposals (the bid cap), the Board blatantly acknowledged its disinterest in serving all market participants and addressing important long-term issues when, at its April 9, 2002 Board meeting, it was stated that the Board is not interested in the incentives that this particular proposal may have on new generation, demand response, or forward contracting because the Board believes that these are State issues.[67] In addition, the Audit Report suggests, with an independent Board and a formal stakeholder advisory process, changes to market design will likely be carried out in a more equitable manner, allowing all market participants to have input on the policies of the CAISO that affect them directly.[68]

53. Moreover, we find that even the perception that the authority who controls the interstate transmission grid is biased can be enough to prevent proper market forces from working, thus hindering market reliability and efficiency. In this case, the perception of bias is compounded by the fact that the State, through DWR's energy purchases, has become a market participant. Removing this conflict of interest from the Board is a critical step in solving significant Western energy market problems.

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[63]See id. at 30; see also infra notes 35-36 and accompanying text.

[64]GAO REP. NO. 02-427, at 30.

[65]Audit Report at 98-99.

[66]Id. at 30-31.

[67]See CAISO Market Surveillance Committee, MSC: Presentation for Training on New Market Design Elements, Market Design 2002 Comprehensive Design Proposal and October 1st, 2002 Design Elements - Action Items from Board Meeting of April 9, 2002 (April 11, 2002) at 21, at http://www.caiso.com/docs/2002/04/11/2002041110172024911.html .

[68]See Audit Report at 37, 99-100 (stating that there must be "an effective stakeholder process available to provide meaningful input into the market re-design").

54. In addition to the aforementioned operational problems caused by a State controlled Board, such a Board also raises jurisdictional issues. Specifically, the CAISO, as defined in section 201(e) of the FPA, is a public utility that provides transmission services, energy imbalance services, and ancillary services within the Commission's exclusive jurisdiction under the FPA. Under section 205 of the FPA, public utilities have the right and responsibility to determine what filings they will make voluntarily.[69] As a public utility, the CAISO should be independent of State control in deciding what filings to submit to the Commission. Furthermore, as a general matter under the FPA, public utilities are required to comply with the Commission's directives, not those of the State, regarding compliance with the FPA. Pervasive control over a public utility by the State conflicts with the Commission's exclusive jurisdiction over these matters and, in particular, the rates, terms, and conditions of transmission service in interstate commerce.

55. The Commission previously allowed the State, acting through the Oversight Board, a level of review authority over the CAISO but only with regard to matters that were not subject to exclusive federal jurisdiction. We allowed the Oversight Board confirmation power over only those members of the Board representing end users and public interest groups and review power over only those CAISO decisions concerning certain state-retail matters.[70] In doing so, we stated,

> [T]he Oversight Board may not review or dictate the rates, terms, and conditions of transmission in interstate commerce and may not require the ISO to make filings with the Commission, dictate the content of such filings, or limit the right of the ISO to make such filings at the Commission.[71]

With the Governor selecting the Board, the State has direct control of the CAISO with respect to all matters, including matters within our exclusive jurisdiction.

56. State control of the Board also conflicts with the independence requirements of Order Nos. 888 and 2000, as well as with our December 15 Order. The first ISO principle in Order No. 888 describes this requirement:

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[69] See, e.g., Commonwealth of Massachusetts, Dep't of Pub. Util. v. FERC, 729 F.2d 886 (1st Cir. 1984) (state cannot dictate a public utility's FERC rate filings).

[70] See California Electricity Oversight Board, 88 FERC ¶ 61,172, reh'g denied, 89 FERC ¶ 61,134 (1999), appeal dismissed sub. nom. Western Power Trading Forum v. FERC, 245 F.3d 798 (D.C. Cir. 2001).

[71] Id. at 61,577-578.

> The ISO's governance should be structured in a fair and non-discriminatory manner. The primary purpose of an ISO is to ensure fair and non-discriminatory access to transmission services and ancillary services for all users of the system. As such, an ISO should be independent of any individual market participant or any one class of participants (e.g., transmission owners or end-users).[72]

57. Similarly, Order No. 2000 states that the principle of independence is the "bedrock" on which an RTO must be built and requires RTO governance to be independent "in both reality and perception."[73] Control of the Board by one state threatens the CAISO's ability to treat in-state and out-of-state transmission users on a non-discriminatory basis, thus undermining the prospect of broader regional cooperation throughout the West. Moreover, now that the State, through DWR, is making substantial purchases of electric energy in the CAISO markets on behalf of the IOUs, it has become a market participant itself. Having a market participant who controls the Board is an untenable situation that must not continue as the West and California move towards a market-based redesign of the wholesale energy markets.

58. Freeing the CAISO from a non-independent, stakeholder Board was an essential component of the remedies we adopted in the November 1 Order to correct the serious dysfunctions in the California electricity markets. As we explained in our November 1 Order:

> The ISO is an institution that is central to the functioning of wholesale power markets in the West and, unless it is able to resolve matters in a timely manner and is independent of market participants, we cannot be assured that rates, terms or conditions of its jurisdictional services will be just, reasonable and not unduly discriminatory or preferential.[74]

59. In addition to the problems posed by State control of the Board, the current Board conflicts with our December 15 Order due to the presence of employees of two organizations that represent end-users. This violates our requirement that the Board consist of non-stakeholders. Without representation from any other stakeholder groups other than end-users, we find that the Board's composition is too one-sided to effectively

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[72]Order No. 888 at 31,730.

[73]Order No. 2000 at 31,061.

[74]November 1 Order, 93 FERC at 61,364.

balance the competing interests of all parties. Moreover, as explained elsewhere in this order and in the November 1 and December 15 Orders, we do not believe the Board should be a stakeholder organization.

60. In our November 1 Order, we also noted the need for appropriate expertise on behalf of candidates for the Board, stating that the new Board should include members with "experience in corporate leadership (at the director or board level) or professional expertise in either finance, accounting, engineering or utility law and regulation" and "experience in the operation and planning of transmission systems."[75] As the Audit Report details, the current Board members, for the most part, "have no prior utility experience."[76] Without this experience, we find that the current Board is ill-equipped to perform many critical functions and make informed decisions necessary to bring about the efficiency and reliability of the interstate transmission facilities in California.

61. For all of the reasons stated above, we direct that the current Board be replaced by an independent, non-stakeholder Board. Because we find that the existing CAISO governance structure, as reflected in the CAISO's proposed amendment to its bylaws, is unjust and unreasonable, unduly discriminatory, and preferential, we reject the amended bylaws the CAISO filed in Docket Nos. EL00-95-030 and EL00-98-029 as inconsistent with the December 15 Order and Order Nos. 888 and 2000.

62. To establish a just and reasonable CAISO governing structure, we direct that the current Board be replaced, by January 1, 2003,[77] with an expert, non-stakeholder Board,[78]

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[75]Id.

[76]Audit Report at 30.

[77]On that date the existing Board will transfer control of the CAISO to the new Board, which will be elected pursuant to the procedures outlined in this order.

[78]This governance design tracks, in large part, the board selection process approved by the Commission for RTO West. See Avista Corporation, et al., 95 FERC ¶ 61,114 (2001). This design is also consistent with the dominant governance models employed by other ISOs. See Order No. 2000 at 31,073. To the extent that the governance design in this order is inconsistent with the one that is ultimately adopted in the final rule on standard market design, the governance design of the CAISO will need to be further revised. See Electricity Market Design and Structure, Docket No. RM01-12-000 (2002). However, the process discussed in this order will serve to allow for the seating of an independent Board by January 1, 2003.

which is composed of nine voting members that are independent of market participants.[79] First, the CEO of the CAISO will be responsible for forming a committee from the CAISO's members (or stakeholders). Members of the committee will belong to one of six member-classes,[80] and each member class is entitled to elect six representatives to the Board Selection Committee (BSC); thus, the six member-classes will elect a 36-member BSC for purposes of voting on a slate of candidates for the Board.[81] By August 15, 2002, we direct the CAISO to file with the Commission a document that lists the six member-classes and the stakeholders within each class. In addition, by August 30, 2002, the CAISO must file a document with the Commission that lists the name and affiliation of each of the six representatives from the six member-classes.

63. A nationally recognized executive search firm,[82] which will be chosen by a majority vote of the BSC, will provide the BSC with a list of one or twocandidates for each open Board seat. We further direct the CAISO, by September 13, 2002, to file with

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[79]This order employs the definition of "market participant" from Order No. 2000. See Order No. 2000 at 31,061-62.

[80]A member and its affiliates may have a representative in only one stakeholder sector. For example, a vertically integrated utility that has a marketing affiliate would have to choose whether it will be represented in the transmission owner sector or the generator/marketer sector. For the purposes of the BSC, we define "member-classes" as not including either the State or its agencies.

[81]The following are the six member-classes: (1) generators and marketers; (2) transmission owners (e.g., vertically integrated utilities, merchant transmission owners); (3) transmission dependent utilities; (4) public interest groups (e.g., consumer advocates, environmental groups, and citizen participation); (5) alternative energy providers (e.g., distributed generation, demand response technologies, and renewable energy); and (6) end-users and retail energy providers (i.e., load serving entities that do not own transmission or distribution assets). The BSC will represent a balanced mix of interested stakeholders to ensure that no market participant or class of market participants will have control over the selection of the initial Board. Each of the member classes will determine the method for selecting its representatives to the BSC. The BSC members will have staggered terms of three years. The initial BSC will draw straws to divide into three initial groups, of which one group will serve a one-year term, one group will serve a two-year term, and one group will serve a three-year term.

[82]The search firm must not have an ongoing business relationship with the market participants in California. In addition, the search firm must have expertise in finding individuals with expertise in corporate leadership, finance, and engineering.

the Commission a document that contains the name of the executive search firm that the BSC selects. In selecting these candidates, the firm will generate a set of qualifications similar to those used to select the boards at the other ISOs and consistent with those outlined in the November 1 Order.[83] If the slate of candidates selected by the search firm only consists of nine nominees, those nine candidates will form the new Board. However, if the number of nominees exceeds nine candidates, each BSC representative has the right to cast votes equal to the number of open Board seats.[84] The BSC will declare the eight candidates with the largest number of votes to be the new Board.[85] The elected Board members will vote to designate one of the members as Chairman of the Board.

64. Each Board member will serve a three-year term (except the members of the initial Board, each of whom will draw straws to divide into three initial classes, with one class serving a one-year term, one class serving a two-year term, and one class serving a three-year term). Board members may be reelected to serve no more than two consecutive terms (for this purpose, an initial Board member who serves a partial term (i.e., one or two years) will be deemed to have served one full term). In addition, Board members may be removed for cause by a majority vote of the BSC. The same process that was used to select the initial Board will be used in the selection of subsequent Board members in the case of resignation, death, or removal for cause (with the exception that the Board that "sits" at that time will choose the search firm).

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[83]See November 1 Order, 93 FERC at 61,364 ("The board[] should include members with experience in corporate leadership (at the director or board level) or professional expertise in either finance, accounting, engineering or utility law and regulation. . . . The CAISO board should include members with experience in the operation and planning of transmission systems.") In addition, some members of the Board should have expertise in information technology. Furthermore, the candidates may not have served for at least the last two years prior to their tenure with the CAISO as directors, officers, or employees of any market participant or its affiliates. See, e.g., Midwest Independent Transmission System Operator, Inc., 97 FERC ¶ 61,326 at 62,504 (2001).

[84]A member shall not cast more than one vote for any one candidate and is not required to either cast all of its votes or vote with its class.

[85]Board seats are filled by a simple majority. Candidates with the highest vote totals are elected to open Board seats. Ties for the last open board seat/seats will have a runoff vote, subject to the same rules as the initial selection process.

65. When the first set of Board members' terms nears the point where they expire, a two stage process will be used for electing new Board members. First, existing Board members, whose terms are expiring, will indicate whether they wish to remain on the Board for a second term. If so, the BSC would vote on whether these existing board members will remain on the Board. Second, if there are any remaining vacancies, a search firm will be retained by the then-existing Board to provide candidates for the vacant seats on the Board, and the same process that was used for filling the initial Board will be used for filling these vacancies.

66. The Board will have the ultimate responsibility for the management of the CAISO. Board meetings will be open to the public (except for matters concerning personnel, security, and litigation), and agenda and briefing papers for any Board meeting must be made available for public review and comment for a specified time prior to an applicable meeting (except in cases of emergency). The Board will act by majority vote except where otherwise specified in the CAISO's bylaws.

67. The Board members will be subject to the following conflict of interest provisions: (1) they must not be affiliated with either a market participant in the CAISO or any affiliate of a market participant; (2) neither they nor their spouses or minor children can own or control securities of a market participant, and any such securities, if held or inherited, must be sold within six months of being elected to the Board; (3) they cannot be an officer, director, partner, or employee of either a market participant or its affiliates; and (4) they cannot have a material ongoing business or professional relationship with either a market participant or an affiliate.

68. The CEO of the CAISO will form a stakeholder advisory committee (SAC) by January 1, 2003. All stakeholders of the CAISO will have the right to join the SAC (with the exception of the State and its agencies), which will not have a fixed size, and will provide advice to the Board, promote input on the Board's decisions, and serve as a focal point for dissemination of information.[86] The SAC members will neither be elected nor divided into classes. The SAC will serve in a purely advisory function and will not be entitled to vote on any issues and may form additional non-voting advisory committees as it deems necessary. The SAC will also be able to provide the new Board with stakeholder input on various issues, such as market redesign. Thus, the SAC will allow stakeholders the opportunity to advise the new Board of their views on pending issues in a timely

[86]We believe that stakeholders often possess the detailed knowledge that is beneficial to a Board in making educated decisions. Also, consultation with stakeholders can result in more consensus decisions and less divisive disputes regarding the CAISO's rules and actions.

manner. In addition, we direct the CEO of the CAISO to form a separate advisory committee, by January 1, 2003, that will consist of only the Oversight Board. This advisory committee will serve as the State's and its agencies' representative in advising the Board.

69. Given that the CAISO has filed amended bylaws, we need not address the arguments of the CAISO and the CPUC, which were made prior to the filing of these amendments, that challenges to the composition of the Board are not ripe until the amended bylaws are filed. We dismiss as moot the Oversight Board's request for rehearing of the December 15 Order to allow the State to restructure the Board subject to subsequent Commission review. We also dismiss as moot Western Power's request for rehearing of the December 15 Order to deny the State any significant role in the selection of a new Board. To the extent that either the CAISO's articles of incorporation or bylaws are inconsistent with the governance proposal put forward here, the CAISO's articles of incorporation and/or bylaws are found to be unjust, unreasonable, unduly discriminatory, and preferential; therefore, they must be revised to reflect the changes discussed in the body of this order. We direct the CAISO to file, by September 30, 2002, revised bylaws that reflect the governance structure and board selection process that are outlined in our order.

70. We reject the Oversight Board's assertion that, in the event that we find the CAISO's proposed governance structure unacceptable, our authority is limited to rescinding the CAISO's tariff. FPA section 206 provides the Commission with authority to fix a just and reasonable rate (or rule or practice affecting a rate) whenever it determines, after hearing, that an existing rate (or rule or practice affecting a rate) is unjust, unreasonable, unduly discriminatory, or preferential.[87] The CAISO's bylaws and the governance provisions contained in them affect the rates, terms, and conditions of jurisdictional services and are on file with the Commission and, thus, are subject to our review under section 206.

71. With regard to the CAISO's argument that any interim absence of the Board would place a "cloud" over the CAISO's corporate authority, we find that the factual predicate on which this argument rests is moot. In this order, we are not requiring that the Board "step down" for an interim period until a new Board is installed. Accordingly, the concerns that lenders and others might have about who has the authority to bind the CAISO are no longer relevant.

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[87]See 16 U.S.C. § 824e(a) (1994).

72. With regard to the requests that we reject prior CAISO filings or void prior CAISO actions as per se invalid, we conclude that such steps would be unduly disruptive and are unnecessary. All filings made by the CAISO during the period in which the current Board was in control have been or are being reviewed by the Commission on a case-by-case basis. We are similarly reviewing all complaints about specific CAISO action taken during that period on a case-by-case basis. These reviews provide adequate protection against any potential problems with the CAISO's conduct during that period.

The Commission orders:

(A) Northern Power's and Dynegy's out-of-time requests for intervention in Docket No. EL01-35-000 are granted.

(B) CPUC's out-of-time notice of intervention in Docket No. PA02-1-000 is granted.

(C) The Oversight Board's request for rehearing of the governance provisions of the December 15 Order is dismissed as moot.

(D) Western Power's request for rehearing of the governance provisions of the December 15 Order is dismissed as moot.

(E) Mirant's request for enforcement of the CAISO tariff creditworthiness requirements is dismissed as moot.

(F) Mirant's request concerning CAISO governance is granted in part and denied in part, as discussed in the body of this order.

(G) The motions in Docket No. EL00-95-012 are granted in part and denied in part, as discussed in the body of this order.

(H) The CAISO is directed to form a Board Selection Committee that will elect an expert, non-stakeholder Board composed of nine voting members that are independent of market participants that will replace the current Board by January 1, 2003, as discussed in the body of this order.

(I) The CAISO's request for rehearing and partial stay of the December 15 Order is denied, as discussed in the body of this order.

(J) The amended bylaws filed by the CAISO in Docket Nos. EL00-95-030 and EL00-98-029 are rejected, as discussed in the body of this order.

(K) The CAISO must file, by August 15, 2002, a document that lists the six member-classes and the stakeholders within each class, as discussed in the body of this order.

(L) The CAISO must file, by August 30, 2002, a list of the name and affiliation of each of the six representatives from each member-class that will serve as the Board Selection Committee, as discussed in the body of this order.

(M) The CAISO must file, by September 13, 2002, a document that contains the name of the executive search firm that the BSC selects, as discussed in the body of this order.

(N) The CAISO must file, by September 30, 2002, revised bylaws that are consistent with the changes discussed in the body of this order.

(O) The CEO of the CAISO is directed, by January 1, 2003, to form a stakeholder advisory committee, as discussed in the body of this order.

(P) The CEO of the CAISO is directed, by January 1, 2003, to form an advisory committee that will consist of the Oversight Board, as discussed in the body of this order.

By the Commission.

(S E A L)

Linwood A. Watson, Jr.,
Deputy Secretary.