UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	)	Docket No. EL04-24-000

REPLY BRIEF OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION

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Pursuant to the Commission's Order of February 17, 2004, in the above identified proceeding, the California Independent System Operator Corporation ("ISO") respectfully submits its Reply Brief.

SUMMARY

I. Intervenors Have Failed to Show that the ISO Improperly Assesses Transmission Losses for Schedules on the APS and IID Portions of SWPL

In its Initial Brief, the ISO explained that a reversal of the Arbitrator's decision is logically compelled by Opinion No. 463-A. San Diego Gas & Electric Company ("SDG&E") and Imperial Irrigation District ("IID") seek unsuccessfully to avoid the impact of the Commission's decision by contending that these rulings are irrelevant because they relate to the Market Operations Charge, not charges for Transmission Losses. Market Operations Charges are billed to SDG&E based on the quantities of Imbalance Energy procured in the ISO's markets to cover the losses according to the ISO methodology. The Commission's approval of this methodology inexorably approves the underlying charges. Moreover, Section 2.4.4.4.4.5 of the ISO Tariff provides for parties to the Existing Contracts to determine whether the ISO's calculations regarding Transmission Losses

result in any associated shortfall or surplus and to settle the difference. If, as SDG&E and IID suggest, the ISO can under Opinion 463-A properly determine and incur Transmission Losses associated with the Arizona Public Service Company ("APS") and IID owned portions of SWPL according to the ISO methodology, but cannot thereafter properly charge the costs of those Transmission Losses to SDG&E, Section 2.4.4.4.5 of the ISO Tariff would serve no purpose. This point is not only crucial; it should be dispositive. At issue is the meaning and application of these very specific ISO Tariff provisions adopted to address responsibility for covering any differences between what the ISO charges for Transmission Losses and what is provided for in Existing Contracts. SDG&E urges an interpretation that would (1) read these provisions out of the ISO Tariff altogether and (2) render the proceedings leading to Opinion Nos. 458 and 458-A meaningless.

II. SDG&E's Efforts to Disavow Its Status as Scheduling Coordinator for the APS and IID Schedules Is Unavailing

Intervenors' arguments concerning Operational Control essentially perpetuate the Arbitrator's misunderstanding of Operational Control. Neither ownership or scheduling rights are a prerequisite to the transfer of Operational Control. Operational Control is more than one dimensional. It is not just ownership and contractual scheduling rights. In its brief, APS offers a tripartite model of Operational Control: Although the ISO does not necessarily endorse this particular model, APS's model illustrates the failure of the positions taken by the Arbitrator, SDG&E and IID. By focusing exclusively on one aspect of

Operational Control, they fail to comprehend the nature of the Operational Control that SDG&E transferred to the ISO.

The ISO has not claimed that SDG&E conveyed to the ISO, or had the right to convey to the ISO, Operational Control of the entirety of SWPL in derogation of the joint ownership and of APS' and IID's rights. Rather, the ISO simply asserts that SDG&E transferred *those rights and obligations that it had under the Participation Agreements and as Control Area Operator* regarding the portions of SWPL owned by APS and IID. In other words, placing facilities under the ISO's Operational Control means simply conveying to the ISO all rights except those protected by the agreements.

Of relevance in this proceeding, the ISO's Operational Control of the APS and IID portions of SWPL involves the balancing function for the entire line, which includes accounting for Transmission Losses, which the ISO performs pursuant to its tariff. Although APS and IID reimburse SDG&E in-kind for Transmission Losses, this reimbursement affects their responsibility to SDG&E, *not* SDG&E's cost responsibility to the ISO. Even if the in-kind Energy or its value were conveyed to the ISO, other Scheduling Coordinators would bear the cost differential between the value of the in-kind Energy and the Transmission Losses as determined by the Commission-approved methodology followed by the ISO. This, of course, is precisely the circumstance that Section 2.4.4.4.4.5, Scheduling Protocol Section 4.3, and Opinions 458 and 458-A address.

The Operational Control that SDG&E has transferred to the ISO does not include or interfere with the rights of APS or IID; rather, it is subject to those

rights and only includes those rights SDG&E possesses under the Participation Agreements, its ownership of SWPL, and its Control Area responsibilities. The only question here is whether the Operational Control that SDG&E transferred to the ISO regarding SWPL includes SWPL as part of the ISO Controlled Grid *for the purposes of the Transmission Loss calculation methodology*. Because the calculation and replacement of Transmission Losses was part of SDG&E's "bundle of rights" in SWPL when it placed SWPL under the ISO's Operational Control, the whole of SWPL is within the ISO's Operational Control for that purpose (albeit still subject to protections provided to APS and IID). As the ISO has shown above and in its Initial Brief, Commission orders and policy, as well as prior dealings, demonstrate that that SDG&E is responsible for the cost of Transmission Losses calculated according to the ISO methodology.

III. SDG&E Cannot Justify Its Failure to Comply With ISO Tariff Sections 11.7.2 and 11.7.3.

The ISO has explained that SDG&E is the Scheduling Coordinator for Schedules on the APS and IID portions of SWPL and that, even if it is not, is obligated to comply with the timelines of Section 11.7.2 and 11.7.3 of the ISO Tariff regarding any billing disputes in connection with those Schedules. SDG&E's assertions in its Initial Brief are simply baseless. SDG&E's support for this contention is testimony of its witness that it "consulted" with the ISO to "seek implementation of the Participation Agreement transmission loss methodology." SDG&E Br. at 57; Exh. SD-17 (R. 3197). This is not *by any stretch of the imagination* a dispute of a settlement statement. SDG&E additionally claims that Mr. Yari "raised the issue" or his predecessor "tried to resolve the dispute", but

beyond these vague recollections, SDG&E offers no record of such an effort and no date. Mr. Yari asserts he raised the issue in late 1999 or early 2000, and his predecessor "long before." Sections 11.7.2 and 11.7.3 preclude SDG&E's claims for amounts that were not disputed under those sections.

STANDARD OF REVIEW

As the ISO explained in its Initial Brief, the Commission should review the Arbitrator's interpretation of the ISO Tariff (and any related documents) *de novo* and should not be misled by the Arbitrator's attempt to insulate his conclusions from review by labeling them "Findings of Fact."[1] It is equally important that the Commission recognize the implicit misinterpretations of the ISO Tariff that underlie the "Findings of Fact" and review these interpretations *de novo* as well.

In its Reply Brief, SDG&E purports to challenge the ISO's characterizations of the Arbitrator's findings. Despite the ISO's specification of each significant factual finding that represents or relies upon conclusions of law, SDG&E identifies only two specific instances that it insists are findings of fact deserving of deference. In the first instance, the ISO agrees that whether the ISO had notice of SDG&E's position is a question of fact; but that is unrelated to the ISO's argument about that finding. The ISO's position in its Initial Brief was simply that the Arbitrator's finding was so devoid of evidentiary support as to require rejection. It is not possible, however, to divorce the second finding – that SDG&E did not transfer Operational Control of the APS and IID owned shares of

[1] Capitalized terms not otherwise defined herein have the meaning set forth in the ISO Tariff Master Definitions Supplement, Appendix A.

SWPL to the ISO – from legal conclusions about the interpretation of the ISO Tariff. In reaching his conclusions about Operational Control, the Arbitrator found:

> Under the definition of Operational Control in the ISO Tariff, [the ISO] cannot and does not direct SDG&E, any other Participating TO, or APS and IID how to operate the APS and IID shares of SWPL "for the purpose of affording comparable nondiscriminatory transmission access."

Findings of Fact ## 20, 21 (R. 4357). As the ISO noted in its Initial Brief, although styled as Findings of Fact, the validity of these conclusory statements is *wholly dependent* on the meaning of Operational Control as used in the ISO Tariff. Characterizing the issue of Operational Control as factual borders on the absurd.

Citing *Great Northern Ry. Co. v. Merchants Elevator Co.*, 259 U.S. 285 (1922) and *Penn Central Co. v. General Mills, Inc.*, 439 F.2d 1338 (8th Cir. 1971), IID takes an enormous leap of illogic and pronounces that "longstanding case law indicates that interpretations of tariff provisions should be treated as findings of fact." IID Br. at 17. In reality, the Court in *Great Northern* said just the opposite:

> [w]hat construction shall be given to a railroad tariff presents ordinarily a question of law which does not differ in character from those presented when the construction of any other document is in dispute.
>
> When the words of a written instrument are used in their ordinary meaning, their construction presents a question solely of law.

259 U.S. at 291. Courts have uniformly maintained this principle. *See, e.g., Rebel Motor Freight Inc. v. ICC,* 971 F.2d 1288, 1290-91 (6th Cir. 1992) and cases cited therein; *Coca-Cola Co. v. Atchison, Topeka, & Santa Fe Ry. Co.,* 608 F.2d 213, 219 (5th Cir. 1979);

The *Great Northern* Court went on to state that when technical terms are involved, the interpretation may involve a technical factual issue with an administrative agency's expertise. 259 US. at 291-92. In the eighty years since *Great Northern,* however, courts have recognized that an agency's application of its specialized expertise to tariff interpretation does not transform a question of law into a question of fact. *See, e.g., Columbia Gas Transmission Corp. v. FPC*, 530 F.2d 1056, 1059 (D.C. Cir. 1976) ("[T]here is room, in review of administrative agencies, for some deference to their views even on matters of law like the meaning of contracts, as on the meaning of statutes, where the understanding of the documents involved is enhanced by technical knowledge of industry conditions and practices."); *North Atl. Westbound Freight Ass'n v. FMC*, 397 F.2d 683, 685 (D.C. Cir. 1968) (per curiam) ("Construction of such an agreement involves a question of law but like other questions of law, e.g., interpretation of regulatory statutes, the agency's determination is entitled to weight on judicial reconsideration.").

Penn Central, IID's other authority, also states that the interpretation of a tariff is typically a question of law. 439 F.2d at 1340. Indeed, the passage quoted by IID refers not to the interpretation of the tariff, but its *application.*

As the ISO discussed in its Initial Brief, the determination of the ISO's tariff requirements draws upon the Commission's technical expertise and is essential to discharging the Commission's obligation to ensure that its policies are appropriately implemented. Whether the Arbitrator's interpretation of the ISO Tariff (and any related documents) is correct is a question of law that the Commission should review *de novo*.

IID also contends that the Commission should give substantial deference to the Arbitrator's conclusions of law. In support, it cites Commission statements in the Policy Statement Regarding Regional Transmission Groups[2] about the desirability of adherence to the results of binding arbitration awards. IID Br. at 19. What IID fails to understand is that the ISO arbitration procedure is *not* binding. Section 13 of the ISO Tariff specifically provides for an appeal to the Commission. The distinction is apparent if one examines the cases cited by the Commission in the Policy Statement, none of which involved authorized appeals to the Commission.

No more persuasive are IID's citations of Commission statements in Order No. 578[3] regarding vacation of arbitration awards. The policies of Order No. 578 are simply not applicable here. Order No. 578 did not involve Commission review of arbitration awards under the terms of tariffs or contracts. Rather, it involved arbitration of disputes that are brought in the first place before the Commission. It was intended to implement the Administrative Dispute Resolution

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[2] *Policy Statement Regarding Regional Transmission Groups*, FERC Stats. & Regs. ¶ 30,976, 30,877 (1993).

[3] *Alternative Dispute Resolution*, FERC Stats. & Regs. ¶ 31,018, 31,328 (1995).

Act ("ADRA") of 1990.[4] The Commission retains the right to determine which disputes are appropriate for alternative dispute resolution. Those regulations do not apply here, even by analogy. Any policy of deference to an arbitrator's award that might be drawn from policies of Order No. 578 and the ADRA (if there were any) would relate to proceedings conducted under different legal authority and would simply be inapplicable here.

In this instance, Section 13.4.1 of the ISO Tariff allows an appeal based on much broader grounds:

> [T]hat the award is contrary to or beyond the scope of the relevant ISO documents, United States federal law, including, without limitation, the FPA, and any FERC regulations or decisions, or state law.

IID's assertions that *de novo* review of questions of law, because of more limited review in the FAA and California law, would encourage forum shopping are similarly unfounded. The Federal Arbitration Act ("FAA")[5] provides very limited grounds for review, 9 U.S.C. § 10. There is a conflict among the circuits the concerning whether the review limitations of the FAA dictate deference to the Arbitrator's conclusions of law or act only as a default when the underlying arbitration agreement does not specify a broader scope of review. Compare *Kyocera Corp. v. Prudential-Bache, Inc.*, 341 F.3d 987 (9th Cir. 2003); *Gateway Technologies, Inc. v. MCI Telecomm. Corp.*, 64 F.3d 993, 996 (5th Cir. 1995).

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[4] *Id.*

[5] 5 USC § 581(a). In an order subsequent to Order No. 578, the Commission conformed its regulations with 1996 amendments to the ADRA and deleted the regulations providing for vacatur of awards. *Complaint Procedures*, FERC Stats. & Regs. ¶ 31,071 (1999).

California law specifically similarly provides for expanded review according to the provisions of the underlying instrument providing for arbitration. *Pacific Gas & Elec. Co. v. Superior Ct.*, 19 Cal Rptr. 2d 295, 303-04 (Cal. Ct. App. 1993). In this instance, Section 13.4.1 of the ISO Tariff allows an appeal based on much broader grounds than the FAA or California arbitration law:

> [T]hat the award is contrary to or beyond the scope of the relevant ISO documents, United States federal law, including without limitation, the FPA, and any FERC regulations or decisions, or state law.

Thus, contrary to IID's view, the FAA and California law provide no basis for a court to apply a standard different from that applied by the Commission and no basis for forum shopping.

ARGUMENT

I. Intervenors Have Failed to Show that the ISO Improperly Assesses Transmission Losses for Schedules on the APS and IID Portions of SWPL

A. SDG&E's and IID's Arguments Disregard SDG&E's Responsibility for the Costs of Transmission Losses, as Established by Opinion No. 463-A, the ISO Tariff, and Commission Policy

In its Initial Brief, the ISO explained that a reversal of the Arbitrator's decision is logically compelled by Opinion No. 463-A, *California Independent System Operator Corp.*, 106 FERC ¶ 61,032 (2004), which was issued after the Arbitrator's decision. SDG&E and IID fail to address the logical consequences of Opinion No. 463-A; instead they seek unsuccessfully to avoid the impact of the Commission's decision by ignoring its fundamental basis.

As discussed in the ISO's Initial Brief, Opinion No. 463-A is significant in that the Commission rejected SDG&E's arguments and reached the following conclusions:

- The SWPL Schedules are wheel-through transactions, importing, transmitting, and exporting Generation to serve APS and IID Load. 106 FERC ¶ 61,032 at P 61.

- Scheduling Coordinators are required to submit balanced Schedules. Although SDG&E is Scheduling for Loads outside the ISO Control Area, the ISO must still match Generation resources for that Load. *Id.* at P 62.

- On this basis, the ISO's authority to charge SDG&E the Market Operation charge for the net procurement of Imbalance Energy to cover Transmission Losses for Schedules on the APS and IID portions of SWPL should be affirmed. *Id.* at PP 64-65.

SDG&E and IID contend that these rulings are irrelevant because they relate to the Market Operations Charge, which, according to SDG&E, has broader application than the charge for Transmission Losses under Section 7.4 of the ISO Tariff, which is limited to the ISO Controlled Grid. SDG&E Br. 45-47; IID Br. at 45-46. This distinction makes no sense. The Commission authorized the ISO to charge SDG&E for the costs involved in procuring Imbalance Energy to cover Transmission Losses on the portions of SWPL owned by IID and APS. Those charges are billed to SDG&E based on the quantities of Imbalance Energy procured in the ISO's markets to cover the losses according to the ISO methodology. 106 FERC ¶ 61,032 at P 60. On its face, the Commission's approval of this methodology inexorably approves the underlying charges.

This position is further supported by the Commission's order, in which it directed the ISO to net Imbalance Energy self-supplied by SDG&E to off-set Transmission Losses. Id. at P 64. If the ISO is not authorized to apply its

methodology for determining the Transmission Losses, then what is the basis for recognizing SDG&E's offsets? There is none; SDG&E's and IID's arguments lead to a logical impasse.

The error of SDG&E's and IID's arguments is even more obvious when viewed in the context of the ISO Tariff. Section 2.4.4.4.4.5 of the ISO Tariff (Original Sheet No. 57) states that the ISO:

> will provide the parties to the Existing Contracts with details of its Transmission Losses and Ancillary Services calculations to enable them to determine whether the ISO's calculations result in any associated shortfall or surplus and to enable the parties to the Existing Contracts to settle the difference bilaterally or through the relevant TO Tariff.

If, as SDG&E and IID suggest, the ISO can under Opinion 463-A properly determine and incur Transmission Losses associated with the APS and IID owned portions of SWPL according to the ISO methodology, but cannot thereafter properly charge the costs of those Transmission Losses to SDG&E, Section 2.4.4.4.5 of the ISO Tariff would serve no purpose. Although SDG&E contends that Section 2.4.4.4.4.5 would still be applicable to charges "properly" assessed by the ISO, SDG&E Br. at 38, such charges would constitute a null set. In light of the fact that the Transmission Loss differentials envisioned by ISO Tariff Section 2.4.4.4.4.5 (and Scheduling Protocol Section 4.3) arise *only* where, as here, the ISO has no rights with respect to the scheduling capacities of non-Participating TOs, under SDG&E's view of Operational Control there would be no

circumstance in which these provisions would apply.[6] SDG&E does not provide any examples of charges that could be "properly" assessed under its reasoning because it cannot. This point is not only crucial; it should be dispositive. At issue is the meaning and application of these very specific ISO Tariff provisions adopted to address responsibility for covering any differences between what the ISO charges for Transmission Losses and what is provided for in Existing Contracts. SDG&E urges an interpretation that would (1) read these provisions out of the ISO Tariff altogether and (2) render the proceedings leading to Opinion Nos. 458 and 458-A meaningless.

SDG&E and IID similarly dismiss Opinion Nos. 458 and 458-A as irrelevant, asserting that they only apply to costs "properly" charged to Scheduling Coordinators. SDG&E Br. at 47-49; IID Br. at 45-46. In making this argument, neither party addressed the fundamental underlying issue. As discussed above, after Opinion No. 463-A, there is no question that the ISO *properly* procured Imbalance Energy according to its Transmission Loss methodology in order to cover Transmission Losses associated with the APS and

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[6] SDG&E now contends that the ISO misreads the Arbitrator's discussion of the relationship between Operational Control and Scheduling Control. SDG&E Br. at 37. *See also* IID Br. at 37. The Arbitrator's reasoning, as discussed in the ISO's Initial Brief at 25-27, is apparent on its face. Moreover, it is precisely that relationship that SDG&E urged before the Arbitrator:

> [I]t is undisputed that APS and IID, rather than the ISO, determine whose energy, at what times, and in what amounts, will be scheduled over that capacity. The ISO does not purport to have a say over how such capacity is used and does not include that capacity in determining how much capacity is available for use by third parties under the ISO Tariff. Thus, in the terms of the definition of Operational Control provided in the ISO Tariff, the ISO cannot and does not "direct" SDG&E, or any other Participating TO, much less APS and IID themselves, how to operate the APS/IID shares of SWPL "for the purpose of affording comparable non-discriminatory transmission access."

SDG&E Post Hearing Br. at 21-22 (R. 3969-70).

IID Schedules submitted by SDG&E pursuant to its Existing Contract; otherwise, there would be no basis for assessing the cost of that procurement to SDG&E. Under SDG&E's and IID's reasoning, the cost of properly incurred Imbalance Energy would be borne by the entire market, instead of by the entity whose Schedules occasioned the costs.[7] Significantly, both SDG&E and IID side step the Arbitrator's explicit adoption of the cost-spreading rationale rejected by the Commission in Opinion No. 458. *See* ISO Br. at 49.

Finally, SDG&E's briefed position on Opinion Nos. 458 and 458-A (similarly, as the ISO has noted in its Initial Brief, ISO Br. at 51, to its position on its liability for the Transmission Loss differentials) is inconsistent with its actual practice. While contending that Opinion Nos. 458 and 458-A are irrelevant to this proceeding, SDG&E acknowledges that the costs that it sought to recover in the proceedings leading up to Opinion Nos. 458 and 458-A are the same costs at dispute in this proceeding. SDG&E Br. at 34. Although SDG&E states that there is nothing inconsistent about a utility recovering costs at the same time it challenges them, it neglects to note that it was *not* doing so "at the same time." SDG&E started recovering the cost differentials for Transmission Losses through its Transmission Owner Tariff at the very beginning of ISO Operations in 1998. *See* Exhibit ISO-22 (R. 2441-42). The earliest date SDG&E can identify with any personal knowledge for raising the issue with the ISO, and certainly the earliest

[7] The ISO has previously noted its support of SDG&E and other parties in the Petition for Review of Opinion Nos. 458 and 458-A which, because of the nature of some Existing Contracts, would allow these costs to be trapped with Participating Transmission Owners rather than borne by the responsible party or recovered through repayment of the Transmission Revenue Requirement. As long as Opinion Nos. 458 and 458-A remain valid, however, SDG&E cannot escape the consequences.

date on which a formal dispute commenced, was *after* the Initial Decision indicated that SDG&E could not recover the costs. *See* Tr. at 86 (R. 1169).[8]

B. Intervenors Repeat the Arbitrator's Errors Regarding Operating Control

Both SDG&E and IID devote considerable portions of their reply briefs to a discussion of the evidence regarding whether SDG&E intended to convey Operational Control of the APS- and IID-owned portions of SWPL to the ISO. The ISO has fully discussed that issue in its Initial Brief, and believes that the evidence refutes the claims made by SDG&E and IID. What is of greater significance is the legal error underlying the Arbitrator's use of the evidence.

As the ISO previously indicated, the foundation of the Arbitrator's decision is his conclusion that SDG&E "could not and did not" transfer those portions of SWPL owned by APS and IID to the ISO's Operational Control. Conclusion of Law # 3, R. 4359. From this he deduced that those portions of the line were not part of the ISO Controlled Grid and not subject to the ISO Tariff methodology governing charges for Transmissions Losses.

With the exception of APS, Intervenors' arguments concerning Operational Control essentially perpetuate the Arbitrator's misunderstanding of Operational Control. SDG&E insists that record evidence supports the

[8] Although SDG&E cites, as "fully supported by the record," the Arbitrators' finding that the dispute first arose in 1998, the *only* evidence SDG&E can cite relates to late 1999. SDG&E Br. at 35. In fact, SDG&E's own internal documents demonstrate beyond dispute that it was aware even prior to ISO operations that it would be required under Scheduling Protocol Section 4.3 to pay the ISO Transmission Loss charges on the APS/IID SWPL transactions and reconcile any differences under the Existing Contracts directly with APS and IID. *See* February 23, 1998 email to David Korinek, ISO Exh. 20 (R. 2435).

Arbitrator's conclusion that Operational Control of the APS and IID portions of SWPL had not been turned over to the ISO.

SDG&E notes, first, that neither APS nor IID have signed the Transmission Control Agreement ("TCA"). It also notes that SDG&E does not own the portions of SWPL at issue. SDG&E Br. at 24. Neither is a prerequisite the ISO's Operational Control of an Entitlement. Except in such circumstances when a Participating TO has an Existing Contract with another Participating TO, the situation that SDG&E describes – that the owner of the transmission line has not signed the TCA and the Participating TO does not own the transmission line – aptly describes any Entitlement under the ISO's Operational Control. This fact does not, however, diminish the nature of the ISO's Operational Control. Additionally, SDG&E, argues that the APS and IID portions of SWPL are not comparable to Existing Rights, because SDG&E has only non-firm scheduling rights. SDG&E Br. at 25. As the ISO has previously explained, scheduling rights are not a prerequisite to Operational Control.[9] Many facilities are placed under the ISO's Operational Control subject to Encumbrances, such that the ISO does not have Scheduling rights on the encumbered portion of the capacity. The ISO nonetheless can charge the Participating TO for Transmission Losses on the capacity under the ISO's Operational Control. ISO Initial Br. at 27-28.

SDG&E also argues that the Control Area operator responsibilities it had at the time of the transfer accorded it no right to convey Operational Control because they entail no scheduling right or ability to assure non-discrimination.

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[9] *See* footnote 6.

SDG&E Br. 25. As explained in the ISO's Initial Brief, however, Operational Control does not necessarily require scheduling rights, and the ability to assure nondiscriminatory transmission is the purpose for which the ISO may direct Participating TOs in the exercise of Operational Control, not the definition of Operational Control.[10] ISO Initial Br. 25-26.

IID makes similar arguments, contending that SDG&E could not convey Operational Control because it had neither ownership nor contractual rights to the APS or IID shares in SWPL, noting that the Participation Agreement impliedly limited the rights of parties to transfer other parties' transmission capability, and arguing that the TCA does not address ISO Operational Control of transmission facilities in which the Participating TO does not have ownership or contractual rights. IID Br. at 32-34. These arguments fail for the same reasons discussed above. Unlike APS, SDG&E and IID do not recognize that Operational Control is more than one dimensional. It is not just ownership and contractual scheduling rights. In its brief, APS offers a tripartite model of Operational Control: Control Area Operation (balancing function); Physical Operational Control (transmission equipment operation, maintenance, outage, scheduling, monitoring, and disturbance/emergency response); and Commercial Operational Control

[10] Southern California Edison ("SCE") has filed a Reply Brief that does not take a position on the merits of the instant dispute, but challenges the ISO's discussion of the meaning of Operational Control. SCE's position appears to be primarily an exercise in semantics, in that it does not contend that its limitation on the definition of Operational Control should control the outcome of this proceeding or have any other specific impact on the ISO's authority. Nonetheless, the arguments against defining Operational Control according to the purpose of directions to Participating TOs, rather than by the types of directions, are equally applicable to SCE's arguments. In particular, it should be noted that such a narrow definition is not necessary in order to define Transmission Revenue Requirements properly. *See* So. Cal. Ed. Br. at 3, n. 2. For example, SDG&E Operational Control over the APS and IID portions of SWPL that it conveyed to the ISO, which does not involve physical ownership or contractual payments, does not entail a revenue requirement.

(managing transmission rights and commercial use of the transmission system). APS Br. at 7-8. Although the ISO does not necessarily endorse this particular model,[11] APS's model illustrates the failure of the positions taken by the Arbitrator, SDG&E and IID. By focusing exclusively on "Commercial Operational Control," they fail to comprehend the nature of the Operational Control that SDG&E transferred to the ISO.

Thus, in all of its evidentiary rebuttal to the ISO's arguments, SDG&E misses the essential point. The ISO has not claimed that SDG&E conveyed to the ISO, or had the right to convey to the ISO, Operational Control of the entirety of SWPL in derogation of the joint ownership and of APS' and IID's rights. It does not claim that SDG&E transferred APS's rights as Operating Agent of the Arizona portion of SWPL (APS Br. at 8-9) or that it transferred APS's or IID's rights to Schedule on the line. As the ISO noted in its Initial Brief, "The Arbitrator identifies nothing, and indeed the Participation Agreements include nothing, that would have prevented SDG&E, when transferring to the ISO's Operational Control the portions of SWPL it owns, from also transferring to the ISO *those rights and obligations that it had under the Participation Agreements and as Control Area Operator* regarding the portions of SWPL owned by APS and IID."[12]

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[11] For example, the ISO believes that it performs much of what APS denominates Physical Operational Control regarding even the East of River portion of SWPL.

[12] APS indicates its Interconnected Control Area Operations Agreement with the ISO to point out that the ISO could not abrogate contractual rights, can only assume rights belonging to Participating Transmission Owners under Existing Contracts, and must operate transmission facilities in accordance with existing contractual agreements. APS Br. at 9. Although the Interconnected Control Area Operations Agreement is of questionable relevance here, because SWPL is entirely within the ISO Control Area, the ISO does not disagree with these principles. The ISO is not attempting to violate the contractual terms of the Participation Agreement or how APS pays SDG&E for Transmission Losses under the Participation Agreement. The ISO is only concerned with how

ISO Br. at 22. This is the significance of "co-owned" and "Encumbrance." *See* SDG&E Br. 27-28.

Placing facilities under the ISO's Operational Control "subject to . . . joint ownership and joint participation agreements" means just what it says: conveying to the ISO all rights except those protected by the agreements. *See* SDG&E Br. at 26. Under circumstances where undivided ownership shares are involved and the conveying party is the scheduling agent and Control Area operator, some of the Operational Control will involve the entire line.

In particular, in this case even APS admits that the ISO's Operational Control of the APS and IID portions of SWPL involves at a minimum what APS would call Control Area operation, which includes the balancing function for the entire line. *See* APS Br. at 11. The balancing function by definition includes accounting for Transmission Losses, which the ISO performs pursuant to its tariff.[13]

Although APS properly notes that it reimburses SDG&E in-kind for Transmission Losses,[14] APS Br. at 12, this reimbursement affects APS' responsibility to SDG&E, *not* SDG&E's cost responsibility to the ISO. Although APS is correct that the APS-owned portion of SWPL is located in Arizona, and serves loads in Arizona using Wheel-through transactions with the ISO, all of

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SDG&E pays the ISO for Transmission Losses.

[13] SDG&E's reference to the Section 7.4 methodology for the calculation of Transmission Losses is incomplete. Transmission losses are calculated for Generators and Imports according to, inter alia, ISO Tariff Sections 2.2.10.5, 7.4.2, and Scheduling Protocol Section 4.2.

[14] Contrary to APS's assertion, the ISO's Initial Brief recognized this reimbursement. ISO Br. at 4-5.

SWPL is in the ISO Control Area; thus, the ultimate responsibility for Transmission Losses on SWPL will fall upon the ISO. The significant fact here is that APS's reimbursement through in-kind Energy is made to SDG&E, not to the ISO. Nothing prevents SDG&E from selling that Energy for its own profit. Even if the in-kind Energy or its value were conveyed to the ISO, other Scheduling Coordinators would bear the cost differential between the value of the in-kind Energy and the Transmission Losses as determined by the Commission-approved methodology followed by the ISO. This, of course, is precisely the circumstance that Section 2.4.4.4.4.5, Scheduling Protocol Section 4.3 and Opinions 458 and 458-A address.

It is worth noting that SDG&E has indicated an intention to net the value of its in-kind reimbursement against any award in this proceeding. In doing so, SDG&E acknowledges the ISO's authority to provide and charge for Imbalance Energy to cover Transmission Losses. Because the ISO's authority must arise from its tariff, this acknowledgement is in direct contradiction to SDG&E's other arguments.

In short, the defenses offered by Intervenors are an exercise in digression and obfuscation.[15] The Operational Control that SDG&E has transferred to the

[15] SDG&E's and IID's efforts to analogize this proceeding to Amendment No. 2 to the ISO Tariff are off the mark. SDG&E Br. at 22; IID Br. at 34-35. Despite IID's fanciful readings, IID Br. at 36, nothing in this ISO's Brief suggests a reading of Operational Control that would encompass all facilities in the ISO Control Area, and the ISO is not herein attempting to so expand its authority. The ISO has never suggested but that its Operational Control is defined by the TCA. The Operational Control issue simply involves the much narrower question of the nature of ISO's Operational Control on jointly owned facilities that have indisputably been placed under ISO's Operational Control by the TCA subject to joint participation and joint ownership agreements. IID's reliance on the COTP arbitration, IID Br. at 34, is also misplaced; that arbitration remains pending before the Commission.

ISO does not include or interfere with the rights of APS or IID; rather, it is subject to those rights and only includes those rights SDG&E possesses under the Participation Agreements, its ownership of SWPL, and its Control Area responsibilities. The only question here is whether the Operational Control that SDG&E transferred to the ISO regarding SWPL includes SWPL as part of the ISO Controlled Grid for the purposes of the Transmission Loss calculation methodology. Because the calculation and replacement of Transmission Losses was part of SDG&E's "bundle of rights" in SWPL when it placed SWPL under the ISO's Operational Control, the whole of SWPL is within the ISO's Operational Control for that purpose (albeit still subject to protections provided to APS and IID). As the ISO has shown above and in its Initial Brief, Commission orders and policy, as well as prior dealings, demonstrate that that SDG&E is responsible for the cost of Transmission Losses calculated according to the ISO methodology.

II. SDG&E's Efforts to Disavow Its Status as Scheduling Coordinator for the APS and IID Schedules Is Unavailing

SDG&E and IID also attempt to support the Arbitrator's conclusion that SDG&E is not the Scheduling Coordinator for the APS and IID Schedules.[16] The ISO has fully addressed the first such argument – that those schedules do not take place on the ISO Controlled Grid – and will not repeat that response. Even if the Schedules are deemed not to occur on the ISO Controlled Grid, however, SDG&E would still remain the Scheduling Coordinator.

[16] SDG&E does not actually assert that the issue of its status as a Scheduling Coordinator for the APS and IID Schedules on SWPL is relevant to its liability for the Transmission Loss cost differentials. Rather, it considers the issue relevant only to whether it is subject to the time bars of Section 11.7.2 and 11.7.3 of the ISO Tariff. SDG&E Br. at 55. IID does not discuss the relevance of the issue. IID Br. at 43-44.

SDG&E focuses first on the Scheduling Coordinator Agreement, noting that it governs all aspects of scheduling Energy and Ancillary Services on the ISO Controlled Grid and requires Scheduling Coordinators to abide by all obligations of the ISO Tariff, including those matters regarding the scheduling of Ancillary Services on the ISO Controlled Grid. SDG&E Br. at 50. These are words of inclusion, however, not exclusion. SDG&E also points to the definition of Scheduling Coordinator as an entity certified to undertake the functions identified in Section 2.2.6, and states that those functions are submitting Schedules for Market Participants, which in turn are defined as entities participating "in the Energy marketplace through buying, selling, transmission, or distribution of Energy or Ancillary Services *into, out or, or through the ISO Controlled Grid*." SDG&E Br. at 52. SDG&E neglects to note that the there are nine other functions specified in Section 2.2.6, including "Paying the ISO charges in accordance with this ISO Tariff" and "Including in its Schedules to be submitted to the ISO under this ISO Tariff, the Demand, Generation and Transmission Losses necessary to give effect to trades with other Scheduling Coordinators." Nothing in Section 2.2.6 indicates that Scheduling Coordinators can only perform functions in connection with transactions that involve the ISO's markets or the ISO Controlled Grid. To the contrary, the Commission has recently ruled that Scheduling Coordinators may be responsible for charges in connections with behind-the-meter schedules that occur on facilities that have not in any manner been identified in a TCA.

III. SDG&E Cannot Justify Its Failure to Comply With ISO Tariff Sections 11.7.2 and 11.7.3.

The ISO has explained that SDG&E is the Scheduling Coordinator for Schedules on the APS and IID portions of SWPL (ISO Br. at 5-6) and that, even if it is not, is obligated to comply with the timelines of Section 11.7.2 and 11.7.3 of the ISO Tariff regarding any billing disputes in connection with those Schedules. Id. at 6-7. Those issues are fairly before the Commission, and the ISO need not repeat its arguments; they have not changed. The ISO cannot let stand, however, SDG&E's assertions that it "repeatedly" tried to resolve this dispute after if first came to its attention in April 1998. SDG&E's support for this contention is testimony of its witness that it "consulted" with the ISO to "seek implementation of the Participation Agreement transmission loss methodology." Exh. SD-17 (R. 3197); SDG&E Br. at 57. This is not *by any stretch of the imagination* a dispute of a settlement statement. SDG&E additionally claims that Mr. Yari "raised the issue" or his predecessor "tried to resolve the dispute", but beyond these vague recollections, SDG&E offers no record of such an effort and no date. Mr. Yari asserts he raised the issue in late 1999 or early 2000, and his precedessor "long before." The ISO has no documentation that such conversations occurred, and submits that SDG&E has presented insufficient evidence even to support a factual finding that the ISO was "on notice," and, even if it were, when.

As discussed in the ISO's Initial Brief, the evidentiary record establishes, and the Arbitrator made no contrary finding, that of the various charge types for which SDG&E makes a claim (Charge Types 404, 405, 407 and 487), SDG&E

failed to submit an electronic dispute form for all but Charge Type 487. Even then, SDG&E failed to submit a dispute form for Charge Type 487 until December of 2000. *See* Exh. ISO-13, p. 6 (R. 2354); *See also* at pp. 90-92 (R. 1173-75); *see also* Exh. ISO-24 (R. 2446). Since this proceeding does not concern, and SDG&E does not allege, a denial of a re-run by the ISO Governing Board, Sections 11.7.2 and 11.7.3 preclude SDG&E's claims for amounts that were not disputed under those sections.

CONCLUSION

For the reasons stated above, the ISO respectfully requests that the Commission reverse the decision of the Arbitrator.

Respectfully submitted,

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Dated: April 6, 2004

CERTIFICATE OF SERVICE

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

Dated at Folsom, California this 6th day of April, 2004.

/s/ Beth Ann Burns

Beth Ann Burns

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