

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

San Diego Gas & Electric Company,)	
Complainant,)	
)	
v.)	Docket Nos. EL00-95-031
)	EL00-95-034
Sellers of Energy and Ancillary Services)	
Into Markets Operated by the California)	
Independent System Operator and the)	
California Power Exchange, Respondents.)	
Investigation of Practices of the California)	
Independent System Operator and the)	Docket No. EL00-98-033
California Power Exchange)	

**MOTION FOR CLARIFICATION AND
REQUEST FOR REHEARING OF THE
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

The California Independent System Operator Corporation (“ISO”)¹ respectfully submits this Motion for Clarification and Request for Rehearing of the Commission’s “Order Providing Clarification and Preliminary Guidance on Implementation of Mitigation and Monitoring Plan for the California Wholesale Electric Markets” issued on May 25, 2001, in the above-captioned dockets, 95 FERC ¶ 61,275 (“May 25 Order”), pursuant to section 313(a) of the Federal Power Act, 16 U.S.C. § 825l(a) (1994), and sections 212 and 713 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. §§ 385.212 and 385.713 (2000).

¹ Capitalized terms not otherwise defined herein are used in the sense given in the Master Definitions Supplement, Appendix A to the ISO Tariff.

The ISO applauds the Commission for the clarification provided on some issues in the May 25 Order – for example, the confirmation that the ISO may use standing “price taker” bids for those generators that are subject to the Commission’s “must-offer” requirement but have not provided the ISO with the data necessary to calculate the “Proxy Price” for those generators. The ISO also notes that certain directives of the May 25 Order on other issues, such as the natural gas price indices to be used in calculating the Proxy Price, have been superseded by subsequent Commission orders.

The ISO, however, does seek clarification or rehearing of the specific price mitigation mechanism for the ISO’s Ancillary Service markets established by the May 25 Order. The ISO also urges the Commission to grant rehearing on the May 25 Order’s mandate that the ISO must “ensure the presence of a creditworthy buyer for all transactions made with all generators who offer power in compliance with the must-offer requirement.”²

I. BACKGROUND

As part of the ongoing proceedings and investigations in the above-captioned dockets, the Commission has concluded that the market structures and rules for wholesale sales of electric energy in California are “seriously flawed,” and, in conjunction with the imbalance of supply and demand in California, have created the ability of suppliers of electricity in those markets to

² May 25 Order, 95 FERC at 61,972.

exercise market power and to charge unjust and unreasonable rates for energy.³

On April 26, 2001, the Commission issued an order⁴ adopting a prospective market monitoring and mitigation plan for real-time wholesale energy markets in California intended to replace the Commission's \$150/MWh "breakpoint mechanism" that had been in effect since January 1, 2001 pursuant to the December 15 Order. The market monitoring and mitigation plan adopted in the April 26 Order, which went into effect on May 29, 2001, included the following elements:

- provision of the ISO with greater authority to coordinate and control planned generator outages;
- the establishment of a requirement that all Participating Generators, as well as all other generators located in California -- including non-public utility generators but excepting hydroelectric units-- that voluntarily make sales through the ISO's markets or use the ISO Controlled Grid, offer all of their available capacity in the ISO's real-time Energy market during all hours; and
- the establishment of a price mitigation mechanism for all sellers bidding into the ISO's real-time Energy market during periods of reserve deficiency (defined as a Stage 1 Emergency or greater) under which the market clearing price will be set at a "proxy price," reflecting the highest marginal cost of all of the units dispatched, as calculated by the ISO, pursuant to a formula set forth by the Commission. Sellers were permitted to submit bids greater than this proxy price, subject to refund and justification.

The April 26 Order required the ISO to submit Tariff revisions to comply with these aspects of the Order within fifteen days. On May 11, the ISO

³ See, e.g., *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator Corporation and the California Power Exchange, et al.*, 93 FERC ¶ 61,294 at 61,998-99 (2000), *reh'g pending* ("December 15 Order").

⁴ *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator Corporation and the California Power Exchange, et al.*, 95 FERC ¶ 61,115 (2001) ("April 26 Order")

submitted proposed revisions to the ISO Tariff in compliance with the Commission's directives. In this compliance filing, the ISO noted that the April 26 Order only specifically provided for price mitigation in the ISO's real-time Imbalance Energy market and did not discuss price mitigation in the ISO's Ancillary Service and Congestion Management markets. The ISO's compliance filing included Tariff revisions to eliminate existing price mitigation measures in those markets to the extent the April 26 Order could be read as eliminating such mitigation.

On May 18 and May 25, 2001, the ISO filed Status Reports in the above-captioned proceeding to update the Commission on the ISO's progress towards implementation of the April 26 Order. In the May 18 Status Report, the ISO requested guidance on various implementation issues. The ISO also reiterated that the April 26 Order could be read to eliminate price mitigation in the ISO's Ancillary Service and Congestion Management markets and stated that "in light of the potentially astronomical impact on California consumers from the exercise of market power in the uncapped Ancillary Service markets and on Adjustment Bids, the ISO requests that the Commission notify the ISO immediately if its interpretation of the April 26 Order is in error." May 18 Status Report at 16.

On May 25, 2001, the Commission issued an order providing clarification and guidance on the implementation of its April 26 Order. The scope of the May 25 Order was limited to guidance concerning:

- price mitigation in the ISO's spot markets other than Imbalance Energy;
- credit support requirements for Energy made available pursuant to the April 26 Order's "must-offer" requirement;

- treatment of generators that did not supply heat and emission rates as required in the April 26 Order; and
- the natural gas price indices to be used in calculating the Proxy Price.

The Commission stated that the April 26 Order did not eliminate all price mitigation in the ISO's Ancillary Service markets. Instead, the Commission clarified that, for the ISO's Ancillary Services markets, the ISO must replace the existing \$150/MW breakpoint mechanism with the methodology adopted in the April 26 Order. Specifically, the Commission directed that:

With respect to calculating the market clearing price for Ancillary Services, we direct the ISO to use each relevant average hourly mitigated Imbalance Energy price. If the Ancillary Services markets clear below the average hourly mitigated Imbalance Energy price for that hour, then the ISO will pay the Ancillary Services clearing price for that market. If the Ancillary Services markets clear above the average hourly mitigated Imbalance Energy price, then the ISO will use that price to clear the market and will pay as-bid for all Ancillary Services that are needed above the mitigated price. Bids accepted above the mitigated price will be subject to refund and justification.

May 25 Order, 95 FERC at 61,971-72. The Commission also clarified that the April 26 Order did not replace the ISO's current methodology for mitigating Adjustment Bid prices. *Id.* at 61,971.

In the May 25 Order, the Commission also granted a motion filed by the Cities of Anaheim, Azusa, Banning, Colton, and Riverside California (collectively "Southern Cities") requesting that the Commission clarify that the April 26 Order's requirement that sellers offer all available power to the ISO in real-time applied only if sellers are assured of a credit support for all Energy dispatched pursuant to the must-offer requirement. The Commission stated that it expects the ISO "to

ensure the presence of a creditworthy buyer for all transactions made with generators who offer power in compliance with the must-offer requirement in the [April 26] Mitigation Plan.” *Id.* at 61,972.

On June 19, 2001, the Commission issued its “Order on Rehearing of Monitoring and Mitigation Plan for the California Wholesale Electric Markets, Establishing West-Wide Mitigation, and Establishing Settlement Conference” in the above-captioned proceeding. 95 FERC ¶ 61,418 (“June 19 Order”). The June 19 Order addressed a number of issues related to the May 25 Order. For example, the Commission confirmed that the April 26 Order (as clarified by the May 25 Order) established “new price mitigation for sales in the California Independent System Operator’s (ISO) ancillary services and imbalance energy markets (spot markets).” June 19 Order, 95 FERC ¶ 61,418, slip op. at 2. The Commission further held that:

For spot market sales, both in the WSCC and in California, in all non- reserve deficiency hours (*i.e.*, when reserve levels in the ISO exceed 7%), we will adapt the use of these market clearing prices. Eighty-five percent (85%) of the highest ISO hourly market clearing price established during the hours when the last Stage 1 (not Stage 2 or 3) was in effect will, absent justification, serve as the maximum price for the subsequent period.

Id., slip op. at 7. The Commission also modified its directives in the April 26 and May 25 Orders as to the natural gas price indices to be used in calculating the Proxy Price.

II. SPECIFICATIONS OF ERROR

In compliance with Rule 713(c)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.7(c)(1), the ISO respectfully submits that the Commission erred in the following respects in the May 25 Order:

A. Price Mitigation Mechanism for Ancillary Service Markets

The Commission erred in concluding that the appropriate price mitigation mechanism for the ISO's Ancillary Service markets is a limitation of the market clearing price in those markets to the "relevant average hourly mitigated Imbalance Energy price" with an opportunity for suppliers to bid above that level and be paid as-bid, subject to refund and cost justification.

B. Ancillary Service Price Mitigation In All Hours

The Commission erred in failing to mitigate the potential for unjust and unreasonable prices in the ISO's Ancillary Service markets in all hours.

C. Credit Support For Must-Offer Transactions

The Commission erred in concluding that the ISO is obligated under the ISO Tariff "to ensure the presence of a creditworthy buyer for all transactions made with generators who offer power in compliance with the must-offer requirement" and in concluding that the Commission's prior orders could impose such a requirement upon the ISO.

D. Consistency with the Ten Percent Credit Risk Adder

The Commission's directive that the ISO must "ensure the presence of a creditworthy buyer for all transactions made with generators who offer power in compliance with the must-offer requirement" is inconsistent with the requirement in the June 19 Order that the "ISO is required to add 10 percent to the market clearing price paid to generators for all prospective sales in its markets to reflect credit uncertainty."

III. ARGUMENT

A. The Price Mitigation Mechanism for the ISO Ancillary Service Markets Should Be Modified.

The ISO strongly supports the Commission's recognition in the May 25 Order that the potential for unjust and unreasonable prices in the ISO's Ancillary Service markets requires that prices in those markets be mitigated. As the Commission is well aware, Ancillary Services costs can be significant in California, and are a causative factor of higher costs in the ISO's real-time Imbalance Energy market,⁵ which is why some form of price mitigation in the ISO's Ancillary Services markets have been in place since the summer of 1998.

The specific Ancillary Service price mitigation mechanism adopted in the May 25 Order – use of the “relevant average hourly mitigated Imbalance Energy price” as a limit on the Ancillary Services market clearing price, with the ability of suppliers to be paid as-bid above that limit subject to cost-justification and refund – is flawed in three important respects, however. First, the May 25 Order improperly suggests that a supplier of Ancillary Services can or should be able to justify Ancillary Service bids in excess of the “average hourly mitigated Imbalance Energy price.” Second, by relying upon the “average hourly mitigated Imbalance Energy price” as the benchmark for Ancillary Service price mitigation, the mechanism adopted in the May 25 Order only provides the potential for *ex post* mitigation of prices in the Ancillary Service markets. Third, the ISO is concerned about the manner in which the Commission apparently sought to

⁵ See, e.g., *Report on Redesign of Markets for Ancillary Services and Real-Time Energy*, prepared by the ISO's Market Surveillance Committee, filed in Docket Nos. ER98-2843-007 *et al.* on March 25, 1999, at 3-14.

adopt an “opportunity cost” approach to mitigating Ancillary Service prices by using the “average hourly mitigated Imbalance Energy price.” Assuming, for the sake of argument, that the Commission used this price to reflect the opportunity cost of holding unloaded capacity instead of providing energy, the ISO believes that true opportunity cost of this capacity is the profit – *i.e.*, the difference between sales price and production cost – a seller could make from selling Energy, not just the Market Clearing Price for that Energy.

As the ISO explained in its request for rehearing of the April 26 Order, there can be no cost justification for bids in the Ancillary Services capacity markets above the applicable limit of price mitigation in the ISO’s real-time Imbalance Energy market, whether that limit is the \$150 cap in effect until May 29 or the current mitigated Market Clearing Price based on the marginal costs of producing Energy. This is because bids into the ISO’s Ancillary Service markets consist of two parts: a capacity bid and an Energy bid. The latter component *already* includes the opportunity for bidders to attempt to justify their Energy bids above the applicable mitigated Market Clearing Price by identifying reasonable costs associated with providing the service. There is no need to provide bidders the opportunity also to “cost justify” the capacity component of their Ancillary Services bids.

Bidders in the Spinning, Non-Spinning, and Replacement Reserve markets submit capacity bids indicating the price at which they are willing to make capacity available to satisfy Ancillary Service requirements *in addition to* Energy bids to cover their costs of producing Energy from that capacity. If the

bid is selected for the Ancillary Service, but the Energy associated with this capacity is not dispatched, then the bidder only receives the capacity payment. On the other hand, when the ISO dispatches Energy from the capacity selected for one of these Ancillary Services, the bidder is assured of payment in accordance with its Energy bid. The Energy component of Ancillary Services bids is subject to the same price mitigation as all other forms of Imbalance Energy, with the same opportunity to justify bids at whatever level is necessary to ensure recovery of the supplier's marginal costs. Since the payments such bidders receive for their Energy bids are no longer subject to any form of hard price cap, bidders can recover all reasonable costs associated with providing Ancillary Services through their Energy bids. Thus, any attempt to "cost justify" Ancillary Service capacity bids based on a unit's costs only would provide the opportunity for double-recovery of those costs.

In addition, under the price mitigation regime adopted in the April 26 Order, as modified by the June 19 Order, the "average hourly mitigated Imbalance Energy price" during reserve deficiency hours (*i.e.*, hours in which the ISO has declared a System Emergency) will not be determined until after the fact. That price will be based on the Proxy Price of the marginal gas-fired unit dispatched in that hour. The ISO's Ancillary Service markets, however, operate on a Day-Ahead and Hour-Ahead basis. Therefore, bidders into those markets for reserve deficiency hours will not know the applicable limit before they bid into the ISO's Ancillary Service markets. Thus the Commission has established a price mitigation regime for Ancillary Services that is inconsistent with the

Commission's conclusion that, "[t]o the extent possible, our price mitigation should have clear rules, *should set prices before they are charged* and should not subject prices to change or adjustment after financial settlement of the day's transactions." June 19 Order, 95 FERC ¶ 61,418, slip op. at 6 (emphasis added).

As the ISO explained in its request for rehearing of the April 26 Order, the cost of providing Ancillary Services, assuming a zero probability of being dispatched for Energy, is the opportunity cost associated with not selling Energy. Thus, the ISO believes that the price mitigation mechanism applicable to the sale of Ancillary Services capacity should reflect the difference between the resource's cost of producing Energy and the price of Energy. For example, when the real-time Market Clearing Price is \$100/MWh, a unit with a production cost of \$40/MWh would have an opportunity cost of \$60/MWh. Since no unit has a production cost of \$0/MWh, this opportunity cost will always be less than the applicable real-time Energy price that unit would earn. Moreover, resources providing Ancillary Services capacity also receive Energy payments – and therefore have no opportunity cost - to the extent Energy from their awarded Ancillary Service capacity is actually dispatched.⁶

The ISO proposed this approach in its Market Stabilization Plan as part of a proposed Day-Ahead unit commitment market. Under the ISO's Market Stabilization Plan proposal, Ancillary Services and Day-Ahead Energy would be procured simultaneously and Ancillary Service capacity prices would reflect the

⁶ This is not the case for Replacement Reserve capacity, where pursuant to the Commission's December 15 Order, dispatched Replacement Reserve capacity receives only the Energy price and not a capacity payment.

maximum differential between real-time Energy prices and the actual production costs of generation. Adopting this approach under the current market structure established by the Commission for the California wholesale electricity markets is not possible because the ISO does not currently have a Day-Ahead Energy market from which to calculate, *ex-ante*, a unit's opportunity cost for providing Ancillary Services.

As an alternative, the ISO believe that there is an approach to price mitigation in the ISO's Ancillary Service markets based on the Commission's current price mitigation plan that would avoid the problems of an *ex post* price mitigation mechanism and eliminate the potential for inappropriate attempts to over-recover the costs associated with the provision of Ancillary Services. In the June 19 Order, the Commission established a limit on the market clearing prices during non-reserve deficiency hours of "Eighty-five percent (85%) of the highest ISO hourly market clearing price established during the hours when the last Stage 1 (not Stage 2 or 3) was in effect." June 19 Order, June 19 Order, 95 FERC ¶ 61,418, slip op. at 7. The ISO recommends that prices in the Ancillary Service markets in all hours be limited to 85% of the highest hourly Market Clearing Price during the most recent Stage 1 period. In other words, the ISO recommends the Commission extend the Ancillary Service price mitigation provided in the June 19, 2001 Order for non-reserve deficiency hours to all hours. For the reasons, described above, the ISO also recommends that the Commission confirm that there is no basis on which suppliers of Ancillary Services can justify Ancillary Service capacity bids above 85% of the highest

hourly Market Clearing Price during the most recent Stage 1 period. This approach would avoid the need for *ex post* adjustments to Ancillary Service prices while at the same time ensuring that Ancillary Service prices remain within a zone of reasonableness. The ISO also believes that this approach more closely replicates an “opportunity cost” approach to Ancillary Services price mitigation. Moreover, unlike a fixed hard cap, this approach reasonably allows for the limitation on Ancillary Service capacity prices to adjust to changes in market conditions.

The ISO notes that it has not had an opportunity to fully assess the impact of the modified market structure established by the April 26 and June 19 Orders on the ISO’s Ancillary Service markets. Although the ISO believes that, with the June 19 Order, the Commission has made tremendous strides towards ensuring just and reasonable rates in the ISO’s markets, there is still the possibility that the modified market structure may permit prohibited anti-competitive bidding in the Ancillary Service markets. As the Commission has directed, the ISO will monitor those markets and, if the potential for anti-competitive bidding is detected, will propose measures to address such behavior.

B. Ancillary Service Price Mitigation Should Be Applicable In All Hours Every Day.

The ISO requests that the Commission clarify that price mitigation in the ISO’s Ancillary Service markets is and has been applicable in all hours. The May 25 Order did not directly address this issue. The previous Ancillary Service price mitigation mechanism – the \$150/MW breakpoint mechanism – applied in all hours. As of the effective date of the June 19 Order – which extended price

mitigation in all California and Western Systems Coordinating Council spot markets to all hours – there is no doubt that price mitigation in the ISO’s Ancillary Service markets will be applicable in all hours. The ISO strongly supports this recognition that price mitigation is needed in all hours. The ISO believes that the Commission should clarify that the May 25 Order also established Ancillary Service price mitigation in all hours. Anything else would be inconsistent with the Commission’s finding that mitigation of Energy and Ancillary Service price during all hours is necessary and appropriate in order to “protect customers.” June 19 Order, 95 FERC ¶ 61,418, slip op. at 5. If the Commission does not provide such clarification, the ISO believes that the Commission’s subsequent findings concerning the need for price mitigation in the ISO spot markets in all hours require that the Commission grant rehearing on this issue and hold that the Ancillary Service price mitigation established by the May 25 Order applies in all hours.

C. There Is No Justification For Requiring the ISO To Ensure Credit Support For All Energy Dispatched Pursuant to the Must-Offer Requirement.

The May 25 Order improperly grants the Southern Cities motion for clarification that the ISO must ensure that a creditworthy purchaser or counterparty will support all transactions made with all generators pursuant to the April 26 Order’s must-offer requirement.

In granting this motion, the Commission states that, “[w]e have previously ruled that generators are entitled to assurances of payment for all energy they provide through the ISO and have directed the ISO to ensure the presence of a

creditworthy counterparty for all power that any third-party suppliers provide to PG&E and SoCal Edison,” citing the Commission’s April 6, 2001, “Order Granting Motion” in Docket Nos. ER01-889 *et al.*⁷

In the ISO’s May 7, 2001, Request for Rehearing of the April 6 Order (the “May 7 Rehearing Request”), the ISO already has detailed why the April 6 Order is contrary to applicable law – including the requirements of the Federal Power Act – and detailed why requiring the ISO to obtain a guarantee that a creditworthy purchaser or counterparty will pay for ISO Market transactions and real-time dispatch instructions issued to maintain the balance of supply and demand on the ISO Controlled Grid, especially during System Emergencies, improperly would place the private interests of suppliers of electricity above the public interest in ensuring that consumers receive reliable electric service. Rather than repeating the substance of its objections to the legal bases for the April 6 Order, the ISO incorporates by reference the substance of the May 7 Rehearing Request, which is provided as Attachment 1 to this filing.

The ISO recognizes that, to date, the Commission has not seen fit to modify its “creditworthiness” orders.⁸ Moreover, in the June 13 Order, the Commission stated in clear and unambiguous language that although the ISO must comply with its “creditworthiness orders, “[t]he ISO tariff does not allow suppliers to ignore emergency dispatch orders.” 95 FERC ¶ 61,391, slip op. at 8. Nonetheless, the ISO believes that now is the appropriate time for the

⁷ *California Independent System Operator Corp. et al.*, 95 FERC ¶ 61,026 (2001) (“April 6 Order”).

⁸ The Commission denied the May 7 Request for Rehearing in an order issued on June 13, 2001. *California Independent System Operator Corp.*, 95 FERC ¶ 61,391 (“June 13 Order”).

Commission to modify those orders. In the April 26 and June 19 Orders, the Commission has held that all available generation in California must be offered into the ISO's real-time market in order "to prevent withholding and thereby to ensure that the ISO will be able to call upon available resources in the real-time market to the extent that energy is needed." June 19 Order, 95 FERC ¶ 61,418, slip op. at 12. The May 25 Order indicates that the ISO must ensure that a creditworthy party will back all transactions made with generators that offer power in compliance with the must-offer requirement. This requirement could undercut the very purpose for which the Commission mandated the must-offer requirement. In the event that the ISO is unable to obtain a creditworthy counterparty for any such transaction, the ISO may have no choice but to curtail service to California consumers, despite the availability of generation to serve those consumers.

D. Requiring the ISO To Ensure Credit Support For All Energy Dispatched Pursuant to the Must-Offer Requirement Is Inconsistent With the Ten Percent Adder For Credit Risk.

Notwithstanding the concerns stated above for the requirement of a creditworthy buyer for must-offer transactions, the ISO believes that the requirement established by the May 25 Order is inconsistent with the requirement established by the June 19 Order that the ISO is to "add 10 percent to the market clearing price paid to generators for all prospective sales in its markets to reflect credit uncertainty."⁹ The rationale for the credit support aspects of the May 25 Order is that the ISO must ensure that suppliers have the equivalent of the

⁹ June 19 Order, 95 FERC ¶ 61,418, slip op. at 35.

assurances of payment that they would have but for the current crisis and financial distress of the California investor-owned utilities. The ten percent adder appears to have the same rationale. The ISO respectfully submits that the combination of the May 25 Order and the June 19 Order inappropriately compensates sellers through the ISO's markets for a credit risk they are not required to assume. Either the ISO is required to take additional steps to ensure that the credit risks in its markets are the equivalent of a normally functioning market, as the May 25 Order requires, or the exceptional credit risks in the ISO's markets support the payment of the ten percent adder mandated by the June 19 Order. There is no basis for retaining both requirements. Doing so would permit suppliers to enjoy the additional profits afforded by the 10 percent adder, while at the same time protecting them from the very credit risk that the Commission cites as justification for that adder.

At least two Commissioners concurring with the June 19 Order acknowledge this disparity: Commissioner Breathitt, in her concurring opinion, notes that "the imposition of such a credit surcharge" is inconsistent with the implementation of "the Commission's creditworthiness standards." June 19 Order, 95 FERC ¶ 61,418, Breathitt conc., slip op. at 1.¹⁰ Similarly, Commissioner Massey, in his concurring opinion states that "I am concerned that

¹⁰ Commissioner Breathitt also "call[s] upon the ISO immediately to implement our orders regarding creditworthiness." *Id.* at 1-2. As the ISO has indicated in numerous filings with the Commission, the ISO has complied with the Commission's orders relating to creditworthiness, notwithstanding the ISO's objections as to the legal basis for those orders. See May 25, 2001, Answer of the California Independent System Operator Corporation to Motion for Clarification of the Cities of Anaheim, Azusa, Banning, Colton and Riverside, California, filed in Docket Nos. EL00-95-000, *et al.* at 4-5; June 7, 2001, Answer of the California Independent System Operator Corporation in Opposition to Expedited Motion for Enforcement Action, filed in Docket Nos. ER01-889-003, *et al.* at 4.

the adder may diminish the ISO's enforcement of those [creditworthiness] requirements." June 19 Order, 95 FERC ¶ 61,418, Massey conc., slip op. at 2.

The ISO will address the justification for the 10 percent credit adder in its future pleadings concerning the June 19 Order. However, to the extent that the Commission retains this aspect of the June 19 Order, the Commission cannot also require the ISO to ensure the presence of a creditworthy purchaser or counterparty for all transactions made with all generators who offer power pursuant to the must-offer requirement. The Commission must modify this aspect of the May 25 Order to avoid excess payments to suppliers.

Finally, the ISO notes that the Southern Cities motion for clarification ("Southern Cities Motion") was premised on the argument that, in the absence of additional assurances of payment for Energy made available pursuant to the April 26 Order's must-offer requirement, "requiring publicly-owned systems to offer energy to the ISO will violate applicable restrictions against gifts of public funds" established by the California State Constitution. Southern Cities Motion at 2. In its May 25, 2001, Answer to the Southern Cities Motion ("May 25 Answer"), the ISO explained why offering and providing Energy in the ISO's real-time Imbalance Energy market would not result in such prohibited "gifts of public funds" even without additional assurances of payment.¹¹ In brief, the ISO explained that, under applicable California state law, public entities like Southern Cities would receive adequate consideration for such Energy even without additional assurances of payment and further that the constitutional prohibitions

¹¹ The Commission issued the May 25 Order acting on the Southern Cities Motion on the same date that it established for filing responses to that Motion.

in question are not applicable if expenditures of public funds or property are made for a public purpose. While the May 25 Order does not indicate that Southern Cities' constitutional arguments were a basis for granting the Southern Cities Motion, to the extent the credit support rulings in the May 25 Order are based on those arguments, the ISO urges the Commission to take into account the discussion in its May 25 Answer, which is incorporated by reference and provided as Attachment 2 to this filing.

IV. CONCLUSION

Wherefore, for the reasons discussed above, the ISO respectfully requests that the Commission grant rehearing and clarification of the May 25 Order in accordance with the discussion above:

Respectfully submitted,

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Dated: June 25, 2001

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in the above-captioned dockets.

Dated at Washington, DC, on this 25th day of June, 2001.

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