121 FERC ¶ 61,193
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Marc Spitzer, Philip D. Moeller,
and Jon Wellinghoff.

California Independent System Operator Corporation Docket Nos. ER04-835-006

Pacific Gas and Electric Company

EL04-103-001
v. (consolidated)

California Independent System Operator Corporation

ORDER ON REHEARING

(Issued November 20, 2007)

1. In this order, we deny rehearing in part and grant rehearing in part and grant clarification of the Commission's opinion issued on December 27, 2006, which affirmed in part and reversed in part an Initial Decision resolving issues related to the allocation of must-offer obligation costs in the California Independent System Operator Corporation's (CAISO) Amendment No. 60 to its open access transmission tariff (CAISO Tariff).[1]

Background

2. On July 20, 2001, the CAISO implemented a temporary must-offer requirement as an element of the mitigation and monitoring plan in response to the California energy crisis.[2] Pursuant to the must-offer obligation, most generators serving California markets

[1] *Cal. Indep. Sys. Operator Corp.*, 113 FERC ¶ 63,017 (2005) (Initial Decision), *aff'd in part and rev'd in part*, 117 FERC ¶ 61,348 (2006) (Opinion).

[2] Through a series of orders issued since April 2001, the Commission has addressed the must-offer obligation, including application and compensation issues. *See Cal. Indep. Sys. Operator Corp.*, 108 FERC ¶ 61,022, at P 2-8 (2004) (Amendment No. 60 Hearing Order) (providing summary of Commission action).

are required to offer all of their capacity in real time during all hours if it is available and not already scheduled to run through bilateral agreements.[3] The must-offer obligation is "designed to prevent withholding and thereby to ensure that the CAISO will be able to call upon available resources in the real-time market to the extent that energy is needed."[4] If must-offer generators are required to operate at minimum load to ensure that they are and will be available for the CAISO to dispatch in real time, then they receive minimum load costs compensation (MLCC) costs.[5] A generating unit may request a waiver of its must-offer obligation. If the CAISO denies a waiver request (must-offer waiver denial), then the generator is required to remain in operation and is compensated for the costs of running at its minimum operating level,[6] including when the CAISO actually dispatches energy from the unit or the generator provides ancillary services. The CAISO currently allocates MLCC costs to market participants on a system-wide basis. The must-offer obligation will continue for a locked-in period that will end with implementation of the CAISO's Market Redesign and Technology Upgrade (MRTU), now expected on March 31, 2008.

3. On May 11, 2004, in Docket No. ER04-835-000, the CAISO filed Amendment No. 60, among other things, to modify certain payment terms and the allocation of must-

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[3] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 95 FERC ¶ 61,115, at 61,355-57 (2001) (April 2001 Order), *order on reh'g*, *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 95 FERC ¶ 61,418 (2001) (June 2001 Order), *order on reh'g*, *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 97 FERC ¶ 61,275 (2001), *order on reh'g*, *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 99 FERC ¶ 61,160 (2002), *petition pending sub nom. Public Utilities Comm'n of the State of California v. FERC*, 9th Cir. Nos. 01-71051, *et al*. (placed in abeyance Aug. 21, 2002).

[4] June 2001 Order, 95 FERC ¶ 61,418 at 62,551.

[5] The MLCC costs consist of minimum operating level costs plus a $6.00/MWh adder for variable operations and maintenance. Initial Decision, 113 FERC ¶ 63,017 at n.24.

[6] These costs consist of start-up, emissions and MLCC costs. Exh. S-6; *see also San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 97 FERC ¶ 61,293, at 62,362-363 (2001) (December 2001 Order), *order on reh'g*, 99 FERC ¶ 61,159, *order on reh'g*, 100 FERC ¶ 61,050 (2002), *order on reh'g*, 105 FERC ¶ 61,065 (2003), *order on reh'g*, 107 FERC ¶ 61,165, *order on reh'g*, 109 FERC ¶ 61,128 (2004), *order on reh'g*, 110 FERC ¶ 61,336, *reh'g denied*, 112 FERC ¶ 61,226 (2005).

offer costs in a manner more consistent with cost causation principles. Based upon its determination that must-offer generation has been committed primarily to satisfy local, zonal or system reliability requirements, the CAISO proposed to allocate MLCC costs according to a three-category (or "bucket") rate design.[7]

4. On May 18, 2004, in Docket No. EL04-103-000, Pacific Gas and Electric Company (PG&E) filed a complaint against the CAISO, alleging that the methodology for allocating must-offer obligation costs to PG&E was unjust, unreasonable and unduly discriminatory. PG&E also alleged that Amendment No. 60 indefinitely prolonged the CAISO's allocation method, even though the CAISO had the ability to apportion must-offer obligation costs more equitably in a timelier manner. PG&E requested that the Commission consolidate its complaint with the Amendment No. 60 proceeding in Docket No. ER04-835-000.

5. On July 8, 2004, the Commission issued two orders. First, the Commission set PG&E's complaint for hearing, established a refund effective date of July 17, 2004 and consolidated Docket Nos. EL04-103-000 and ER04-835-000.[8] Second, the Commission accepted Amendment No. 60, subject to modification, and set for hearing the allocation of must-offer obligation costs.[9]

6. The Initial Decision generally upheld as just and reasonable the proposed method for allocating must-offer obligation costs.

7. In the Opinion, the Commission summarily affirmed and adopted the findings by the judge with respect to the following issues: (1) the factors to consider in determining whether Amendment No. 60's cost allocation proposal is just, reasonable and not unduly discriminatory (Issue No. 1); (2) whether the concept of classifying MLCC costs into three buckets is just and reasonable (Issue No. 2); (3) the proposal of the Cites of Anaheim, Azusa, Banning, Colton and Riverside, California (collectively, Southern Cities) to use the CAISO's RMR cost allocation methodology; (4) the California Department of Water Resources State Water Project's (SWP) proposal to create geographic sub-zones so that costs are allocated only to loads located in areas for which costs are incurred and based on scheduling coordinator (SC)-identified load groups or

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[7] *See* Opinion, 117 FERC ¶ 61,348 at P 16.

[8] *Pacific Gas and Elec. Co. v. Cal. Indep. Sys. Operator Corp.*, 108 FERC ¶ 61,017 (2004) (PG&E Complaint Hearing Order).

[9] Amendment No. 60 Hearing Order, 108 FERC ¶ 61,022.

other CAISO settlement designations and loads located in areas that do not cause MLCC costs to be incurred are excluded; (5) the CAISO treatment of MLCC costs related to must-offer waivers denied for more than one reason (Issue No. 12); (6) whether non-local MLCC costs should be assessed only to load occurring in the peak time periods for which must-offer waivers are denied (Issue No. 6); and (7) if non-local MLCC costs should be allocated only to loads occurring in the peak time periods for which must-offer waivers are denied, how the peak period should be defined (Issue No. 7).

8. The Commission reversed the findings by the judge with respect to the following issues: (1) whether wheel-through schedules should be exempted from all or some system MLCC costs, and (2) whether start-up and emissions costs of units denied must-offer waivers should be allocated in the same manner as those associated with MLCC and whether a revision to the allocation of these costs should be addressed in this proceeding.

9. The CAISO; SWP; Southern Cities; Powerex Corp. (Powerex); Southern California Edison Company (SoCal Edison) filed requests for rehearing of the Opinion. Powerex filed an answer to the CAISO's request for rehearing.

Discussion

A. Procedural Matters

1. Powerex Answer to Rehearing Request

10. Rule 713(d)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d)(1) (2007), prohibits an answer to a request for rehearing. Therefore, we will not accept Powerex's answer.

2. Motion to Reopen the Record

11. Prior to the Commission's issuance of the Opinion, Powerex filed a motion to reopen the record to admit evidence that became available after the close of the record, which it claimed would shed light on whether Amendment No. 60 comported with the principle of cost causation and whether Powerex's alternative proposal was just and reasonable.[10] Powerex sought admission of the CAISO's Market Monitoring Report for Events of June-July 2005 and Assessment of Day-Ahead Scheduling Practices issued on September 7, 2005 (Market Monitoring Report); the CAISO's Amendment No. 72 to its tariff filed with the Commission in Docket No. ER05-1502-000 on September 22, 2005

[10] Opinion, 117 FERC ¶ 61,348 at P 10.

(Amendment No. 72);[11] and the Commission's November 21, 2005 Order on Amendment No. 72.[12] Trial Staff has requested that the Commission provide the opportunity for discovery and answering testimony if this additional evidence is admitted into the record.[13]

12. In the Opinion, the Commission denied Powerex's motion because it found that Powerex had failed to demonstrate the existence of extraordinary circumstances that outweighed the need for finality in the administrative process.[14] The Commission found that Powerex had merely put forth additional documentation that it claimed supported its position.[15] Because it denied Powerex's motion, the Commission struck all references to the documents at issue from Powerex's brief on exceptions.[16]

Rehearing Request

13. On rehearing, Powerex contends that both the Market Monitoring Report and the Amendment No. 72 filing are extraordinary because they directly contradict the position taken by the CAISO in this proceeding. Powerex argues that these documents contradict the CAISO's position that the cost allocation methodology for system MLCC costs, including the allocation of costs based on SC net negative uninstructed deviation (NNUD),[17] is just and reasonable and satisfies the Commission's cost causation

[11] In Amendment No. 72, the CAISO proposed to revise the CAISO tariff to require scheduling coordinators to submit day-ahead schedules that reflect 95 percent of their forecasted daily demand.

[12] *Cal. Indep. Sys. Operator Corp.*, 113 FERC ¶ 61,187 (2005).

[13] *See* Opinion, 117 FERC ¶ 61,348 at P 12; Trial Staff Answer to Motion to Reopen the Record, Docket Nos. ER04-835-000 and EL04-103-000, at 15-16 (Dec. 15, 2005).

[14] Opinion, 117 FERC ¶ 61,348 at P 13.

[15] *Id*.

[16] *Id*.

[17] NNUD is defined as the real-time change in generation or demand associated with under-scheduled load (i.e., load that appears unscheduled in real-time) and over-scheduled generation (i.e., generation that is scheduled in forward markets and does not appear in real-time.) *See* CAISO Tariff, Master Definitions Supplement; Exh. S-18 at 15:2-11. Deviations are netted for each settlement interval, apply to a SC's entire

(continued…)

principles.[18] Powerex contends that these documents indicate that the proposed system MLCC cost allocation methodology would increase costs for market participants and would not create incentives for accurate day-ahead scheduling. Powerex adds that the release of the Market Monitoring Report and the filing of Amendment No. 72 shortly after the close of the administrative record also constitute extraordinary circumstances.[19] Therefore, Powerex requests that the Commission grant rehearing on this issue.

Commission Determination

14. In order to persuade the Commission to exercise its discretion to reopen the record, the requesting party must demonstrate the existence of "extraordinary circumstances."[20] The Commission has held that

> [t]he party must demonstrate a change in circumstances that is more than just material -- it must be a change that goes to the very heart of the case. This policy against reopening the record except in extraordinary circumstances is based on the need for finality in the administrative process.[21]

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portfolio, and include load, generation, and interchange (imports and exports). *See* Exh. S-18 at 15:8-10. An interchange deviation, measured from the final hour-ahead schedule, consists of any operational adjustments (i.e., a real-time change to a final hour-ahead schedule not made pursuant to a bid in the CAISO's markets). *See* Exh. S-23 at 1. Real-time curtailments are negative deviations; real-time increases are positive deviations. *See Id*. NNUD represents the amount of energy the CAISO must secure within real-time to keep demand and supply in balance. *See* Exh. ISO-22 at 27:20-28:5.

[18] Powerex Rehearing Request at 24 (citing Powerex Brief on Exceptions, Docket Nos. ER04-835-000 and EL04-103-000, App. A at 15 (Nov. 30, 2005) (Powerex Brief on Exceptions).

[19] *Id*. at 3 (citing *Pacific Gas & Elec. Co.*, 67 FERC ¶ 61,239 (1994)) and 24.

[20] *See CSM Midland Inc.*, 56 FERC ¶ 61,177 at 61,624 (1991).

[21] *See Id.* (citing *S. Co. Servs., Inc.*, 43 FERC ¶ 61,003, at 61,024 (*Southern Companies*), *reh'g denied*, 43 FERC ¶ 61,394 (1988), *aff'd mem. sub nom. Gulf States Utils. Co. v. FERC*, 886 F.2d 442 (D.C. Cir. 1989), *cert. denied*, 495 U.S. 947 (1990); *Friends of the River v. FERC*, 720 F.2d 93, 98 n.6, 109 (D.C. Cir. 1983)).

In *Southern Companies*, the Commission found that "the question of whether to reopen the evidentiary record is a matter of agency discretion" with courts only requiring agencies to reopen records when there are "extraordinary circumstances."[22] The Commission noted that "extraordinary circumstances" have been defined as a change in circumstances "that is not merely 'material' but rises to the level of a change in 'core' circumstances, the kind of change that goes to the very heart of the case."[23]

15. We find that Powerex has failed to demonstrate the existence of "extraordinary circumstances" that would warrant reopening the record. Powerex again argues that extraordinary circumstances exist because the evidence at issue directly contradicts the position taken by the CAISO in this proceeding.[24] Even if this evidence were material, we do not find that it rises to the level of extraordinary because it merely supplements other record evidence provided by Powerex. Moreover, other parties to the proceeding have not had an opportunity to evaluate or challenge this evidence. Finally, that this evidence became available shortly after the close of the record does not result in a change in core circumstances.[25] We find that the circumstances here do not outweigh the need for finality in the administrative process. For these reasons, we deny Powerex's rehearing request.

B. Cost Allocation Issues

16. In the Opinion, the Commission summarily affirmed and adopted the judge's findings that the concept of allocating MLCC costs according to which category a unit

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[22] *Southern Cos.*, 43 FERC ¶ 61,003 at 61,024 (1988) (citing *Bowman Transp., Inc. v. Ark. Best Freight System, Inc.*, 419 U.S. 281, 296 (1974)).

[23] *Id.* (quoting *Am. Fin. Servs. Ass'n v. FTC*, 767 F.2d 957, 964, n. 5 (D.C. Cir. 1985); *Am. Optometric Ass'n v. FTC*, 626 F.2d 896, 907 (D.C. Cir. 1980); *see also Greater Boston Television Corp. v. FCC*, 463 F.2d 268, 283 (D.C. Cir. 1971), *cert. denied*, 406 U.S. 950 (1972)).

[24] *See* Opinion, 117 FERC ¶ 61,348 at P 11; Powerex Motion to Reopen the Record, Docket Nos. ER04-835-000 and EL04-103-000, at 8 (Dec. 1, 2005).

[25] Even if this information had a bearing on our determination, we find that it is not persuasive because, while the evidence may have become available shortly after the close of the record, Powerex did not file its motion to reopen the record until four months after the judge closed the record on August 1, 2005.

belongs is just, reasonable and not unduly discriminatory.[26] But, consistent with the judge's findings, the Commission agreed that the CAISO's proposed criteria for determining whether a generating unit falls within the local, zonal or system categories, set forth in Attachment E to the filing, had not been included in the CAISO Tariff itself and thus were not part of the tariff amendment.[27] The Commission agreed therefore that the judge could consider the alternative proposals before him.[28]

1. Should MLCC Costs be Allocated to Each of the Local, Zonal and System Categories Pursuant to the Criteria Used by the CAISO to Classify Units Committed Under the Must-Offer Waiver Denial Process as Set Forth in Attachment E to the CAISO's Filing or in Another Manner? (Issue No. 3)

a. Review of Alternative Cost Allocation Proposals

(1) CAISO's Attachment E Criteria

17. In the Opinion, the Commission summarily affirmed and adopted the judge's finding that the Attachment E MLCC cost allocation was just, reasonable and not unduly discriminatory and satisfied the Commission's cost causation and benefits derived standard.[29] The next issue considered was whether the CAISO's actual classification of units pursuant to the Attachment E criteria was just and reasonable.[30]

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[26] Opinion, 117 FERC ¶ 61,348 at P 19.

[27] *See Id*. P 20, 22.

[28] *Id*. P 21-22.

[29] *Id*. P 25.

[30] *See Id*. P 26-39.

(a) Application of Attachment E Criteria: Miguel Transform Bank (Miguel) and South of Lugo Transformer Path (South of Lugo)

Initial Decision and Opinion No. 492

18. In the Initial Decision, the judge raised concerns about the classification of two constraints pursuant to the Attachment E criteria: Miguel and South of Lugo.[31] The CAISO had proposed to include Miguel and South of Lugo in the zonal cost allocation category because the CAISO determined that, operationally, each provides a "more regional benefit" to the entire SP-15 zone.[32]

19. The judge found that Miguel did not satisfy the inter-zonal interface definition because it lies within the three existing CAISO congestion zones and, therefore, would fall into the local cost allocation category.[33] However, the judge agreed with the CAISO's decision to categorize it as a zonal constraint because its actual operational characteristics indicated that it provides regional reliability benefits that are more consistent with the zonal category.[34] The judge concluded that it was not necessary for the CAISO to modify the Attachment E zonal criteria in order to categorize Miguel as a zonal constraint; however, the judge suggested that the CAISO modify either the tariff definition of inter-zonal interface or the Attachment E zonal criteria to accommodate Miguel.[35] In the Opinion, the Commission affirmed the judge's findings that Miguel should be categorized as a zonal unit.[36] The Commission found that Miguel satisfied the zonal criteria set forth in Attachment E and that that criteria would not need to be

[31] *Id*. P 26 (citing Initial Decision, 113 FERC ¶ 63,017 at P 88).

[32] *Id*.

[33] *Id*. P 27 (citing Initial Decision, 113 FERC ¶ 63,017 at P 67, n.38, 88, n.34).

[34] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 90).

[35] *Id*.

[36] *Id*. P 31.

modified to accommodate Miguel.[37] However, as recommended in the Initial Decision, the Commission directed the CAISO to modify the tariff definition of inter-zonal interface to describe Miguel's function more accurately.[38]

20. In the Initial Decision, the judge found that South of Lugo should be categorized as a local, rather than a zonal, constraint.[39] The judge made this finding because the unit: (1) did not satisfy the inter-zonal interface definition because it lies within the three existing CAISO congestion zones; (2) did not implicate transmission paths between congestion zones; (3) constituted a network location where must-offer generation is used to maintain acceptable voltage levels; and (4) did not operate within the requirements of any nomogram governing the operations of an inter-zonal transmission path.[40] The judge concluded that South of Lugo should be categorized as a local constraint based upon its operational characteristics and the CAISO's Operating Procedures and because the judge determined that assertions to the contrary were based on broad statements.[41]

21. In the Opinion, the Commission affirmed the judge's finding that South of Lugo should be categorized as a local constraint.[42] The Commission found that the South of Lugo constraint satisfied all of the Attachment E criteria for the local category and none for the zonal category.[43] The Commission also found that South of Lugo's operational characteristics and the CAISO's Operating Procedures demonstrated that it should be characterized as a local constraint.[44] Also, in response to the arguments that there was no basis upon which to distinguish between Miguel and South of Lugo for cost allocation purposes and for allowing the Attachment E criteria to be modified to accommodate

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[37] *Id*. (citing Exh. S-6 at 22-24 (protected); Exh. S-13 at 2 (protected); Exh. S-6 at 23 (protected); Exh. S-13 at 6 (protected)).

[38] *Id*.

[39] *Id*. P 32 (citing Initial Decision, 113 FERC ¶ 63,017 at P 91).

[40] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 67, n.38, 88, n.34, 91).

[41] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 91).

[42] *Id*. P 39.

[43] *Id*.

[44] *Id*.

Miguel but not South of Lugo, the Commission made two findings.[45] First, the Commission found that the judge's conclusions demonstrated that South of Lugo fully satisfied the local criteria under Attachment E while Miguel satisfied the zonal criteria.[46] Second, the Commission found that the Attachment E criteria did not need modification to accommodate the Miguel constraint.[47]

Rehearing Request

22. On rehearing, SoCal Edison argues that the Commission erred by not directing the CAISO to modify the Attachment E criteria to allow South of Lugo to be classified as a zonal constraint.[48] First, SoCal Edison claims that the failure to classify South of Lugo as a zonal constraint will lead to an unjust and unreasonable result because all CAISO grid users in southern California cause South of Lugo's costs and benefit from the CAISO's must-offer calls that relieve that constraint. In particular, SoCal Edison contends that it will be held responsible for over $165 million in MLCC costs associated with South of Lugo from 2004-2006, while Southern Cities, San Diego Gas and Electric Company (SDG&E) and other load serving entities in the SP-15 zone will not pay anything. Second, SoCal Edison argues that, although South of Lugo is not an inter-zonal interface, it should be classified as zonal because (1) resolution of constraints on the South of Lugo path provide a regional benefit to Southern Cities' loads and Southern Cities contribute to constraints on the South of Lugo path;[49] (2) South of Lugo is associated with multiple

[45] *Id*.

[46] *Id*.

[47] *Id*.

[48] SoCal Edison Rehearing Request at 5 (citing Initial Decision, 113 FERC ¶ 63,017 at P 96, n.58, P 116, n.80).

[49] *Id*. at 6 (citing Initial Decision, 113 FERC ¶ 63,017 at P 95 (pointing to evidence in the record indicating that Southern Cities' loads cause and benefit from SP-15 zonal MLCC cost incurrence in the same manner as SoCal Edison's load); Exh. ISO-1 at 26:16-27:15)) and 7 (citing Exh. SCE-6, 10:18-21; Exh. ISO-1, 26:16-27:15).

500kV transmission paths;[50] (3) loads and generation of SDG&E and other LSEs in SP-15 impact power flows over the South of Lugo path;[51] and (4) South of Lugo has significant regional impacts on more than one participating transmission owner (PTO).[52]

23. SoCal Edison also argues that the Commission erred by accepting the Attachment E criteria because these criteria do not follow cost causation and benefits derived principles. SoCal Edison disputes the criteria's delineation between intra-zonal and inter-zonal constraints to distinguish between local and zonal units because this delineation does not recognize that intra-zonal constraints, such as South of Lugo and Miguel, can have broad regional impacts that justify the zonal allocation of costs incurred to resolve those constraints.[53] SoCal Edison claims that, after it filed Amendment No. 60, the CAISO advocated revising the Attachment E classification criteria to shift South of Lugo and Miguel from the local to the zonal category to track cost causation and benefits received more appropriately.[54]

24. SoCal Edison claims that the Commission compounded its error of accepting the Attachment E criteria by rigidly applying those flawed criteria to classify South of Lugo as a local constraint, while departing from the Attachment E criteria to reclassify Miguel as a zonal constraint. SoCal Edison argues that both Miguel and South of Lugo satisfy the local criteria because both are intra-zonal constraints.[55] SoCal Edison claims that the fact that Miguel also satisfies one of the zonal criteria because Operating Procedure T-132E is a nomogram that governs an inter-zonal path as well as Miguel does not overcome the fact that Miguel also meets all of the local criteria and that the Attachment E criteria must be modified to resolve that conflict.[56] SoCal Edison adds that the Commission departs from the Attachment E criteria in the factors it cites as favoring the

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[50] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 93).

[51] *Id*. at 7 (citing Exh. SCE-6, 24:17-25:7).

[52] *Id*. (citing Exh. ISO-22 at 23:20, 25:8-9; Tr. 501:1-2; Exh. SCE-6 at 10:20-21).

[53] *Id*. at 9 (citing Exh. S-21; Initial Decision, 113 FERC ¶ 63,017 at P 65 n.34, 88, n.52; Exh. ISO-22 at 23).

[54] *Id*. (citing Opinion, 117 FERC ¶ 61,348 at P 26; Initial Decision, 113 FERC ¶ 63,017 at P 67 n.38).

[55] *Id*. at 10-11 (citing Initial Decision, 113 FERC ¶ 63,017 at P 65 n.34, 88, n.52).

[56] *Id*. at 11 (citing Exh. S-13; Opinion, 117 FERC ¶ 61,348 at P 31).

classification of Miguel as a zonal constraint (i.e., reliability benefits and the ability of units throughout the zone to resolve congestion at Miguel). SoCal Edison claims that the judge recognized that the MLCC costs incurred to resolve constraints on the South of Lugo path also provide broad zonal reliability benefits and congestion relief. SoCal Edison argues that focusing on the CAISO's Operating Procedures ignores the key point of the allocation of MLCC costs: to ensure that those who contribute to MLCC costs and benefit from the incurrence of such costs pay their fair share.[57] SoCal Edison concludes that the record evidence justifies adopting classification criteria in the CAISO Tariff that result in South of Lugo's classification as a zonal constraint.[58]

Commission Determination

25. Upon further review, we will grant rehearing and find that South of Lugo should be categorized as a zonal constraint. Although South of Lugo does not satisfy the inter-zonal interface definition in Attachment E, we find that it should be categorized as a zonal constraint because, like Miguel, its actual operational characteristics indicate that it provides regional reliability benefits that are more consistent with a zonal constraint. The record indicates that: (1) resolution of constraints on the South of Lugo path provide a regional benefit to Southern Cities' loads and Southern Cities contribute to constraints on the South of Lugo path;[59] (2) South of Lugo is associated with multiple 500kV transmission paths;[60] (3) loads and generation of SDG&E and other LSEs in SP-15 impact power flows over the South of Lugo path;[61] and (4) South of Lugo has significant regional impacts on more than one PTO.[62]

26. Upon further review, we also find that the most current CAISO operating procedure for South of Lugo (Operating Procedure T-144, version 4.4) supports

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[57] *Id*. at 12 (citing Initial Decision, 113 FERC ¶ 63,017 at P 88, 91, n.55).

[58] *Id*. at 8 (citing Initial Decision, 113 FERC ¶ 63,017 at P 67 n.38) and 12.

[59] *See* Initial Decision, 113 FERC ¶ 63,017 at P 95 (citing Exh. SCE-19 at 2; Exh. SCE-10 at 2-3; Tr. at 1404-06 (protected); Exh. SOC-42 at 6-7; Exh. S-37; Exh. SCE-6 at 9-11; Tr. at 1387-88; Exh. SCE-9 at 6, 9); *see also* Exh. ISO-1 at 26:16-27:5; Exh. SCE-6 at 10:18-21.

[60] *See Id*. P 93 (citing Exh. ISO-22 at 23, 25).

[61] Exh. SCE-6 at 24:17-25:9; Exh. S-37.

[62] Exh. ISO-22 at 25:7-16; Exh. S-37; Exh. SCE-6 at 10:20-21.

categorizing South of Lugo as a zonal constraint.[63] This version of the Operating Procedure T-144 was revised to indicate that the parties affected by South of Lugo include utility distribution companies in SP-15 and metered subsystems in SP-15.[64] It was also revised to indicate that, if the CAISO needs to curtail load in the event of a South of Lugo overload, then the CAISO should curtail not only SoCal Edison load, but also SP-15 load.[65] These revisions indicate that South of Lugo has a regional impact that is more consistent with a zonal constraint. We disagree with the judge's apparent conclusion that, even though the revisions in version 4.4 support categorizing South of Lugo as a zonal constraint, version 4.4 is not reliable because the revisions therein are not based upon engineering studies, analysis, calculations or other documentation.[66] We find that this type of documentation is not necessary to support instructions on curtailing load and identification of the parties affected by a constraint. For these reasons, we grant rehearing and find that South of Lugo should be categorized as a zonal constraint. We direct the CAISO to make a compliance filing, within 30 days of the date of this order, modifying the Attachment E zonal criteria to accommodate South of Lugo.

(b) Under Attachment E, Whether the "Incremental Cost of Local" Approach for Determining the Allocation of MLCC Costs Between "System" and "Local" Categories is Just and Reasonable? (Issue No. 4)

27. In addition to the three bucket allocation, the CAISO included an "incremental cost of local" cost allocation methodology in its Attachment E criteria. According to this methodology, when a must-offer unit is committed for local reliability requirements and the unit commitment simultaneously satisfies a system requirement, the CAISO allocates

[63] *See* Exh. SCE-12 (protected); Exh. SCE-6 at 23:3-7.

[64] *See* Exh. SCE-12 at 9 (protected); *compare with* Exh. S-16 at 9 (protected); *see also* Exh. SCE-6 at 23:20-25.

[65] *See* Exh. SCE-12 at 5, 7 (protected); *compare with* Exh. S-16 at 5,7 (protected); *see also* Exh. SCE-6 at 23:10-19, 23-25; Exh. S-37.

[66] *See* Initial Decision, 113 FERC ¶ 63,017 at n.55 (citing Exh. S-42; Tr. at 612-13 (protected)).

only the incremental cost of committing the unit to the local category/PTO.[67] The incremental cost of local is calculated by subtracting the cost of committing the cheapest available unit(s) from the cost of committing the required must-offer unit(s).[68]

Initial Decision and Opinion No. 492

28. In the Initial Decision, the judge concluded that Commission policy and the record support the net incremental cost of local approach.[69] He found that the CAISO was capable of implementing the methodology.[70] He also found that the methodology was capable of differentiating between local and system MLCC cost components when a must-offer unit committed for local reliability requirements simultaneously satisfies system requirements.[71] He concluded that this differentiation was consistent with Commission policy that costs be matched, to the greatest extent practicable, to the customers responsible for imposing the cost burden or benefiting from it.[72] He also found that the net incremental approach results in appropriate cost sharing, not cost shifting.[73] He rejected any claim that the net incremental cost of local approach undermines the California Public Utilities Commission's (CPUC) policies on local reliability/resource adequacy.[74] He also rejected any contention that the approach was discriminatory or preferential because it inures primarily, or exclusively, to SoCal Edison's benefit because a non-differentiated local MLCC cost allocation would impose unwarranted system costs on SoCal Edison.[75] Although the judge concluded that the net

[67] *Id*. P 117 (citing Exh. S-21 at 2).

[68] *Id*. (citing Exh. S-21 at 2).

[69] Opinion, 117 FERC ¶ 61,348 at P 41 (citing Initial Decision, 113 FERC ¶ 63,017 at P 120).

[70] *Id*.

[71] *Id*.

[72] *Id*.

[73] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 121).

[74] *Id*.

[75] *Id*.

incremental approach was generally just, reasonable and not unduly discriminatory, he found that certain modifications were necessary due to data inaccuracies in the proceeding.[76]

29. In the Opinion, the Commission affirmed the judge's findings.[77] The Commission agreed that the differentiation was consistent with the Commission's policy that costs be matched, to the greatest extent practicable, to the customers responsible for imposing the cost burden or benefiting from it.[78] The Commission also agreed that, if a must-offer unit was denied a waiver for local reasons and another generating unit that otherwise would have been committed for system reasons was not denied a waiver because the local unit also met the system needs, it was appropriate to distribute the costs of the must-offer unit among the system and local buckets.[79] The Commission found that the CAISO's proposal to reflect part of these costs as local and part as system was just and reasonable because, under its Security Constrained Unit Commitment (SCUC) application, the CAISO had established that it was capable of differentiating between local and system MLCC cost components when a must-offer unit committed for local reliability requirements simultaneously satisfied system requirements.[80] The Commission also directed the CAISO to make the modifications that the judge recommended.[81]

Rehearing Request

30. On rehearing, Southern Cities argue that the CAISO's must-offer obligation authority serves as a substitute for reliability must run (RMR) generation in southern California and, as such, MLCC costs should be allocated in the same manner as RMR costs (i.e., to the responsible utility, or PTO, that is best suited to remedy the need for the

[76] *Id*. P 42 (citing Initial Decision, 113 FERC ¶ 63,017 at P 122).

[77] *Id*. P 48.

[78] *Id*.

[79] *Id*.

[80] *Id*.

[81] *Id*. P 49.

CAISO to take steps to address local reliability problems in the first instance).[82] Southern Cities contends that the net incremental cost of local approach is inequitable because different reliability cost allocation schemes exist between northern California (where the CAISO manages reliability issues with RMR resources) and southern California (where the CAISO uses its must-offer obligation authority).[83] Southern Cities claims that, unlike the cost allocation approach for RMR costs used throughout the rest of the CAISO grid, when the CAISO incurs MLCC costs in the SP-15 zone to address local needs, the CAISO reallocates a portion of those costs to the system category, which spreads the costs throughout the CAISO Control Area.[84] Southern Cities contends that, as a result, this cost allocation approach for MLCC costs fails to provide the local PTO with the appropriate market signals to take steps to reduce must-offer obligation charges.[85] Southern Cities argues that the Commission must explain the shift in policy that allows the CAISO to impose the net incremental cost of local cost allocation approach and depart from the prior practice of allocating reliability costs incurred for local reasons to the PTO.

Commission Determination

31. We will deny Southern Cities' rehearing request. We do not agree that reliability costs incurred through RMR contracts and the must-offer obligation are identical. The record shows that the CAISO will commit and dispatch RMR units before denying a must-offer waiver except where (1) the operating problem being addressed falls outside of the authority conferred on the CAISO under the RMR contract (e.g., a system energy need or use for managing inter-zonal congestion), or (2) the available RMR unit would not be effective in mitigating the local problem.[86] Thus, because the CAISO does not have authority to commit RMR units to address system energy needs or to manage inter-zonal congestion, the use of RMR units is limited to resolving local reliability problems.

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[82] Southern Cities Rehearing Request at 3 (citing *Cal. Indep. Sys. Operator Corp.*, 90 FERC ¶ 61,315 at 62,041 (2000)) and 5.

[83] *Id*. at 8 (citing Tr. 475:8-25; Tr. 1203:13-19; Tr. 845:3-19; Tr. 490:19-491:4) and 9.

[84] *Id*. at 9 (citing Exh. No. ISO-1 at 40:17-44:4).

[85] *Id*. at 9-10 (citing Tr. 577:24-578:10; Tr. 915:18-916:18).

[86] *See* Exh. SCE-17.

In contrast, the CAISO has no such limitation with respect to committing must-offer units and may, as it does under the incremental cost of local approach, use a local must-offer unit to resolve both local and system reliability requirements.

32. Under the net incremental cost of local approach, the CAISO charges the costs of a local must-offer unit that resolves a local and a system problem to the affected local PTO and to the system bucket. Under the SCUC application, if a unit is denied a waiver for local reasons and another unit would have been committed for system reasons but for the local unit being denied a waiver, the costs are then allocated to both the local and system categories.[87] This sharing of costs is consistent with the principles of cost causation and benefits received, which are used to determine if a rate methodology is just and reasonable and non-discriminatory. If the reliability costs incurred through an RMR contract and the must-offer obligation were identical, the SCUC run would produce identical results and no costs would be allocated to the system category. Therefore, any ensuing price signal would be appropriate. Furthermore, in the Opinion, the Commission directed the CAISO to post on its website adequate information to provide market participants with the ability to confirm the appropriateness or accuracy of its incremental cost of local allocations. Therefore, contrary to Southern Cities' assertion, the Commission's determination on this issue is not a departure from – but is consistent with – our policy of allocating reliability costs incurred for local reasons to the responsible PTO. For these reasons, we deny Southern Cities' rehearing request.

(2) Other Proposals

(a) Whether ETC Schedules Should be Exempted from All or Some Zonal MLCC Costs (Issue No. 8)

33. SWP proposed that ETC schedules be exempt from the portion of zonal MLCC costs associated with inter-zonal congestion.[88]

Initial Decision and Opinion No. 492

34. In the Initial Decision, the judge found that SWP's argument that its proposal was consistent with historical circumstances failed because: (1) it does not account for the

[87] *See* Opinion, 117 FERC ¶ 61,348 at P 48, n.90; s*ee also* Exh. S-21 at 2; Exh. S-18 at 13:5-11.

[88] Opinion, 117 FERC ¶ 61,348 at P 65 (citing Initial Decision, 113 FERC ¶ 63,017 at P 100, 105).

fact that the must-offer obligation was an emergency measure implemented by the Commission in response to the California energy crisis and (2) it is inconsistent with the Commission edict that "all users of the transmission grid will be assigned [MLCC] costs consistent with the [CAISO's] markets performing a reliability function."[89] The judge also rejected the contention that the Commission's alleged prohibition on charging congestion charges to ETCs, except in contract conversion or termination, extends to MLCC cost allocation.[90] The judge concluded that ETC schedules should not be exempted from the portion of zonal MLCC costs associated with inter-zonal congestion.[91] Thus, he found that Amendment No. 60 was just, reasonable and not unduly discriminatory insofar as it allocates zonal MLCC costs to total demand within the affected zone, including ETC loads.[92]

35. In the Opinion, the Commission affirmed the judge's findings.[93] The Commission stated that, since the inception of the must-offer program, ETC customers have been liable for and have paid MLCC.[94] The Commission noted that MLCC costs are different from congestion costs and charges for RMR units; thus the allocation of MLCC costs to ETC customers is not a double recovery.[95] The Commission explained that MLCC charges are incurred to compensate a generator that operates at minimum load, regardless of whether that generator is dispatched by the CAISO to relieve congestion.[96] Therefore,

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[89] *Id*. P 65 (citing Initial Decision, 113 FERC ¶ 63,017 at n. 70 (*quoting San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 99 FERC ¶ 61,158, at 61,633 (2002) (May 2002 Order), *order on reh'g*, 100 FERC ¶ 61,050, *order on reh'g*, 105 FERC ¶ 61,065, *order on reh'g*, 107 FERC ¶ 61,165, *order on reh'g*, 109 FERC ¶ 61,128, *order on reh'g*, 110 FERC ¶ 61,336, *reh'g denied*, 112 FERC ¶ 61,226).

[90] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 106-07 (*citing* Item by Reference #1, v. 1, First Revised Sheet No. 323, Second Revised Sheet No. 307A, Original Sheet No. 56; Exh. S-18 at 20)).

[91] *Id*. P 65 (citing Initial Decision, 113 FERC ¶ 63,017 at P 108).

[92] *Id*.

[93] *Id*. P 68.

[94] *Id*.

[95] *Id*.

[96] *Id*.

the Commission agreed with the judge that there is a distinct difference between MLCC costs that are incurred to ensure grid reliability and congestion charges that are based on grid usage.[97]

Rehearing Request

36. On rehearing, SWP argues that the Commission disregarded evidence and precedent in reaching its determination. SWP again argues that the CAISO may not allocate to ETCs congestion charges of any kind, except in the circumstances concerning conversion or termination of contract rights.[98] SWP claims that the Commission erred in its determination that ETC customers should pay MLCC costs due to inter-zonal congestion because, since the inception of the must-offer program, they have been liable and have paid MLCC. SWP asserts that the Commission's determination is undermined by its statement in the hearing order that the use of must-offer units has changed since the must-offer was introduced as a temporary measure to prevent withholding during the California energy crisis.[99] SWP claims that the Commission's holding is also contradicted by CAISO Tariff sections 2.3.1.2.1, 2.4.4.4.4.3 and 2.4.4.5.2, which state that ETCs shall be honored and not modified without consent or absent a specific filing concerning that contract. SWP adds that ETC customers have not been given the reasonable notice required by the FPA[100] of charges because they did not know, until Amendment No. 60 was filed, that they would be allocated must-offer costs incurred due to inter-zonal congestion.[101] SWP argues that, if the CAISO did not charge ETC customers for must-offer costs due to inter-zonal congestion prior to Amendment No. 60, then the Commission has relied on erroneous facts.

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[97] *Id*.

[98] SWP Rehearing Request at 67 (citing 16 U.S.C. § 796(28)(B) (2005); *Cal. ex. rel. Lockyer v. FERC*, 383 F.3d 1006, 1012 (9th Cir. 2004) (*Lockyer*)).

[99] *Id*. at 70-71 (citing Amendment No. 60 Hearing Order, 108 FERC ¶ 61,022 at P 62-63).

[100] *Id*. at 73 (citing *Keyspan-Ravenswood, LLC v. FERC*, No. 05-1332 (D.C. Cir. Jan. 12, 2007); *Pacific Gas and Elec. Co. v. FERC*, 373 F.3d 1315, 1320 (D.C. Cir. 2004); *Lockyer*, 383 F.3d 1006, 1012).

[101] *Id*. at 72-73 (citing Tr. at 305:21-24, Exh. SWP-5 at 13-14; Theaker Depo. Vol. 2 at 267:14-268:8).

37. SWP also argues that it is factually and legally inaccurate to find that MLCC costs are distinct from congestion charges because MLCC costs are incurred to ensure grid reliability. SWP claims that this Commission finding disregards the plain language of CAISO Tariff section 5.11.6.1.4, which states that the Amendment No. 60 zonal category of costs are incurred due to inter-zonal congestion. SWP states that the CAISO could not reconcile the purported distinction between inter-zonal congestion costs and must-offer costs due to inter-zonal congestion.[102] SWP argues that, to the contrary, the definition of congestion in CAISO Tariff App. A includes the conditions that are addressed through commitment of must-offer generation due to inter-zonal congestion. SWP adds that the CAISO has admitted that must-offer generation costs incurred due to inter-zonal congestion are incurred to manage inter-zonal congestion.[103] To support its position, SWP points to the CAISO's experience addressing inter-zonal congestion under the standard congestion management scheme, which SWP claims is similar in nature and source to must-offer generation due to inter-zonal congestion.[104] SWP states that, if the Commission does not agree that the costs in question are due to inter-zonal congestion, then the Commission should direct the CAISO to modify the tariff to identify accurately the basis of the costs.

38. SWP asserts that, if the must-offer costs at issue are attributable to grid reliability, the Commission's determination is contrary to Commission precedent stating that, absent unbundling and a contract amendment, firm ETC service, which already encompasses reliability, should not be double charged through additional socialized grid reliability charges.[105]

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[102] *Id*. at 74-75 (citing Exh. ISO-19 at 16:11-13; Tr. at 304:2-20, 723:8-19).

[103] *Id*. at 76 (citing Tr. at 303:13-16, 720:18-721:1).

[104] *Id*. at 76-77 (citing Exh. SWP-18 at 26:1-27:11, 27:15-31:16; Tr. at 306:16-307:1, 1040:9-15; Exh. SWP-22B at 12-13; Patterson Depo. Vol. 2 at 198-200).

[105] *Id*. at 69, 78-80 (citing *Midwest Indep. Transmission Sys. Operator, Inc.*, 108 FERC ¶ 61,236, at P 162 (2004), *on reh'g*, 111 FERC ¶ 61,042 (2005), *on reh'g*, 112 FERC ¶ 61,311 (2005); *accord*, *Consolidated Edison Co. v. Public Serv. Elec. and Gas Co.*, 105 FERC ¶ 61,343, at P 23 (2003); *Pacific Gas & Elec. Co.*, 100 FERC ¶ 61,160, at P 19 (Opinion No. 459), *reh'g denied*, 101 FERC ¶ 61,139 (2002), *reh'g denied*, 102 FERC ¶ 61,009 (2003); *Cal. Indep. Sys. Operator Corp.*, 89 FERC ¶ 61,229, at 61,682 (1999), *on reh'g*, 90 FERC ¶ 61,315 (2000); *Cal. Indep. Sys. Operator Corp.*, 82 FERC ¶ 61,348 (1998)).

Commission Determination

39. We will deny SWP's rehearing request. SWP continues to argue that the distinction drawn by the judge and affirmed by the Commission regarding the nature of inter-zonal congestion is incorrect. We continue to believe that it is generally appropriate for ETC customers to be excluded from the assignment of usage charges for the use of a specified congested inter-zonal interface during a given hour. However, based on the facts of this case, we find that it is appropriate for ETC customers to be assigned a portion of MLCC costs incurred by the CAISO to assure that the grid has sufficient inter-zonal interface reliability. This assignment is not predicated on usage. Rather, these costs are incurred to assure that the grid will be available to allow for the transmission of all entitlements, including those of ETCs.[106] As noted by the CAISO, if the CAISO lacks adequate resources to resolve inter-zonal congestion, the ETC may be subject to curtailment.[107]

40. It is true that, in Opinion No. 459, the Commission rejected PG&E's proposed pass-through of CAISO Reliability Service (RS) charges to ETC customers because those customers receive and pay for RS pursuant to ETCs.[108] The Commission also determined that the allocation of RS charges to the unadjusted rates of the ETC customers would result in a double recovery.[109] However, the Commission has also held that all users of

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[106] *See* CAISO Brief Opposing Exceptions, Docket Nos. ER04-835-000 and EL04-103-000, at 19-21 (Dec. 20, 2005) (CAISO Brief Opposing Exceptions) (citing CAISO Tariff sections 7.2.1.5, 7.3.1, 7.3.2 (Item by Reference at Sheets 199, 207, 212), and 5.11.6.1.2 (Item by Reference 1 at Sheet 184E; *Cal. Indep. Sys. Operator Corp.*, 89 FERC ¶ 61,229 at 61,681-82; CAISO Tariff Dispatch Protocol section 8.3; Schedules and Bids Protocol section 3.3 (Item by Reference 1, Sheets 477, 549-51)); Trial Staff Brief Opposing Exceptions, Docket Nos. ER04-835-000 and EL04-103-000, at 39-42 (Dec. 20, 2005) (Trial Staff Brief Opposing Exceptions) (citing Initial Decision, 113 FERC ¶ 63,017 at P 105 (citing Exh. ISO-19 at 16; Tr. at 721-722), 106-107; Tr. at 720:18-721:1, 722:1-14, 1038:5-1039:1; Exh. ISO-19 at 16:4-13, 16:14-17, 16:17-17:4; December 2001 Order, 97 FERC ¶ 61,293 at 62,363; Exh. S-18 at 20:16-19).

[107] *See* CAISO Brief Opposing Exceptions at 21 (citing CAISO Tariff Dispatch Protocol section 8.3; Schedules and Bids Protocol section 3.3 (Item by Reference 1, Sheets 477, 549-51)).

[108] Opinion No. 459, 100 FERC ¶ 61,160 at P 18-20.

[109] *Id*.

the transmission grid will be assigned MLCC costs consistent with the CAISO markets' performing a reliability function, without exempting ETCs.[110] Further, the MLCC costs at issue herein were not included in any of the previous Control Area Agreements and therefore post-date the ETCs.[111] Because the MLCC costs post-date the ETCs, the MLCC costs are distinguishable from RS charges that could have been included in the underlying firm transmission rates of ETCs. Therefore, SWP is incorrect. There is no double recovery here and the unbundling directed in Opinion No. 459[112] is not required. Accordingly, consistent with the Commission's earlier findings regarding the allocation of MLCC costs to all users of the grid and to provide for full compensation of costs to provide reliable transmission service, we deny SWP's rehearing request.

(b) Whether the CAISO Should Allocate System MLCC Costs Based on Deviations Between Metered Load and Day-Ahead Scheduled Load (Where Day-Ahead Scheduled Load Deviates from Total Metered Load by More Than a Five Percent Threshold) (Issue No. 13)

41. Under the Attachment E cost allocation criteria, the CAISO would first allocate system MLCC costs to SCs with a NNUD up to a $/MWh capped rate.[113] To ensure MLCC costs are not allocated disproportionately, the CAISO would then allocate to all demand within the CAISO Control Area and in-state exports the system MLCC costs that exceed the capped rate.[114]

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[110] *See* May 2002 Order, 99 FERC 61,158 at 61,633 (citing December 2001 Order, 97 FERC ¶ 61,293 at 62,370).

[111] *See* CAISO Reply Brief, Docket Nos. ER04-835-000 and EL04-103-000, at 22-23 (Sept. 2, 2005) (citing *Pacific Gas and Elec. Co.*, 109 FERC ¶ 61,093, at P 66 (2004)).

[112] *See* Opinion No. 459, 100 FERC ¶ 61,160 at P 20.

[113] *See* Exh. ISO-1 at 28:12-29:9; Exh. S-18 at 14:13-17.

[114] *See* Exh. ISO-1 at 29:9-30:4.

Initial Decision and Opinion No. 492

42. In the hearing, Powerex objected to the Attachment E system category criteria because they allocate system MLCC costs to NNUDs.[115] Powerex claimed that allocating system MLCC costs to NNUDs unfairly imposes duplicate charges on energy imports.[116] Powerex also argued that the CAISO's proposed allocation was inappropriate because system MLCC costs are incurred in day-ahead timeframe, while NNUD is a function of real-time imbalances between schedules and demand.[117] Instead, Powerex proposed allocating system MLCC costs to the SC(s) responsible for the day-ahead scheduled load/actual metered load differentials that caused the costs to be incurred.[118]

43. In the Initial Decision, the judge agreed that allocating system MLCC costs to NNUDs compels an entity to make two payments based on the same deviation but disagreed that the payments were duplicative.[119] He found that, like a toll, the system MLCC costs are a use charge that recovers the proportionate cost the underlying deviation imposes on the transmission system.[120] He also found that, because fault was immaterial to cost incurrence and therefore cost causation, it was appropriate to allocate deviations beyond the importer's control to NNUDs.[121]

44. The judge found that the record did not support Powerex's proposal for several reasons.[122] First, he found that Powerex had not demonstrated any compelling reason to bind SCs to total day-ahead scheduled load for system MLCC cost allocation purposes.[123]

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[115] Opinion, 117 FERC ¶ 61,348 at P 73 (citing Initial Decision, 113 FERC ¶ 63,017 at P 110).

[116] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 110, 113).

[117] *Id*.

[118] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 110).

[119] *Id*. P 74 (citing Initial Decision, 113 FERC ¶ 63,017 at P 111).

[120] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 111, n.73).

[121] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 112).

[122] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 113-14).

[123] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at P 114).

Second, he found that Powerex had not provided a basis for the five percent tolerance band other than a data response indicating that it was generally accepted that forward market schedules should be within five percent of real-time load.[124] He stated that it was unclear how and why system MLCC costs would be allocated when the total system day-ahead schedule/metered load differential falls between 95 and 100 percent.[125]

45. In the Opinion, the Commission affirmed the judge's findings.[126] The Commission found that, because SCs are effectively "buying" the amount of energy represented by the NNUDs (i.e., the amount of energy that the CAISO must secure in real-time to keep demand and supply in balance) to balance their portfolios in real-time, the amount of NNUDs a SC incurred was the appropriate quantity to use to allocate the costs of the CAISO procuring the additional supply needed to keep the CAISO Control Area in balance.[127] The Commission rejected Powerex's arguments because the CAISO's day-ahead must-offer commitments are based on day-ahead estimates of the degree to which demand will exceed supply in real-time and must-offer waiver denials are based on estimated real-time loads for the day on which units will be required to be online, not final day-ahead schedules.[128] The Commission concluded that, therefore, it was misleading to characterize the must-offer waiver denial process as purely a "day-ahead" process.[129]

Rehearing Request

46. On rehearing, Powerex argues that the CAISO's proposal for allocating system MLCC costs does not satisfy the Commission's cost causation principles, which require cost to be allocated to entities that cause costs or benefit from their incurrence,[130] because

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[124] *Id*. (citing Initial Decision, 113 FERC ¶ 63,017 at n.76).

[125] *Id*.

[126] *Id*. P 80-81.

[127] *Id*. P 80.

[128] *Id*. P 81 (citing Exh. S-25; CAISO Operating Procedure M-432C).

[129] *Id*. (citing Exh. S-18 at 18).

[130] Powerex Rehearing Request at 2-3 (citing PG&E Complaint Hearing Order, 108 FERC ¶ 61,017 at P 62 (2004); *Alabama Elec. Coop. v. FERC*, 684 F.2d 20, 27 (D.C. Cir. 1982); *American Elec. Power Serv. Corp.*, 111 FERC ¶ 61,180, at P 5, 25-30 (2005); (continued…)

NNUD do not cause the issuance of must-offer waiver denial or the incurrence of the associated system MLCC costs. Powerex contends that, because the CAISO does not consider actual NNUD, or even the deviation underlying the NNUD, when making its must-offer waiver denial decision, it cannot base its waiver decision on these data.[131]

47. Powerex disagrees that it is misleading to characterize the must-offer waiver denial process as purely a day-ahead process because the CAISO does not incorporate actual schedule deviations into its forecasts, only average historical hour-ahead schedules.[132] Powerex argues that average historical practices do not tell the CAISO which SCs will actually deviate in a particular operating hour and which SCs are the ultimate reason demand may exceed supply in real-time. Powerex also claims that, regardless of SCs' ability to adjust their schedules in the hour-ahead market, the CAISO issues must-offer waiver denials and thus locks in associated costs in the day before the operating hour. Powerex contends that minimum load energy (automatically committed through the must-offer obligation process and taking place the day before the operating hour) is real-time energy only in the sense that it reduces the requirement for the CAISO to dispatch incremental real-time energy to balance generation or load that does not appear scheduled in real-time.[133] Powerex adds that the CAISO describes the must-offer waiver denial process as a day-ahead process in its Operating Procedure M-432C.[134]

48. Powerex contends that the CAISO's proposal is internally inconsistent because, while the CAISO considers historical data showing deviations between the day-ahead and the hour-ahead timeframes in the must-offer waiver denial process, the CAISO would allocate system MLCC costs based on the deviation between the hour-ahead and real-time timeframes (based on NNUD). Powerex therefore claims that the proposal does not accurately reflect the factors the CAISO takes into account during the must-offer commitment process.

49. Powerex argues that, although there is a correlation between the amount of energy in an NNUD and the energy the CAISO must procure in the real-time market to balance

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Cal. Indep. Sys. Operator Corp., 106 FERC ¶ 61,032, at P 5, 20 (2004); *New York Indep. Sys. Operator*, 102 FERC ¶ 61,284, at P 14-15 (2003)).

[131] *Id*. at 11-12 (citing Exh. PWX-3 at 5-6; Tr. at 530:7-17, 542:21-543:20).

[132] *Id*. at 13 (citing Exh. PWX-3 at 7; Tr. at 570:18-23).

[133] *Id*. (citing Tr. at 1495:10-16).

[134] *Id*. (citing Exh. PWX-3 at 5-6).

schedules, it does not follow that these deviations cause the CAISO to procure must-offer capacity. Powerex points out that the CAISO procures in real-time, not through must-offer waiver denials, most of the energy to make up for deviations underlying NNUD.[135] Therefore, according to Powerex, these deviations are not an appropriate basis upon which to allocate the system MLCC costs arising from the issuances of must-offer waiver denials. Powerex adds that the allocation proposal imposes excessive costs on SCs who already pay the replacement costs of energy that the CAISO must procure in real-time.[136]

50. Powerex asserts that, contrary to the Commission's finding with respect to who benefited from the costs at issue, the record is void of any quantitative showing that SCs, particularly SCs for system resources, benefit from the incurrence of system MLCC costs.[137] Powerex contends that the record only contains speculative and conclusory statements that all market participants benefit from a reliable grid.[138] Powerex claims that, instead, the vast majority of benefits from the must-offer process will accrue to load that is internal to the CAISO Control Area. Finally, Powerex argues that the CAISO's proposal creates uncertainty for importers.

51. Powerex contends that the rejection of its alternative proposal is not supported by the record and is inconsistent with cost causation principles. Powerex argues that, by recognizing that the CAISO makes its must-offer unit commitment decisions in the day before the operating hour and based on information available to the CAISO at that point, its proposal would assign costs from this day-ahead process to load serving entities' day-ahead scheduling activity. Powerex states that its proposal would allocate system MLCC costs to the SCs that actually cause the CAISO to commit must-offer generation (i.e., to the load and demand that do not accurately schedule in the day-ahead market).[139] Powerex claims that its proposal would provide a valuable incentive for SCs to forecast their day-ahead scheduled load more accurately in the day-ahead timeframe. Powerex

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[135] *Id*. at 14-15 (citing Exh. PWX-2 at 6-7; Tr. at 533:4-6, 534:6-9).

[136] *Id*. at 10, 15 (citing Tr. at 1509:19-23).

[137] *Id*. at 16 (citing Opinion, 117 FERC ¶ 61,348 at P 18).

[138] *Id*. (citing CAISO Post-Hearing Initial Brief, Docket Nos. ER04-835-000 and EL04-103-000, at 10-13 (Aug. 16, 2005) (CAISO Post-Hearing Initial Brief)).

[139] *Id*. at 17-18 (citing Exh. PWX-1 at 10:2-19; Exh. PWX-5 at 8:7-10; Tr. at 1485:22-1486:19).

states that its proposal is consistent with the Commission's finding that a 95 percent day-ahead scheduling requirement is an appropriate remedy to address the significant problem of under-scheduling in the CAISO control area.[140]

Commission Determination

52. We will deny Powerex's rehearing request. Powerex maintains that the CAISO's allocation of System MLCC costs has no relation to NNUD and is inconsistent with cost causation principles because it is based on capacity committed in the day-ahead market to meet projected demand and not based on real-time deviations from final schedules. However, the record indicates that the CAISO's day-ahead must-offer commitments are based on day-ahead estimates of the degree to which demand will exceed supply in real-time.[141] If the CAISO determines that resources that were included in load schedules are insufficient to meet projected control area demand requirements for the next operating day, the CAISO will commit additional must-offer resource capacity in the day-ahead timeframe.[142] The CAISO's estimates of control area demand, forecasted a day in advance, are comprised of various types of forecast data including historical, day-ahead, hour-ahead and actual load and weather conditions.[143] Therefore, although this information may be estimated a day in advance of actual operations, the relevant deviations are between final schedules and real-time deliveries.[144] In addition, the fact that must-offer units are committed by the CAISO in the day-ahead time frame for the next operating day does not mean that the unit commitment was based solely, if at all, on the CAISO's projection of day-ahead hourly loads and demands.[145]

53. We also disagree with Powerex's assertion that the CAISO cannot consider NNUD while making must-offer waiver denial decisions in the day-ahead timeframe

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[140] *Id*. at 18 (citing Initial Decision, 113 FERC ¶ 63,017 at P 114; Powerex Brief on Exceptions at 11-15; Exh. PWX-1 at 9:21-23, 10:13-11:2).

[141] *See Id*. at 27:16-20.

[142] *See* Exh. PWX-3 at 4, CAISO Operating Procedure No. M-432C; Exh. S-18 at 18:9-12.

[143] *See* Exh. S-25 at 1, 3.

[144] *See* Exh. PWX-3, CAISO Operating Procedure No. M-432C; Exh. S-18 at 17-18.

[145] *See* Exh. S-18 at 18:13-15.

because NNUD is not known until after the operating hour. The record indicates that generating units committed under the must-offer obligation are among the resources dispatched by the CAISO to respond to real-time NNUD caused by events such as transmission derates and unit outages.[146] We also find that Powerex's claim that there is no evidence that SCs benefit from the incurrence of system MLCC costs is unfounded.[147] The CAISO incurs system MLCC costs when it expects demand to exceed supply, "not in expectation that Day-Ahead import schedules will be under-delivered in real-time."[148] If import schedules are under-delivered in real-time, and any resultant unattended demand is served by generating units committed by the CAISO (even though the units were not expressly committed to address the import deviation), it is reasonable for NNUD to bear a portion of those minimum load costs.[149] Therefore, we continue to find that the amount of NNUDs that a SC incurs is an appropriate quantity upon which to base the allocation of system MLCC.

54. Powerex has claimed that the CAISO's proposal creates uncertainty for importers, but it has not provided an explanation or references to the record to support this assertion. As a result, we are not able to definitively respond to this argument. To the extent that Powerex is concerned with the financial impact the allocation methodology will have on its transactions, because the charges are after-the-fact, we agree with the judge's finding that such uncertainty is an unavoidable consequence of the market design.[150] Such uncertainty is not a sufficient reason to allocate MLCC costs under a different methodology. Powerex's alternative proposal, to a degree, suffers from the same deficiency. Finally, because we continue to find that the CAISO's proposal is just and reasonable, we will not consider Powerex's alternative proposal.[151] Accordingly, we deny Powerex's rehearing request.

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[146] *See* Exh. PWX-2 at 7.

[147] We note that Powerex has not cited to any record evidence to support this assertion. *See* Powerex Rehearing Request at 16.

[148] Exh. PWX-2 at 6.

[149] *See Id*. at 6-7.

[150] *See* Initial Decision, 113 FERC ¶ 63,017 at P 112 n.74.

[151] *See Cal. Indep. Sys. Operator Corp.*, 111 FERC ¶ 61,337, at P 27 (2005).

2. Other Issues

a. Whether Start-Up and Emissions Costs of Units Denied Must-Offer Waivers Should be Allocated in the Same Manner as Those Associated with MLCC and Whether Revisions to the Allocation of These Costs Should be Addressed in This Proceeding? (Issue No. 14)

Initial Decision and Opinion No. 492

55. In the Initial Decision, the judge found that the Commission had not set the allocation of start-up and emissions costs for hearing and that therefore the issue was beyond the scope of this proceeding.[152] In the Opinion, the Commission reversed the judge's finding.[153] The Commission determined that the PG&E Complaint Hearing Order set for hearing the allocation of all must-offer obligation costs (MLCC, start-up, and emissions), not just MLCC.[154] The Commission also found that its precedent supported a determination that all three costs associated with the must-offer obligation must be allocated consistently.[155] The Commission found that the record established that the CAISO has the data available to allocate these costs in a manner consistent with MLCC costs.[156] Accordingly, the Commission required the CAISO to allocate emissions and start-up costs in proportion and in a similar manner to MLCC costs.[157]

Rehearing Requests

56. On rehearing, Powerex argues that the Commission's precedent does not require that start-up and emissions costs be allocated consistent with MLCC costs.[158] Powerex

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[152] *See* Opinion, 117 FERC ¶ 61,348 at P 91.

[153] *Id*. P 96.

[154] *Id*. (citing PG&E Complaint Hearing Order, 108 FERC ¶ 61,017 at P 16).

[155] *Id*. P 98.

[156] *Id*.

[157] *Id*.

[158] Powerex Rehearing Request at 3 (citing December 2001 Order, 97 FERC ¶ 61,293 (2001); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 107 FERC ¶ 61,166, *clarified*, 108 FERC ¶ 61,219, *order on reh'g*, 108 FERC ¶ 61,311 (continued…)

argues that the Commission has not held that, if the allocation methodology changed for one type of cost, then the CAISO was required to apply the revised methodology to the other costs as well. Powerex underscores this point by noting that the Commission has directed a change to the cost allocation of start-up fuel costs but has not directed similar changes to the allocation of emissions or MLCC costs.[159]

57. Powerex also contests the Commission's determination that the allocation of start-up and emissions costs are within the scope of this proceeding. First, Powerex notes that the CAISO did not seek to revise the allocation of those costs in Amendment No. 60.[160] Second, Powerex argues that, although the PG&E complaint asked the Commission to examine whether the "must-offer costs" were just and reasonable, the thrust of the complaint concerned the allocation of MLCC costs without discussing start-up and emissions costs. Third, Powerex states that the Commission's July 8, 2004 Orders on Amendment No. 60 and the PG&E complaint did not include any specific discussion of start-up and emissions costs, other than a reference to the general category of must-offer obligation costs.[161]

58. Finally, Powerex disputes the Commission's determination that the CAISO has the data available to allocate these costs in a manner consistent with MLCC costs. Powerex contends that the CAISO has indicated that the allocation of start-up and emissions costs would be infeasible, difficult to verify and otherwise problematic. In particular, Powerex notes that the CAISO has stated that it would be problematic to allocate emissions costs consistent with MLCC costs because the CAISO cannot isolate emissions cost data submitted by scheduling coordinators; and, even if the emissions costs could be segregated, they would be difficult to verify.[162] Powerex adds that, while the CAISO technically could implement a revision to its allocation of start-up costs, it does not currently have the capability to assign start-up costs that correspond to or are consistent

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(2004), *order on reh'g*, 110 FERC ¶ 61,293 (2005), *reh'g denied*, 114 FERC ¶ 61,223 (2006)).

[159] *Id*. at 20 (citing *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 107 FERC ¶ 61,166 at P 62-63).

[160] *Id*. at 7 (citing Exh. ISO-1 at 21:17-22:5).

[161] *Id*. (citing PG&E Complaint Hearing Order, 108 FERC ¶ 61,017 at P 1).

[162] *Id*. at 8 and 21 (citing Exh. ISO-19 at 19:16-20:11; Tr. at 836-42; Tr. at 756:18-19, 757:11-12).

with MLCC costs.[163] Powerex argues that, as a result, if the CAISO were to allocate start-up costs under Amendment No. 60, they would have no relationship to the actual start-up costs of the particular units that were paid the minimum load compensation costs. Powerex adds that, even if the CAISO allocates start-up costs consistently with MLCC costs, such an allocation would not represent reality and thus would defeat the purpose of having consistent allocation methodologies.

59. The CAISO requests clarification that the Opinion permits it to use "estimated" start-up and emissions cost data in the proportional allocation. The CAISO explains that it does not have the actual data available for calculating start-up and emissions costs because, unlike MLCC costs, the CAISO does not have true start-up and emissions costs figures until up to a year after the cost is incurred when it receives a bill from the generating unit owner who incurred the costs.[164] The CAISO states that, as a result, it will have to use projected or estimated total costs to allocate start-up and emissions cost in proportion to MLCC costs.[165] The CAISO notes that the Opinion did not state whether the CAISO could use estimated start-up and emissions cost data in the proportional allocation mechanism directed therein. The CAISO seeks clarification that it is permitted to do so.

60. Alternatively, the CAISO requests rehearing on this issue because it is not possible for it to use actual start-up and emissions figures to calculate the proportional share of such costs to allocate to market participants. The CAISO states that only through a manual, labor-intensive effort would it be able to determine the purpose of each start-up in the case of units that are on for a month or more at a time. The CAISO also states that, although it can determine emissions costs in a manner proportional to the megawatt hours in question, the receipt of invoices for emissions a year after the cost are incurred will require a "re-allocation" based on actual figures. The CAISO contends that such a "re-allocation" would be akin to doing a re-run of the cost allocation of start-up and emissions costs every month. The CAISO argues that the cost and effort of such

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[163] *Id*. at 21-22 (citing Exh. ISO-19 at 19:4-11).

[164] The CAISO notes that, in contrast, it calculates and pays MLCC based on heat rate on the normal CAISO payment calendar.

[165] CAISO Rehearing Request at 16-17 (citing Tr. 836). The CAISO points out that PG&E and SWP have proposed mechanisms for allocating start-up and emissions costs in proportion to MLCC costs. *Id*. at 15-16 (citing Exh. PGE-4 at 6; Exh. SWP-1 at 40).

workaround would not be justified because these costs are relatively small compared to MLCC costs[166] and the must-offer mechanism is not a permanent CAISO market design feature.

Commission Determination

61. We disagree with Powerex's assertions. First, PG&E raised the issue of all must-offer obligation costs, not just MLCC costs, in its complaint when it asserted that "the allocation by the CASIO to PG&E of Must Offer Obligation (MOO) costs, including [MLCC] costs … is unjust, unreasonable and unduly discriminatory."[167] If PG&E had intended to raise concerns with MLCC costs only, it would have only mentioned MLCC costs. By touching upon "must-offer obligations costs, including MLCC costs," it indicated that the scope of its concerns went beyond MLCC costs to must-offer obligations costs in general. Must-offer obligation costs consist of start-up, emissions and MLCC costs.[168] Therefore, the CAISO's allocation of start-up and emissions costs was part of its complaint. In addition, in the PG&E Complaint Hearing Order, the Commission identified the CAISO's current allocation of must-offer obligation costs as a material issue of fact set for hearing. Again, if the Commission had intended to limit the scope of the hearing to the CAISO's current allocation of MLCC costs, it would have stated so. Instead, by stating that the broader category of must-offer obligation costs would be reviewed, it indicated that the current allocation of start-up, emissions and MLCC costs was a material issue of fact set for hearing.[169] Finally, even if the CAISO did not seek to revise the allocation of emissions and start-up costs in Amendment No. 60 because those costs were relatively small,[170] the allocation of those costs became an issue that had to be considered under Amendment No. 60 when the Commission consolidated the PG&E complaint proceeding with the Amendment No. 60 proceeding.[171]

62. Second, contrary to Powerex's assertion, since the establishment of the must-offer obligation program, the Commission has required the CAISO to allocate in a consistent

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[166] *Id*. at 18 n.13 (citing Exh. ISO-1 at 22:2-5).

[167] PG&E Complaint, Docket No. EL04-103-000, at 1 (May 18, 2004).

[168] *See supra* note 6.

[169] *See* PG&E Complaint Hearing Order, 108 FERC ¶ 61,017 at P 16.

[170] *See* Exh. ISO-1 at 21:19-22:5.

[171] *See* PG&E Complaint Hearing Order, 108 FERC ¶ 61,017 at P 1.

manner all three costs associated with must-offer generators. Specifically, in a June 19, 2001 Order, the Commission stated that "[s]ellers will invoice the [CAISO] their actual start-up fuel costs for recovery by the [CAISO] in the same manner that emissions costs are recovered, and the [CAISO] must pay these invoices."[172] Also, in the December 2001 Order, the Commission stated that the CAISO should recover MLCC costs "consistent with the methodology utilized for the recovery of emissions and start-up fuel costs."[173] Through this precedent, the Commission has sought to ensure that all costs associated with the must-offer obligation would be recovered in a consistent manner, and we continue to support this approach. Therefore, any change to the MLCC cost allocation methodology requires a similar change to the allocation of start-up and emissions costs. Powerex's reference to the Commission's order in the California refund proceeding regarding the fuel cost allowance for spot-market gas purchases made for spot-market energy sales[174] is inapposite. In that proceeding, the Commission found that a fuel cost allowance did not have to be allocated in the same manner as emissions costs offsets because the fuel costs at issue were substantially different in nature from the emissions costs discussed therein.[175] That difference is not present here because, in the California refund proceeding, the fuel cost allocation was based on consumption of energy and thus it was appropriate to assign those costs to the entities that relied on the energy sales to serve load. However, due to the nature of emissions costs and its relation to the reliability of the CAISO grid, it was appropriate that emissions costs be assessed against all in-state load served on the CAISO's transmission system. In this proceeding, both start-up and emissions costs are part of the must-offer obligation in which all costs are incurred for reliability purposes and should therefore be allocated in the same manner. Therefore, the Commission's order in the California refund proceeding does not control our determination here. For these reasons, we deny Powerex's rehearing request.[176]

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[172] June 2001 Order, 95 FERC ¶ 61,418 at 62,563.

[173] December 2001 Order, 97 FERC ¶ 61,293 at 62,363.

[174] *See supra* P 56 n.159.

[175] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 107 FERC ¶ 61,166 at P 62-63.

[176] Powerex's concerns regarding the availability of the data necessary to allocate the start-up and emissions costs in a manner consistent with MLCC costs are addressed by the clarification we provide below on this issue. As a result, we find that this rehearing request is now moot.

63. In response to the CAISO's request for clarification, we clarify that the CAISO may use estimated cost data when allocating emissions and start-up costs in a similar and proportional manner to MLCC costs. A requirement to use actual costs would be burdensome and could result in billing delays. The estimates are reasonable approximations for an allocation process, and no one has shown that the estimates are unreliable or produce unreasonable results.[177] In the Opinion, the Commission noted that both PG&E and SWP proposed similar mechanisms for categorizing and allocating emissions and start-up costs in the same proportion as MLCC costs.[178] Additionally, in the Opinion, the Commission noted that the CAISO stated that it had data available to allocate these costs in a manner consistent with MLCC costs.[179] However, the Commission failed to observe that the CAISO had testified that this allocation could be implemented easily only if the CAISO used cost estimates.[180] We find it reasonable for the CAISO to use estimated costs rather than actual costs in this circumstance. With this clarification, we find that the CAISO's alternative request for rehearing is now moot.

b. Does the CAISO Have the Authority to Commit a Generating Unit Under the Must-Offer Obligation to Provide Ancillary Services? (Issue No. 18)

Initial Decision and Opinion No. 492

64. In the Initial Decision, the judge found that the CAISO had not established that it had authority to commit must-offer generators to provide ancillary services.[181] The judge stated that the CAISO sought to grant itself authority to commit must-offer generation to provide ancillary services by citing Amendment No. 60.[182] The judge stated that the

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[177] When the actual data for start-up and emissions costs becomes available, the CAISO must reconcile with market participants any differences between the estimated costs initially recovered and the actual costs incurred by the CAISO.

[178] Opinion, 117 FERC ¶ 61,348 at P 97 (citing Exh. PGE-4 at 6; Exh. SWP-1 at 40).

[179] *Id*. (citing Tr. at 842:17); *see also* Tr. at 836:1-11.

[180] *See* Tr. at 836: 1-6.

[181] Opinion, 117 FERC ¶ 61,348 at P 104 (citing Initial Decision, 113 FERC ¶ 63,017 at P 138).

[182] *Id*.

CAISO should not be permitted to circumvent and expand the ancillary services market by abusing the must-offer obligation to force generators to have no rational choice but to offer into the market.[183]

65. In the Opinion, the Commission affirmed the judge's findings. The Commission concluded that the current must-offer obligation tariff provisions did not include the authority to commit a generating unit to provide ancillary services or to deny an exemption from the must-offer obligation in anticipation of a shortage of ancillary services.[184] The Commission found that, in order for the CAISO to deny must-offer obligation waivers in anticipation of a shortage of ancillary services, the CAISO would need to file a tariff amendment pursuant to FPA section 205 proposing such authority,[185] which would then require Commission approval.

Rehearing Request

66. The CAISO argues that it was contradictory to find that: (1) the CAISO has sole discretion to grant exemptions from the must-offer requirement, which pursuant to CAISO Tariff section 5.11.6 should provide sufficient on-line generating capacity to meet operating reserve requirements but that (2) the CAISO does not have authority to deny exemptions from the must-offer obligation in anticipation of a shortage of operating reserves (i.e., a shortage of certain ancillary services).[186] The CAISO claims that CAISO Tariff section 5.11.6 expressly provides that the CAISO should not grant (i.e., should deny) a must-offer waiver if the CAISO believes that there will be a shortage of certain ancillary services that will prevent the CAISO from meeting operating reserve requirements. The CAISO contends that, in the Opinion, the Commission has

[183] *Id*.

[184] *Id*. P 110-11.

[185] *Id*. P 111.

[186] The CAISO notes that, under the CAISO Tariff, "operating reserves" are defined as the combination of spinning and non-spinning reserves required to meet WECC and NERC requirements for reliable operations of the CAISO Control Area. The CAISO adds that, under the WECC Minimum Operating Reliability Criteria, operating reserves are the equivalent of the CAISO's regulation, spinning reserves and non-spinning reserve ancillary services. CAISO Rehearing Request at 7 n.8 (citing Tr. 737).

substantially limited its discretion to grant exemptions by rejecting the CAISO's authority to deny must-offer waiver requests in anticipation of a shortage of operating reserves.

67. The CAISO states that, in Amendment No. 60, it simply moved the previously accepted language concerning granting and denying must-offer waivers from section 5.11.6[187] to section 5.11.6.2.[188] The CAISO argues that, because CAISO Tariff section 5.11.6.2 was accepted and not set for hearing in the Amendment No. 60 Hearing Order, it was proper to continue to rely on this language to deny must-offer waiver requests in anticipation of operating reserve shortages.[189] The CAISO contends that, in the Opinion, the Commission improperly rejected the CAISO's authority under current CAISO Tariff language to deny exemptions from the must-offer obligation to provide sufficient on-line generating capacity to meet operating reserve requirements. According to the CAISO, the Commission erred because it did not find, pursuant to FPA section 206, that the Commission-accepted tariff language had become unjust, unreasonable, unduly discriminatory or preferential.

68. The CAISO argues that it has never asserted that the must-offer requirement authorizes it to compel generating units to submit bids into the ancillary services markets nor has it directed a resource to submit bids. The CAISO states that, consistent with Commission precedent,[190] if a generating unit has been denied a must-offer waiver to allow the CAISO to ensure sufficient on-line generating capacity to meeting operating reserve requirements and does not bid into the ancillary services markets, the CAISO has

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[187] The CAISO states that the Commission accepted this language on May 15, 2002. *Id*. at 10 (citing May 2002 Order, 99 FERC ¶ 61,158, at 61,630). The CAISO notes that, subsequent to the filing of Amendment No. 60, this language was moved to CAISO Tariff section 40.9. *Id*. at 5 n.4, 10.

[188] The CAISO states that the language that was moved states that "[t]he [CAISO] shall grant waivers so as to: (1) provide sufficient on-line generating capacity to meet operating reserve requirements; and (2) account for other physical operating constraints, including Generating Unit minimum up and down times." *Id*. at 5.

[189] *Id*. at 10 (citing Amendment No. 60 Hearing Order, 108 FERC ¶ 61,022 at Order Paragraph (A)) and 13 n.12 (citing Opinion, 117 FERC ¶ 61,348 at P 111 ("In the Amendment No. 60 Hearing Order, the Commission accepted the transfer of this authority from CAISO tariff section 5.116 to section 5.11.6.2.")).

[190] *Id*. at 9-10 (citing May 2002 Order, 99 FERC ¶ 61,158 at 61,630).

the option of calling upon the generating unit for energy under the must-offer obligation or as needed to address system emergency conditions under the CAISO Tariff. According to the CAISO, this includes situations that might arise due to insufficient operating reserves.[191] The CAISO contends that this ability to call upon a generating unit does not mean that the CAISO's authority to deny must-offer waiver requests compels such generating units to bid into the ancillary services markets.

69. The CAISO claims that, in the Opinion, the Commission substantially narrowed the scope of the must-offer obligation in the CAISO Tariff by requiring that the CAISO grant exemptions from the must-offer obligation in all circumstances, except when the CAISO anticipates that it will need energy in real-time from a generator subject to the obligation. The CAISO asserts that this directive is contrary to the broad scope of the must-offer obligation. The CAISO states that there is no provision in the CAISO Tariff requiring the CAISO to deny waivers for any particular reason because generators are not entitled to waivers under specific circumstances. The CAISO argues that, because the grant of waivers is at the CAISO's sole discretion, subject to Commission oversight,[192] the CAISO does not need specific authority to decline to exercise its discretion to grant a waiver; it only needs to exercise its discretion in a reasonable and non-discriminatory manner.

70. Unless it elects to grant a waiver, the CAISO asserts that the must-offer obligation applies to every generator, except hydroelectric units, at all times regardless of whether the CAISO identifies a need for the resource. The CAISO further argues that the must-offer obligation applies even if a resource is not needed for either energy or ancillary services. The CAISO states that a finding that the CAISO does not have the authority to deny waivers in anticipation of a shortage of ancillary services would make sense only if the must-offer obligation applied solely to the resources that the CAISO concludes would be required to generate energy in real-time. The CAISO contends that such an interpretation would prevent the CAISO from using the must-offer obligation to fulfill one of its original purposes: providing the CAISO adequate capacity to help meet operating requirements.[193]

71. If the Commission did not intend these adverse effects, the CAISO requests that the Commission clarify that the Opinion does not prevent the CAISO from taking into

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[191] *Id*. at 9 (citing CAISO Tariff section 7.4).

[192] *Id*. at 11 (citing May 2002 Order, 99 FERC ¶ 61,158 at 61,630).

[193] *Id*. at 12 (citing May 2002 Order, 99 FERC ¶ 61,158 at 61,630).

account the need for generating capacity to meet operating reserve requirements in determining whether to grant must-offer waivers. To this end, the CAISO suggests adding "other than an anticipated shortage of operating reserves" to the end of the existing CAISO Tariff language. If amended as suggested, the provision would state that the CAISO does not have the authority under the must-offer provisions of the CAISO Tariff to: (1) require any generating unit to bid into the CAISO's ancillary services markets or (2) deny a requested exemption from the must-offer obligation in anticipation of a shortage of ancillary services *other than an anticipated shortage of operating reserves*. The CAISO agrees that it does not require the authority to deny a waiver from the must-offer obligation in anticipation of a shortage of ancillary services other than an anticipated shortage of operating reserves.

Commission Determination

72. We will grant the CAISO's request for clarification. The CAISO is correct that the must-offer obligation was designed to ensure that the CAISO would be able to call upon available resources in the real-time market to the extent that energy is needed and to provide adequate capacity to help meet operating requirements.[194] The tariff language that implemented the must-offer obligation states that exemptions will be granted so as to provide sufficient on-line generating capacity to meet operating reserve requirements and to account for other physical operating constraints of generating units.[195] We find that the proposed tariff language, which clarifies that the CAISO can use the must-offer obligation for an anticipated shortage of operating reserves, is consistent with the objective set by the Commission when the obligation was established: to ensure the adequate operation of the grid and adequate resources to meet interruptible and firm load.[196] We note that the proposed tariff language is also consistent with CAISO Operating Procedure No. M-432 related to must-offer waivers, which became effective December 13, 2002.[197] Specifically, CAISO Operating Procedure No. M-432 includes Waiver Evaluation Guidelines, which include: (1) to serve all interruptible and firm load based on day-ahead load forecasts and expected imports, and (2) to satisfy WECC

[194] May 2002 Order, 99 FERC ¶ 61,158 at 61,630; April 2001 Order, 95 FERC ¶ 61,115 at 61,355-6; *see also* December 2001 Order, 97 FERC ¶ 61,293 at 62,363.

[195] May 2002 Order, 99 FERC ¶ 61,158 at 61,630.

[196] May 2002 Order, 99 FERC ¶ 61,158 at 61,630; *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 99 FERC ¶ 61,159 at 61,640.

[197] *See* CAISO Data Response Attachment, Docket No. EL00-95-063 (Mar. 25, 2003).

Minimum Operating Reserve Criteria Operating Reserve, based upon day-ahead load forecasts and expected imports.[198] For these reasons, we will grant the CAISO's requested clarification and find that its proposed tariff language, as described above, is just and reasonable. We direct the CAISO to make a compliance filing, within 30 days of the date of this order, with this tariff modification.

c. Whether the Refund Effective Date of July 17, 2004 Should be Conditioned in Any Way (Issue No. 21)

Initial Decision and Opinion No. 492

73. In the Initial Decision, the judge found that, although the CAISO did not object to a July 17, 2004 refund effective date, the net incremental local costs should not be used to calculate refunds from July 17, 2004 to September 30, 2004.[199] In the Opinion, the Commission noted that the judge did not explain why net incremental local costs should not be used during the July 17 – September 30, 2004 time period, which raised the question of how refunds would be calculated during that period.[200] The Commission explained that the CAISO had proposed an October 1, 2004 effective date for the Amendment No. 60 methodology, in part, because the software needed to calculate the net incremental local costs (i.e., the SCUC) would not be available until September 3, 2004.[201] Subsequently, the CAISO signed Stipulation No. 3, which stated that, as of July 17, 2004, it was no longer just and reasonable to allocate the entirety of MLCC costs system-wide.[202]

74. In the Opinion, the Commission affirmed both the July 17, 2004 and the October 1, 2004 dates.[203] The Commission found that the July 17, 2004 stipulated date for the proposed allocation of must-offer related charges under Amendment No. 60 was just and reasonable because the CAISO was the filing party and a signatory to Stipulation

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[198] *Id*. at 5.

[199] Opinion, 117 FERC ¶ 61,348 at P 115.

[200] *Id*.

[201] *Id*.; *see also* Exh. ISO-1 at 38:7-44:4.

[202] *See* Stipulation No. 3, Docket Nos. ER04-835-000 and EL04-103-000 (July 29, 2005).

[203] Opinion, 117 FERC ¶ 61,348 at P 123.

No. 3.[204] The Commission also found that refunds related to the net incremental cost of local component of the CAISO's proposal should commence on October 1, 2004 because the software for that calculation was not in place until that time.[205] The Commission also clarified that, because it was not necessary to use the CAISO's proposed SCUC proxy methodology,[206] that methodology was rejected.[207]

Rehearing Request

75. On rehearing, SoCal Edison argues that a July 17, 2004 date is inappropriate because the SCUC-based methodology used to calculate the incremental cost of local could not be implemented until October 1, 2004. SoCal Edison contends that the Commission made vague references to FPA sections 205 and 206 and Trial Staff's unsupported assertions when it found that Stipulation No. 3 resolved this issue. SoCal Edison asserts that the Commission can only adopt a stipulation lacking unanimity, such as Stipulation No. 3, if it "makes an independent finding supported by 'substantial evidence on the record as a whole.'"[208] SoCal Edison argues that the Commission failed to make such a finding here.

76. SoCal Edison also contends that the Commission ignores evidence presented at hearing that, contrary to Stipulation No. 3, the CAISO's method of allocating MLCC costs before October 1, 2004 for Amendment No. 60 was just, reasonable and not unduly discriminatory given the data available at the time. SoCal Edison claims that it is undisputed that significant data problems pre-October 1, 2004 prevented the CAISO from implementing Amendment No. 60 before October 1, 2004.[209] SoCal Edison argues that

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[204] *Id*.

[205] *Id*.

[206] *See* Exh. ISO-1 at 40:17-44:4.

[207] Opinion, 117 FERC ¶ 61,348 at P 123.

[208] SoCal Edison Rehearing Request at 13 (citing *Mobil Oil Corp. v. Federal Power Comm'n*, 417 U.S. 283, 312-14 (1974)).

[209] *Id*. at 13-14 (citing Trial Staff Post-Hearing Initial Brief, Docket Nos. ER04-835-000 and EL04-103-000, at 35-36 (Aug. 16, 2005) (Trial Staff Post-Hearing Initial Brief) ("Additionally, Trial Staff has some concerns and misgivings, however, as to how the ISO intends to ensure that the incremental cost calculations are accurate given that there is a lack of transparency to the SCUC data and *given the many data problems the ISO experience in compiling MLCC costs*.") (emphasis added); Southern Cities Post-

(continued…)

the Commission should not rely on Trial Staff's contention that implementing Amendment No. 60 as of July 17, 2004 without the net incremental cost of local methodology would alleviate SoCal Edison's concern regarding the CAISO's ability to accurately and reasonably implement the incremental cost approach to determine the local MLCC cost from July 17, 2004 through September 30, 2004. SoCal Edison argues that, instead, the Commission should alleviate SoCal Edison's concerns by retaining the October 1, 2004 date, which will ensure that SoCal Edison will not be unfairly charged costs logged as local that should be spread system-wide. SoCal Edison adds that, because the Commission has found that the net incremental cost of local methodology is just and reasonable, the implementation of an MLCC cost allocation approach that does not incorporate that methodology cannot be just and reasonable.

77. If the Commission adopts the July 17, 2004 date, SoCal Edison argues that the Commission should order the CAISO to use the proxy net incremental cost of local methodology, even if imperfect,[210] from July 17, 2004 through September 30, 2004 because it will shift some of the system-wide costs out of the local bucket, thus reducing some of the unwarranted system costs SoCal Edison will otherwise unjustly and unreasonably incur. SoCal Edison claims that use of the proxy will address its greatest concern (i.e., the unwarranted costs it will incur if there is no net incremental cost of local methodology for the pre-October 2004 period).

Commission Determination

78. We will deny in part and grant in part SoCal Edison's rehearing request. The Commission established the refund effective date in the PG&E Complaint Hearing Order, in which it consolidated Docket Nos. ER04-835-000 and EL04-103-000.[211] Given the

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Hearing Initial Brief, Docket Nos. ER04-835-000 and EL04-103-000, at 60 (Aug. 16, 2005) (Southern Cities Post-Hearing Initial Brief) ("[R]ampant data problems will preclude an accurate calculation of refunds for the July 17 to October 1, 2004 refund period."); SWP Post-Hearing Initial Brief, Docket Nos. ER04-835-000 and EL04-103-000, at 3-4 (Aug. 16, 2005) (SWP Post-Hearing Initial Brief) ("During this time [in 2004], ISO 'logging data, which had not been collected for cost allocation purposes, were, in many cases, vague, incomplete or inaccurate,"); SWP Post-Hearing Initial Brief at 11 ("As late as September 2004, the ISO had attributed very significant amounts of MLCC costs to 'Unknown Reasons not captured.'")).

[210] SoCal Edison Rehearing Request at 15 (citing Tr. 1198:23-1199:17).

[211] *See* PG&E Complaint Hearing Order, 108 FERC ¶ 61,017 at P 2, 3, 17.

Commission's establishment of the refund effective date in the PG&E Complaint Hearing Order, the Commission's reliance on Stipulation No. 3 in the Opinion was unnecessary. In the PG&E Complaint Hearing Order, the Commission explained that in cases, such as this one, where the Commission institutes an investigation on complaint under FPA section 206, section 206(b) requires the Commission to establish a refund effective date that is no earlier than 60 days after the filing of the complaint but no later than five months subsequent to the expiration of the 60-day period.[212] The Commission determined that, consistent with its general policy of providing maximum protection to consumers, it would set the refund effective date at the earliest date possible (i.e., 60 days after the date of the filing of the complaint or July 17, 2004).[213] Therefore, the Commission has determined that the refund effective date is July 17, 2004.

79. The question before us now is not the date that was earlier established as the refund effective date from which the Commission could order refunds, but rather what should be ordered (i.e., when refunds should begin). The Commission's discretion is at its zenith when it comes to the fashioning of remedies.[214] Furthermore, absent some conflict with the explicit requirements or core purposes of a statute, the courts have refused to constrain the Commission's discretion by imposing a presumption in favor of refunds.[215] The Commission need only show that it considered relevant factors and struck a reasonable accommodation among them and that its order granting or denying refunds was equitable in the circumstances of the litigation.[216]

80. We continue to find that refunds for the proposed allocation of must-offer related charges under Amendment No. 60 should be ordered beginning July 17, 2004, except for the net incremental cost of local methodology. The only evidence that SoCal Edison points` to as support for a finding to the contrary relates to claimed data problems that SoCal Edision states could interfere with the implementation of Amendment No. 60 on July 17, 2004. However, contrary to SoCal Edison's assertion, we do not find that there is any evidence of continuing data problems.

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[212] *Id*. at P 17.

[213] *Id*. (citing *Canal Elec. Co.*, 46 FERC ¶ 61,153 at 61,539, *reh'g denied*, 47 FERC ¶ 61,275 (1989).

[214] *Niagara Mohawk Power Corp. v. FPC*, 379 F.2d 153, 159 (D.C. Cir. 1967).

[215] *Towns of Concord v. FERC*, 955 F.2d 67, 76 (D.C. Cir. 1992).

[216] *Id*. (citations omitted).

81. SoCal Edison provides three citations for its assertion of flawed data.[217] SoCal Edison begins with Trial Staff's concerns regarding the transparency of the SCUC data that will be used to calculate net incremental local costs and the CAISO's past problems compiling MLCC costs.[218] First, we note that, in the Opinion, the Commission directed the CAISO to take steps that will remedy concerns with the transparency, appropriateness and accuracy of the data used.[219] Second, of the evidence cited by Trial Staff to support its concerns, only one piece of evidence relates to data problems that have existed[220] and that testimony refers generally to "the many data problems that have existed."[221] We find this testimony too vague to provide support for SoCal Edison's position. SoCal Edison next quotes an unsupported, conclusory statement by Southern Cities.[222] Not only is the quoted statement unsupported but also the testimony cited by Southern Cities in the second half of that sentence undermines SoCal Edison's position.[223] It states that the CAISO has the data available to reasonably categorize MLCC costs as local, zonal or system during the July 17 to October 1, 2004 period.[224] Third, SoCal Edison points to evidence cited by SWP with respect to data problems. SWP referred to CAISO testimony that logging data that had not been collected for cost allocation purposes were, in many cases, vague, incomplete or inaccurate.[225] We note that, in that same testimony, the CAISO filed to eliminate this incorrect data.[226] In addition, SWP alleged that

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[217] SoCal Edison Rehearing Request at 14 n.48.

[218] *Id*. (citing Trial Staff Post-Hearing Initial Brief at 35-36).

[219] Opinion, 117 FERC ¶ 61,348 at P 49.

[220] *See* Trial Staff Post-Hearing Initial Brief at 36 (citing Exh. S-30 at 8:8-14).

[221] *See Id*.

[222] *See* SoCal Edison Rehearing Request at 14 n.48 (citing Southern Cities Post-Hearing Initial Brief at 60 ("[R]ampant data problems will preclude an accurate calculation of refunds for the July 17 to October 1, 2004 refund period.")).

[223] *See* Southern Cities Post-Hearing Initial Brief at 60 (citing Exh. S-18 at 29:17-19).

[224] *See Id*.

[225] *See* SoCal Edison Rehearing Request at 14 n.48 (citing SWP Post-Hearing Initial Brief at 3-4 (quoting Exh. ISO-20 at 5:4-5)).

[226] *See* Exh. ISO-20 at 5:5-6:13, 46:6-47:18; *see also* Exh. ISO-19 at 11:13-16.

evidence indicated that, as late as September 2004, the CAISO had attributed very significant amounts of MLCC costs to "unknown reasons not captured."[227] We note, however, that SWP's witness later testified that the data problems had been resolved sufficiently, except with regard to dual categorization and implementation of net incremental local costs prior to October 1, 2004.[228] As for dual categorization, in the Opinion, the Commission affirmed the methodology recommended by the judge for addressing the dual categorization problem (i.e., MLCC costs related to must-offer waivers denied for more than one reason).[229] Therefore, the only data issue remaining relates to the fact that the SCUC software used for calculating the net incremental cost of local was not available until September 3, 2004. This lack of SCUC data, which is addressed below, is a separate issue from the alleged flawed data because absence of data is different from data flaws. For these reasons, we do not find SoCal Edison's allegations of flawed data convincing. Therefore, we deny SoCal Edison's rehearing request regarding the date when we should order refunds under Amendment No. 60 to begin.

82. As for the refunds associated with the net incremental cost of local methodology, we have two options before us: (1) order refunds from October 1, 2004 because the first full month of SCUC data was available in October 2004[230] or (2) accept the proxy methodology proposed by the CAISO for the period from July 17 to October 1, 2004, which would permit us to order refunds from July 17, 2004. SoCal Edison has changed its position on the CAISO's proxy methodology. Initially, SoCal Edison argued that the proxy was not a reasonable substitute for a SCUC-based determination of costs.[231] SoCal Edison now requests that, if we order refunds back to July 17, 2004 for Amendment No. 60, we order the CAISO to use the proxy incremental cost of local methodology, even if imperfect, from July 17, 2004 through September 30, 2004 because it will shift some of the system-wide costs out of the local bucket, thus reducing some of the unwarranted system costs SoCal Edison will otherwise unjustly and unreasonably incur.

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[227] *Id*. (citing SWP Post-Hearing Initial Brief at 11 (citing Exh. SWP-3P at 14)).

[228] *See* Exh. SWP-18 at 34:15-36:6; *see also* Tr. at 1201:6-1202:3.

[229] *See infra* P 84.

[230] *See* Exh. PGE-6 at 6:6-7; Tr. at 335:15-17.

[231] *See* SoCal Edison Brief on Exceptions, Docket Nos. ER04-835-000 and EL04-103-000, at 16-17 (Nov. 30, 2005) (SoCal Edison Brief on Exceptions); SoCal Edison Brief Opposing Exceptions, Docket Nos. ER04-835-000 and EL04-103-000, at 16-18 (Dec. 20, 2005) (SoCal Edison Brief Opposing Exceptions).

Given SoCal Edison's change of position on the proxy methodology and the CAISO's conclusion that the proxy allocation methodology would be superior to the pre-Amendment No. 60 alternative,[232] we no longer reject the use of the proxy methodology. Therefore, we grant rehearing and order refunds from July 17, 2004 for the net incremental cost of local methodology and direct the CAISO to use its proposed proxy incremental cost of local methodology from July 17, 2004 through September 30, 2004.

d. How Should the CAISO Treat MLCC Costs Related to Must-Offer Waivers Denied for More Than One Reason? (Issue No. 12)

83. The CAISO records the reason a must-offer generator is committed, including a reference to the specific constraint addressed, in its logging system called Scheduling and Logging for ISO of California (SLIC).[233] A proper entry would reference only one constraint.[234] Between July 17 and August 26, 2004, the CAISO sometimes improperly referenced two constraints in the same entry.[235] These dual categorizations were problematic if they implicated more than one cost allocation category.[236]

Initial Decision and Opinion No. 492

84. In the Initial Decision, the judge found that it would be difficult and resource-intensive to attempt to determine the appropriate classification category for the improper entries.[237] The judge stated that no participant opposed the proposal made by the CAISO, Trial Staff, SWP and SoCal Edison to allocate the costs 50/50 between categories.[238] The

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[232] *See* CAISO Post-Hearing Initial Brief at 30.

[233] *See* Exh. ISO-1 at 41:10-11; Exh. ISO-22 at 41:10-11.

[234] Initial Decision, 113 FERC ¶ 63,017 at P 130.

[235] *Id*. at P 130 (citing Exh. SWP-18 at 38:15-22 (protected)); *see also* CAISO Post-Hearing Initial Brief at 38 (citing Exh. SWP-18 at 34); Exh. SWP-18 at 38:5-12 (protected).

[236] CAISO Post-Hearing Initial Brief at 39.

[237] Initial Decision, 113 FERC ¶ 63,017 at P 131.

[238] *Id*.

judge concluded that, under the circumstances, it was reasonable to adopt the 50/50 dual allocation process.[239] In the Opinion, the Commission summarily affirmed the judge's finding.[240]

Rehearing Request

85. On rehearing, Southern Cities contradict the judge's statement that they did not oppose the 50/50 allocation in their Pre- and Post-Hearing Briefs.[241] Southern Cities also raised this issue in its Brief on Exceptions.[242] Southern Cities argue that the CAISO should allocate dual local/zonal costs to the local category because the CAISO's operating procedures dictate that local constraints must be resolved before zonal constraints.[243] Southern Cities request that the Commission reverse its summary affirmation of the proposal to allocate dual-category costs equally between the two categories, instead of allocating those costs to the local category only.

86. In its Brief Opposing Exceptions, Trial Staff responded that the fact that the CAISO addresses local requirements first is not an indication that it is the most likely reason for the constraint.[244] Trial Staff added that, given the data problems that the CAISO has experienced, it would be difficult for the CAISO to go back to the period

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[239] *Id*.

[240] Opinion, 117 FERC ¶ 61,348 at P 8.

[241] Southern Cities Rehearing Request at 14 (citing Pre-Hearing Brief at 27-28; Southern Cities Post-Hearing Initial Brief at 48-49). Southern Cities also raised this issue in its Brief on Exceptions. Southern Cities Brief on Exceptions, Docket Nos. ER04-835-000 and EL04-103-000, at 26-27 (Nov. 30, 2005).

[242] *Id*.

[243] Southern Cities Rehearing Request at 14 (citing Exh. SOC-63 at 3 (the CAISO "determines its generation requirements for SP 15 beginning with the most local constraints, then the more regional constraints . . . then finally the SCIT nomogram")).

[244] Trial Staff Brief Opposing Exceptions at 7, 89.

between July 17 and August 26, 2004 to ascertain the most accurate reason for the constraint.[245] Therefore, Trial Staff argued that it was more equitable and reasonable to divide those costs equally between the local and zonal categories.[246]

Commission Determination

87. We disagree with Southern Cities' assertion that the MLCC costs incorrectly logged as being caused by both a local and a zonal constraint should be allocated to the local cost allocation category, based upon Southern Cities' interpretation of the CAISO's operating procedures. There is no evidence in the record to support the interpretation that the CAISO operating procedures require that local constraints must be resolved before zonal constraints. The record only indicates that there were problems collecting accurate data and making correct log entries;[247] it does not indicate that the correct designation would most likely have been a local constraint because the CAISO resolves local constraints before zonal constraints. Given that it would be difficult for the CAISO to re-categorize the costs for this period[248] and the fact that the dual allocation problem spanned a limited period of time, we find that the most equitable and reasonable solution is splitting the costs 50/50 between the local and zonal categories. For these reasons, we deny Southern Cities' request for rehearing.

e. Whether non-local MLCC costs should be assessed only to load occurring in the peak time periods for which must-offer waivers are denied (Issue No. 6)

88. SWP proposed to modify Attachment E so that zonal and system MLCC costs would be allocated to the peak period loads for which they are incurred (i.e., time-of-use rates would be implemented).[249] SWP defined peak period loads as occurring Monday through Saturday (excluding holidays) between 1:00 p.m. and 6:00 p.m. in summer and between 3:00 p.m. and 8:00 p.m. in winter.[250] According to SWP, the CAISO conceded

[245] *Id*. (citing Exh. ISO-22 at 44-46; Exh. SWP-18 at 39:4-40:11 (protected)).

[246] *Id*. at 7, 90.

[247] Exh. ISO-19 at 11-12; Exh. ISO-22 at 44-46; Exh. SWP-18 at 33:1-35:9 (protected).

[248] *Id*.; CAISO Post-Hearing Initial Brief at 38-39.

[249] *See* Initial Decision, 113 FERC ¶ 63,017 at P 100.

[250] *See Id*. P 103 (citing Exh. SWP-18, at 15-16).

that, with the exception of Sylmar-related costs, the overwhelming majority of MLCC costs are incurred to meet on-peak needs.[251] SWP also alleges that the CAISO concedes that off-peak MLCC costs are incurred to meet on-peak needs and that all MLCC costs should be allocated to peak period loads—as SWP defines them—as a consequence.[252]

Initial Decision and Opinion No. 492

89. In the Initial Decision, the judge disagreed that the CAISO made the concessions that SWP asserted.[253] First, the judge found that the evidence that SWP cited in support of its assertion confirmed that SWP grossly overstates or purposefully misinterprets the CAISO's position.[254] The judge found that, according to the CAISO, the must-offer obligation is designed "to ensure that the ISO has sufficient capacity reserves to deal with a Contingency,[255] particularly the failure of a major transmission line or Generating Unit. A contingency may occur any hour of the day, off or on peak."[256] Second, the judge found that most MLCC costs actually are incurred in off-peak hours, that a variety of off-peak events and circumstances require the CAISO to commit must-offer generation, and that off-peak loads themselves benefit from both off-peak and on-peak must-offer waiver denials.[257] The judge also found that various *non-load* factors occurring off-peak can contribute to must-offer waiver denials.[258]

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[251] *See Id*.

[252] *See Id*.

[253] *Id*.

[254] *Id*. P 103 (citing Exh. SWP-5D at 1-2; Exh. ISO-22 at 35; Tr. 1637), n.66 (citing Tr. 388-93, 571-75, 1636-38).

[255] The judge noted that the CAISO Tariff defines contingency as a "[d]isconnection or separation, planned or forced, of one or more components from an electrical system." *Id*. n.67 (citing Item by Reference #1, v.1, Substitute Fourth Revised Sheet No. 308).

[256] *Id*. P 103 (citing Exh. ISO-21 at 6).

[257] Id. (citing Exh. ISO-22 at 35; Tr. at 142, 145, 156-58, 182-83, 388-92, 571-75).

[258] *Id*. n.68 (citing Exh. S-45; Tr. at 1170).

90. Third, the judge found that the CAISO does not operate in accordance with anything remotely resembling SWP's proposed peak period definition.[259] The judge found that, instead, the CAISO adheres to the standard North American Reliability Council (NERC) and Western Electricity Coordinating Council (WECC) definitions of peak period for the Western Interconnection: 7:00 a.m. to 10:00 p.m., Monday through Saturday (excluding specified holidays).[260] The judge found no indication that the CAISO deviated from this definition when it prepared the peak hour cost allocation exhibits it submitted in this proceeding,[261] at least two of which[262] SWP itself used to prove the feasibility of its proposal to allocate zonal/system MLCC costs on a daily basis.[263]

91. The judge found that, most importantly, the record did not support the peak period load analysis that laid the foundation for SWP's proposal.[264] The judge concluded that SWP misconstrued the evidence to achieve its objectives.[265] The judge explained that SWP exploited various deposition characterizations of "maximum" on-peak hours, "super" peak, "highest" load hours and "highest" peak to extrapolate to a narrow definition of "peak period loads," which ostensibly reflected the CAISO's own operational demarcations.[266] However, the judge found that the definition was

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[259] *Id*. P 103.

[260] *Id*. (citing Tr. at 146, 149, 387; Exh. S-1 at 10-11; Exh. S-2; Exh. S-3). The judge noted that, unfortunately, counsel and witnesses repeatedly used the term "peak" in a number of different senses before and during the course of the hearing, including as operational shorthand for specific points in time, one to two hour periods, "highest" peak periods of indeterminate hourly durations, particular days, etc. *Id*. n.69. In addition, the judge found that at least one data response creates some ambiguity with respect to whether ISO excludes Sunday from the peak period definition. *Id*. (citing Exh. S-4).

[261] *Id*. P 103 (citing Exh. ISO-9; Exh. ISO-11; Exh. ISO-15).

[262] *Id*. (citing Exh. ISO-11; Exh. ISO-15)

[263] *Id*. (citing SWP Post-Hearing Initial Brief at 25).

[264] *Id*. P 104.

[265] *Id*.

[266] *Id*. (citing Exh. SWP-5 at 20-21; Exh. S-1 at 8-10).

egregiously insufficient and unrepresentative.[267] Therefore, the judge concluded that SWP had failed to satisfy its burden to prove that it would be just, reasonable and not unduly discriminatory for the CAISO to allocate zonal/system MLCC costs as proposed by SWP.[268] The judge also concluded that SWP had failed to prove: (1) that it would be just, reasonable and not unduly discriminatory for the CAISO to deviate from the NERC/WECC definitions of peak period for the Western Interconnection for any purpose; or (2) that it would be just, reasonable and not unduly discriminatory for the CAISO to allocate zonal/system MLCC costs in any manner—other than daily—based on time-of-use.[269]

92. In the Opinion, the Commission summarily affirmed the judge's finding.[270]

Rehearing Request

93. On rehearing, SWP argues that the record establishes that time-sensitive rates to promote demand response shifting load to off-peak periods could reduce the need for must-offer generation, promoting efficiency, enhancing reliability, and producing cost savings.[271] SWP contends that, in the Opinion, the Commission eliminated meaningful price signals to loads, thus frustrating demand response in contravention of federal law[272]

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[267] *Id*. (citing Exh. S-1 at 12-14; Exh. S-5).

[268] *Id*.

[269] *Id*.

[270] Opinion, 117 FERC ¶ 61,348 at P 8.

[271] SWP Rehearing Request at 42 (citing Tr. at 200:24-201:3, 202:10-13; Exh. SWP-18 at 23:1-4).

[272] *Id*. at 44-45 (citing Energy Policy Act of 2005 § 1252(f), 16 U.S.C. § 2642 (2005); U.S. Government Accountability Office, Report to the Chairman, Committee on Governmental Affairs, U.S. Senate, Electricity Markets: Consumers Could Benefit from Demand Programs, But Challenges Remain, http: www.gao.gov/new.items/d04844.pdf, at 31-33, 43-44, 51-52 (Aug. 2004); United States Department of Energy, Benefits of Demand Response in Electricity Markets and Recommendations for Achieving Them: A Report to the United States Congress Pursuant to section 1252 of the Energy Policy Act of 2005, http: www.oe.energy.gov/DocumentsandMedia/congress_1252.pdf, at x, 7 (Feb. 2006)).

and Commission policy.[273] SWP implies that, because the Commission has found that price-responsive demand provides the CAISO gird reliability and efficiency,[274] when the Commission rejected SWP's proposal, it acted arbitrarily and capriciously and imposed unjust and unreasonable rates.

94. SWP insists that uncontested evidence shows that must-offer costs could be reduced if peak demand were reduced through shifting loads away from the peak hour.[275] SWP denies that it overstated or misinterpreted the CAISO's position and argues instead that anticipated next day's peak load determines (or causes) the must-offer generation to be committed.[276] SWP also asserts that the judge never considered the evidence and arguments that SWP presented.[277] SWP claims that it is nonsensical and contrary to Commission precedent that allows allocation of costs to peak load to argue that a "contingency may occur any hour of the day, off or on peak."[278] SWP also contends that

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[273] *Id*. at 42-43 (citing *PJM Interconnection, LLC*, 117 FERC ¶ 61,331, at P 131, 133 (2006); *Midwest Indep. Sys. Operator, Inc.*, 117 FERC ¶ 61,325, at P 42 (2006); *Occidental Chemical Corp. v. PJM*, 102 FERC ¶ 61,275, at P 2, *reh'g denied*, 104 FERC ¶ 61,142 (2003)), 46 (citing Assessment of Demand Response and Advanced Metering, Docket No. AD06-2, at x, 7, 13, 133 (2006)).

[274] *Id*. at 46-48 (citing *Cal. Indep. Sys. Operator Corp.*, 100 FERC ¶ 61,060, at P 161, *on reh'g*, 101 FERC ¶ 61,061 (2002), *on reh'g*, 102 FERC ¶ 61,050 (2003); *Removing Obstacles to Increased Electric Generation and Natural Gas Supply in the Western United States*, 94 FERC ¶ 61,272, at 61,972, *reh'g dismissed*, 95 FERC ¶ 61,225, *order on reh'g*, 96 FERC ¶ 61,155, *order on reh'g*, 97 FERC ¶ 61,024 (2001); *Cal. Indep. Sys. Operator Corp.*, 105 FERC ¶ 61,140, at P 70; *reh'g dismissed*, 105 FERC ¶ 61,278 (2003); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 93 FERC ¶ 61,121, at 61,371 (2000); California Energy Commission and Public Utilities Commission, Energy Action Plan II, www.energy.ca.gov/energy_action_plan/ 2005-09-21_EAP2_FINAL.PDF, at 4-5 (Sept. 21, 2005); *Cal. Indep. Sys. Operator Corp.*, 116 FERC ¶ 61,274, at P 10 (2006), *on reh'g*, 119 FERC ¶ 61,076 (2007)).

[275] *Id*. at 49 (citing Tr. at 200:24-201:3, 202:10-13; Exh. SWP-18 at 23:1-4).

[276] *Id*. at 49-50 (citing Tr. at 147:4-10, 175:9-14).

[277] *Id*. at 53-54 n.151 (pointing out that the CAISO revised its testimony on this issue three times) (citing Exh. SWP-18 at 33:6-9; Tr. at 764:24-765:3; 765:18-766:4).

[278] *Id*. at 50-51 (quoting Initial Decision, 113 FERC ¶ 63,017 at P 103).

the fact that "most MLCC costs actually are incurred in off-peak hours"[279] so that must-offer generation contributes to over-generation reliability problems[280] only signifies that the costs relate to slow-start generation units that are operated at minimum load through the night to meet the following day's peak loads.

95. SWP argues that the flat, non-time-differentiated monthly allocation methodology does not provide load with price signals encouraging the shift away from peak periods[281] and thus erects a barrier to demand response. SWP contends that the Commission erred by adopting the judge's rationale that off-peak users, for which must-offer unit commitments are not made, may benefit from such commitments in the event of a contingency and thus should pay socialized rates.[282] According to SWP, in doing so, the Commission has prioritized a general potential benefit for off-peak loads above specific causes of cost incurrence, which precludes any inquiry into how price signals could be enhanced to promote demand response. SWP claims that this failure is inconsistent with uncontroverted CAISO testimony that reducing peak demand could reduce the need for must-offer generation.[283] SWP argues that, as a result, the Commission will not explore the key hours in which demand could be reduced to diminish the need for must-offer generation.

96. SWP claims that the Commission's acceptance of a flat, non-time sensitive rate unduly discriminates against demand response.[284] SWP states that: (1) demand can be used to a lesser degree to address the constraints identified in Amendment No. 60;[285] (2) must-offer costs could be reduced if peak demand were reduced through shifting loads away from peak periods;[286] and (3) SWP could provide more demand-based

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[279] *Id*. at 51 (quoting Initial Decision, 113 FERC ¶ 63,017 at P 103).

[280] *Id*. (citing Exh. SWP-42 at 1).

[281] *Id*. (citing Tr. at 204:10-23).

[282] *Id*. at 52 (citing Initial Decision, 113 FERC ¶ 63,017 at P 103).

[283] *Id*. (citing Tr. at 200:24-201:3, 202:10-13; Exh. SWP-18 at 23:1-4).

[284] *Id*. at 66 (citing Tr. at 204:10-23).

[285] *Id*. (citing Exh. ISO-21 at 15:4-7).

[286] *Id*. (citing Tr. at 202:10-13).

resources if it received price signals.[287] SWP argues that, by not providing equal opportunity for competing resources, the Commission has violated a cornerstone of federal energy regulation and has violated the FPA.[288]

97. SWP asserts that substantial evidence and Commission precedent support a coincident peak cost allocation, SWP's 5-hour peak period,[289] or the CAISO's 4-hour peak period to develop time-sensitive rates that would permit demand response. SWP contends that the CAISO has stated that the timing of the precise peak is less important than encouraging load shifting away from the peak hour.[290] SWP adds that PG&E and SoCal Edison agreed that SWP's proposed timeframe would send price signals to retail loads to encourage them to shift off-peak.[291] In support of its argument, SWP points out that Commission precedent related to other ISO/RTOs supports use of a coincident peak approach, which allocates costs based on a load's contribution to the system peak.[292]

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[287] *Id*. (citing Tr. at 1056:2-20, 1082:21-1083:8).

[288] *Id*. at 66-67 (citing *PJM Interconnection, LLC,* 115 FERC ¶ 61,079, at P 29, *reh'g denied*, 117 FERC ¶ 61,331; *Cal. Indep. Sys. Operator Corp.*, 105 FERC ¶ 61,140 at P 70; *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 93 FERC ¶ 61,121 at 61,371; *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 730-31 (D.C. Cir. 2000), *aff'd, New York v. FERC*, 535 U.S. 1 (2002); 16 U.S.C. § 796(28)(B) (2005); *Lockyer*, 383 F.3d 1006, 1012).

[289] *Id*. at 54-55 (citing Exh. SWP-18 at 15:13-16; Tr. at 180:20-23; Tr. at 1074:16-24, 181:6-10), n.152 (citing Exh. SWP-8 at 2; Tr. at 175:9-14, 665:15-23, 674:14-17).

[290] *Id*. at 55 (citing Exh. SWP-22W at 6).

[291] *Id*. at 55 (citing Exh. SWP-24A at 16; Exh. SWP-24B at 9, 22-23).

[292] *Id*. at 55-58 (citing PJM Interconnection, LLC, Reliability Assurance Agreement § 1.53, Second Revised Rate Schedule FERC No. 27, Third Revised Sheet No. 15 (Sept. 18, 2006); ISO New England Inc., Market Rule 1, FERC Electric Tariff No. 3, § III.1, Original Sheet Nos. 7060, 7236-37 (Dec. 1, 2006); New York Independent System Operator, Inc., FERC Electric Tariff Original Volume No. 2, § 2.194a, Third Revised Sheet No. 73 (Dec. 2, 2002), § 5.11, First Revised Sheet No. 122A (Jan. 9, 2004); PJM Interconnection, LLC, FERC Electric Tariff, Sixth Revised Vol. No. 1, First Revised Sheet No. 468 (Jan. 1, 2006); ISO New England, Inc., FERC Electric No. 3, Market Rule 1, Original Sheet Nos. 7237-7238 (Dec. 1, 2006); Con Edison Energy, Inc. v. ISO New England, 111 FERC ¶ 61,001 at P 2 (Apr. 1, 2005); PJM Interconnection, LLC, FERC Electric Tariff, Sixth Revised Vol. No. 1, Attachment DD § 5.1, Original

(continued…)

SWP argues that the coincident peak allocation is a reasonable alternative because the CAISO's use of that allocation for certain reliability costs shows that the CAISO is capable of administering such a methodology and that it is appropriate for the California grid. SWP points to the CAISO's proposal to use an annual coincident peak allocation for certain backstop reliability costs associated with its Reliability Capacity Services Tariff (RCST), the Commission's acceptance of a 1-CP cost allocation for CAISO resource adequacy backstop generation purchases,[293] the California Public Utilities Commission's order to allocate resource adequacy capacity among retail customers on a 12-month coincident peak basis,[294] and the allocation of reliability costs to retail customers using a 12-CP or monthly coincident peak method.

Commission Determination

98. In the Opinion, the Commission noted that the must-offer obligation is "designed to prevent withholding and thereby to ensure that the CAISO will be able to call upon available resources in the real-time market to the extent that energy is needed."[295] The Commission also observed that the CAISO filed Amendment No. 60 to modify the allocation of must-offer costs to be more consistent with cost causation principles.[296] Specifically, based on its determination that must-offer generation has been committed to

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Sheet No. 576 (effective June 1, 2007); PJM Interconnection, LLC, Second Revised Rate Schedule FERC No. 27, Reliability Assurance Agreement Article 1.53, Third Revised Sheet No. 15 (effective Sept. 18, 2006); Midwest ISO, FERC Electric Tariff, Third Revised Vol. No. 1, Schedule 3, Third Revised Sheet No. 862 (Apr. 1, 2005); *PJM Interconnection, LLC*, 107 FERC ¶ 61,112, at P 15, 19, 22 (2004), *on reh'g*, 110 FERC ¶ 61,053 (2005), *on reh'g*, 112 FERC ¶ 61,031 (2005), *reh'g denied*, 114 FERC ¶ 61,302 (2006)).

[293] *Id*. at 58 (citing *Cal. Indep. Sys. Operator Corp.*, 116 FERC ¶ 61,274 at P 1194, 1196-98; MRTU Tariff § 42.1.8, Original Sheet No. 524 (filed Feb. 9, 2006)).

[294] *Id*. at 59 (citing California Public Utilities Commission, *Order Instituting Rulemaking to Integrate Procurement Policies and Consider Long-Term Procurement Plans*, Rulemaking 06-02-013, Decision 06-07-029, "Opinion on New Generation and Long Term Contract Proposals and Cost Allocation" at 31, P 15 (2006)).

[295] *See* Opinion, 117 FERC ¶ 61,348 at P 3 (quoting June 2001 Order, 95 FERC ¶ 61,418 at 62,551).

[296] *Id*. P 4.

primarily satisfy local, zonal, or system reliability requirements, the CAISO proposed to allocate MLCC costs according to a three-category rate design.[297] A critical component of this description is that MLCC costs are incurred for reliability purposes. The Commission has previously considered a CAISO proposal that utilized cost minimization as a criterion for determining whether to grant must-offer obligation waivers to generators.[298] The Commission rejected this criterion because reliability was paramount and minimization of costs could not be used to the detriment of reliability.[299]

99. Among other arguments, in the instant rehearing request, SWP contends that economic considerations support its position that the MLCC costs should be allocated to on-peak hours and that failure to do so thwarts price signals and demand response. We disagree. While SWP's stated goals through its proposed on-peak allocation of MLCC costs are laudable, they are misplaced in the instant proceeding. MLCC costs are incurred to support reliability, and the allocation of those costs should be consistent with that.

100. In addition, the record indicates that the CAISO incurs MLCC costs in off-peak periods because of minimum run time requirements for generators committed under the must-offer obligation.[300] The record also indicates that the CAISO may incur MLCC costs in off-peak periods, such as Sundays, depending on whether a contingency develops that would require the incurrence of MLCC costs.[301] Furthermore, the CAISO has stated that it needs must-offer generation in off-peak periods and that must-offer generation is valuable 24-hours a day.[302] Therefore, we continue to find that the CAISO's flat, non-time sensitive rate design for MLCC costs is just and reasonable.

101. Finally, we note that the Amendment No. 60 cost allocation better assigns cost responsibility to those responsible for the incurrence of such costs, as compared to its

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[297] *Id*. P 4, 16.

[298] *See* May 2002 Order, 99 FERC ¶ 61,158 at 61,629-30.

[299] *See Id*. at 61,630.

[300] Exh. ISO-21 at 6:2-5; Tr. at 574:4-575:3.

[301] Tr. at 571:24-574:3.

[302] Tr. at 389:6-11.

predecessor.[303] Moreover, we note that the must-offer obligation will remain in effect only until implementation of MRTU and that the MRTU proposal as conditionally accepted by the Commission will significantly further improve price signals.[304] For these reasons, we deny SWP's rehearing request.

f. Whether Non-Local MLCC Costs Should Be Allocated on a Daily or Monthly Basis (Issue No. 5)

102. SWP proposed that zonal and system cost would be allocated daily, not monthly.[305]

Initial Decision and Opinion No. 492

103. In the Initial Decision, the judge concluded that daily allocation was just, reasonable and not unduly discriminatory.[306] However, the judge also observed that it would be just, reasonable and not unduly discriminatory to allocate these costs on a monthly basis as done in Attachment E, particularly given that monthly allocation squares with the CAISO's start-up and emissions cost allocation methodology.[307]

104. In the Opinion, the Commission found that, because the CAISO proposed only a monthly allocation of non-local MLCC costs in Amendment No. 60, the determination that the monthly allocation was just and reasonable should have ended the judge's

[303] Prior to the Amendment No. 60 proposal, the CAISO allocated MLCC costs to market participants on a system-wide basis.

[304] *See Cal. Indep. Sys. Operator Corp*., 116 FERC ¶ 61,274 at P 10, 689-90.

[305] Initial Decision, 113 FERC ¶ 63,017 at P 100, 101.

[306] The judge finds that the CAISO does not oppose calculating these costs daily, it is capable of doing so, and such allocation is not inconsistent with procedural requirements or other Commission precedent. *Id*. P 102 (citing Exh. ISO-20 at 36; Tr. 852; Exh. ISO-9; Exh. ISO-11; Exh. ISO-15; Exh. ISO-17; Exh. ISO-20 at 46-47; Exh. ISO-8).

[307] *Id*. P 116.

analysis, and alternative proposals should not have been considered.[308] Therefore, the Commission rejected as unnecessary the judge's conclusion that daily cost allocation would also be just, reasonable, and not unduly discriminatory.

Rehearing Request

105. On rehearing, SWP argues that the Commission's determination is inconsistent with its holding in the Opinion that the judge could consider alternative proposals because the CAISO's filing did not provide proposed tariff sheets with specific, fixed or transparent category classification criteria.[309] SWP claims that the Commission did not dispute SWP's concern that a monthly, as opposed to daily, allocation methodology is damaging to price signals and thus demand response[310] but offered no explanation why it was not unjust and unreasonable to erect unnecessary barriers to demand response. SWP claims that the Commission's position on this issue conflicts with Commission precedent.[311] SWP adds that the CAISO has stated that the daily allocation is feasible and more appropriate than the monthly allocation.[312]

Commission Determination

106. It is true that the Commission found that the judge could consider alternative proposals before him.[313] In fact, he reviewed the alternatives and concluded that the Amendment No. 60 – Attachment E alternative was just, reasonable and not unduly discriminatory.[314] Having made that finding, and given the Commission's affirmance of that finding,[315] we were correct in adopting the CAISO's proposal, including the

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[308] *See Cal. Indep. Sys. Operator Corp.*, 111 FERC ¶ 61,337 at P 27.

[309] SWP Rehearing Request at 60 (citing Opinion, 117 FERC ¶ 61,348 at P 22).

[310] *Id*. (citing Opinion, 117 FERC ¶ 61,348 at P 63).

[311] *Id*. at 61 (citing *PJM Interconnection, LLC*, 115 FERC ¶ 61,079 at P 29).

[312] *Id*. at 61-62 (quoting CAISO Answer, Docket No. ER04-835, at 30 (June 16, 2004); citing Exh. ISO-20 at 47:3-4; Exh. ISO-9; Exh. ISO-11; Exh. ISO-15; Exh. ISO-17).

[313] *See* Opinion, 117 FERC ¶ 61,348 at P 22.

[314] *See* Initial Decision, 113 FERC ¶ 63,017 at P 116.

[315] *See* Opinion, 117 FERC ¶ 61,348 at P 25.

allocation of zonal/system costs on a monthly basis. The judge's suggestion that SWP's proposal to allocate zonal/system costs on a daily basis might be preferable is irrelevant because, once he determined, and we affirmed, that the CAISO's proposal was just and reasonable, the Commission's review was complete.[316] We are required to adopt just and reasonable rates, terms and conditions. We are not required to adopt the best or most just and reasonable approach.[317]

107. In addition, while the judge found that SWP's daily allocation proposal would, in his view, be preferable, we disagree.[318] We find that the CAISO's monthly allocation proposal is preferable. First, as the judge noted, the daily cost allocation does not square with the CAISO's monthly allocation of start-up and emissions cost.[319] As noted herein, the Commission has held that the CAISO should recover MLCC costs consistent with the methodology used to recover start-up and emissions costs.[320] Therefore, it would be contrary to Commission precedent to allocate MLCC costs on a daily basis.

108. Second, the allocation of MLCC costs on a daily basis is inappropriate due to the "long-start" nature of certain units, which, at times, are started-up or dispatched to remain

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[316] *See Cities of Bethany v. FERC*, 727 F.2d 1131,1136 (D.C. Cir. 1984) (the Commission's authority to review rates under the FPA is limited to an inquiry into whether the rates proposed by a utility are reasonable -- and not to extend to determining whether a proposed rate schedule is more or less reasonable than alternative rate designs); *Louisville Gas and Elec. Co.*, 114 FERC ¶ 61,282 at P 29 (2006) (the just and reasonable standard under the FPA is not so rigid as to limit rates to a "best rate" or "most efficient rate" standard; rather, a range of alternative approaches often may be just and reasonable), *reh'g denied*, *E. ON U.S. LLC*, 116 FERC ¶ 61,020 (2006).

[317] *Id*.

[318] We note that SWP's claim that the Commission did not dispute SWP's concern that a monthly, as opposed to daily, allocation methodology is damaging to price signals and thus demand response without offering an explanation why it was not unjust and unreasonable to erect unnecessary barriers to demand response misconstrues the Opinion. *See* SWP Rehearing Request at 60 (citing Opinion, 117 FERC ¶ 61,348 at P 63). In that portion of the Opinion, the Commission merely summarized SWP's argument; it did not provide an assessment of the merits of SWP's argument, as SWP contends.

[319] *See* Initial Decision, 113 FERC ¶ 63,017 at P 116.

[320] December 2001 Order, 97 FERC ¶ 61,293 at 62,363.

on days in advance of when they are actually needed.[321] The allocation of MLCC costs to each day a "long-start" unit is on would not properly allocate costs to those loads that gave rise to the need for the CAISO to call on that unit.[322] Any attempt to allocate some portion of MLCC costs to the appropriate day will be both complex and flawed due to the many subjective assumptions that are necessary to facilitate such a detailed allocation process.[323] In addition, if a must-offer waiver denial is needed for a "long-start" unit, that generator must be committed well in advance of system reliability needs and would incur must-offer waiver denial costs for the entire start-up period.[324] This creates a problem in how to allocate the start-up costs of this generator fairly on a daily basis.[325] Thus, instead of trying to split the costs between SCs who may use the system in varying degrees, on different days, in differing amounts, a monthly allocation fairly shares the costs of a must-offer waiver denial based on SCs' system usage and the CAISO's reliability needs.[326] For these reasons, we continue to find that the monthly allocation of non-local MLCC costs is just and reasonable and reject the daily allocation proposal. Accordingly, we deny SWP's rehearing request.

g. Impact on Proceeding in Docket No. EL05-146-000

Initial Decision and Opinion No. 492

109. In the Opinion, the Commission noted that the CAISO's RCST in Docket No. EL05-146-000, which will terminate with MRTU implementation, will follow the cost allocation methodology accepted in this proceeding.[327]

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[321] Exh. PGE-4 at 7:14-8:4.

[322] *See* Exh. PGE-4 at 7:21-8:1.

[323] Exh. PGE-4 at 7:17–8:4.

[324] Exh. S-6 at 32:17–33:12.

[325] *Id*.

[326] Exh. S-6 at 33: 13-17.

[327] *See* Opinion, 117 FERC ¶ 61,348 at n.10.

Rehearing Request

110. On rehearing, SWP argues that, without notice and supporting evidence, the Commission improperly prejudged the allocation of reliability capacity costs in Docket No. EL05-146-000. SWP states that, in Docket No. EL05-146-000, the Commission ordered a paper hearing to determine whether a contested settlement's proposed allocation of capacity costs, including the proposal to allocate RCST must-offer costs using the Amendment No. 60 methodology, was just and reasonable.[328] SWP argues that the Commission's determination that the RCST will follow the cost allocation methodology accepted in this proceeding is contrary to the Commission's finding in the hearing order in the RCST proceeding. SWP states that, in that proceeding, the Commission determined that the proposal to use the Amendment No. 60 methodology for RCST cost allocation had not been shown to be just and reasonable with respect to the must-offer obligation.[329] SWP states that, in the RCST proceeding, it challenged the application of the Amendment No. 60 methodology for allocating CAISO energy payments to RCST costs related to CAISO capacity payments.

111. If the Commission finds that it was appropriate to make its determination in this proceeding, SWP requests that the Commission consider the following evidence it claims it established in Docket No. EL05-146: (1) RCST reliability capacity costs are incurred to meet peak loads;[330] (2) time-sensitive cost allocation is necessary for demand response that can reduce the need for reliability generation capacity;[331] (3) testimony supports time-sensitive, not socialized, cost allocation;[332] and (4) the CAISO is capable of using a

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[328] SWP Rehearing Request at 3-4, 18-19 (citing *Indep. Energy Producers v. Cal. Indep. Sys. Operator Corp.*, 116 FERC ¶ 61,069, at P 1, *order on clarification*, 116 FERC ¶ 61,297 (2006).

[329] *Id*.

[330] SWP Rehearing Request at 25 (citing Response of Supporting Parties, Docket No. EL05-146, at 4; Cavicchi Affidavit at P 4 (Aug. 21, 2006)).

[331] *Id*. (citing SWP Comments, Docket No. EL05-146, L. Terry Affidavit, at 5-6 (Apr. 20, 2006); SWP Responsive Post Order Comments, Docket No. EL05-146, Second L. Terry Affidavit at P 6-7, 10-14, 20 (Sept. 26, 2006)).

[332] *Id*. at 31-36 (citing IEP Complaint, Docket No. EL05-146, A. Joseph Cavicchi Affidavit at P 26 (Aug. 26, 2005); IEP *pro forma* tariff section 5.12.5; Response of Supporting Parties, Docket No. EL05-146, SoCal Edison General Rate Case Attachment Excerpts (Aug. 21, 2006); Response of Supporting Parties, Docket No. EL05-146, SoCal

(continued…)

coincident peak allocation methodology.[333] SWP requests that the Commission refrain from pre-judging the outcome of the proceeding in Docket No. EL05-146-000. If the Commission does address the merits of the issue here, SWP requests that the Commission allocate must-offer capacity costs in that proceeding using a 12-coincident peak approach consistent with the California Public Utilities Commission's approach or the 1-coincident peak approach partially adopted by the CAISO.

Commission Determination

112. We agree that the Commission acted prematurely when it stated in the Opinion that the CAISO's RCST in Docket No. EL05-146-000 would follow the cost allocation methodology in this proceeding because that issue was then pending in Docket No. EL05-146-000. However, since then, the Commission has issued an order on the paper hearing in Docket No. EL05-146-000, in which it found that it was just and reasonable for the CAISO to allocate the RSCT capacity costs incurred for the dispatch of units under the must-offer obligation in accordance with the Commission's determination in this proceeding.[334] Because the Commission has issued a final determination on this issue in Docket No. EL05-146-000, we find that SWP's arguments are now moot. Accordingly, we deny rehearing on this point.

Edison General Rate Case Attachment Excerpts, SoCal Edison Silsbee Testimony at 1:8-9, 1:12-13, 20:4-5 (Aug. 21, 2006); SWP Initial Post-Order Comments, App. A, SoCal Edison Silsbee Testimony, at 21:7-9 (Sept. 11, 2006); Response of Supporting Parties, Docket No. EL05-146, PG&E General Rate Case Attachment Excerpts, PG&E Pease Testimony at 2-2:2-3, 2-2:13-14, 2-2:17-19 (Aug. 21, 2006); SWP Initial Post-Order Comments, Docket No. EL05-146, App. B, PG&E Martyn Testimony at 2-2:2-5, 2-6:1-2, n.5 (Sept. 11, 2006); SWP Initial Post-Order Comments, Docket No. EL05-146, App. C, PG&E Bell Testimony at 4-1:16-17 (Sept. 11, 2006); SWP Initial Post-Order Comments, Docket No. EL05-146, App. C, PG&E Mayers Testimony at 2-9:29 to 2-10:1 (Sept. 11, 2006); SWP Initial Post-Order Comments, Docket No. EL05-146, App. C, PG&E Alvarez Testimony at 3-8:22-25 (Sept. 11, 2006); Response, Docket No. EL05-146, PG&E Critical Peak Pricing Case Attachment Excerpts, PG&E Alvarez Testimony at 3-9:4-6, 3-10:9-10 (Aug. 21, 2006)).

[333] *Id*. at 36-37 (citing Settlement Explanatory Statement, Docket No. EL05-146, at 7 (Mar. 31, 2006); Settlement *pro forma* tariff section 43.2.1.1, Docket No. EL05-146 (Mar. 31, 2006)).

[334] *Indep. Energy Producers Assoc. v. Cal. Indep. Sys. Operator Corp.*, 118 FERC ¶ 61,096, at P 125, 154, *reh'g denied*, 119 FERC ¶ 61,266 (2007).

The Commission orders:

(A) The requests for rehearing are hereby granted, in part, and denied, in part, as discussed in the body of this order.

(B) The CAISO is hereby directed to make a compliance filing, within 30 days of the date of this order, as discussed in the body of this order.

By the Commission. Commissioner Kelly not participating.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.