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FEDERAL ENERGY  
REGULATORY COMMISSION

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

Pacific Gas and Electric Company	)	Docket Nos. ER01-2998-000
	)	and ER02-358-000
Northern California Power Agency	)	
	)	
v.	)	Docket No. EL02-64-000
	)	
Pacific Gas and Electric Company	)	
and the California Independent	)	
System Operator Corporation	)	

**REPLY COMMENTS OF THE  
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

Pursuant to Rule 602(f)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.602(f)(2), the California Independent System Operator Corporation ("ISO") hereby submits its reply to the comments on the Offer of Settlement submitted by the Modesto Irrigation District ("MID"). As explained herein, MID's opposition to a portion of the comprehensive settlement package is without merit and will disrupt the ISO's implementation of the agreement. As explained below, the Commission should accept both the Offer of Settlement in the above-captioned docket and the ISO's companion filing of Amendment No. 46 in Docket No. ER02-2321-000, without modification.

The Offer of Settlement and Amendment No. 46 provide for an orderly transition for the Northern California Power Agency ("NCPA"), Silicon Valley Power ("SVP"), and the City of Roseville, California ("Roseville") from their historic interconnection agreements with Pacific Gas and Electric Company ("PG&E") to the new California

marketplace and transmission regime administered by the ISO. This is accomplished by permitting these governmental entities to operate as metered subsystems (“MSS”). As NCPA has recognized, with these agreements “the CAISO, NCPA, SVP, and Roseville have found a means of coexisting which preserves the ability of the MSS entities to perform essential utility functions to serve their customers.”<sup>1</sup>

## **I. BACKGROUND**

In Amendment No. 27 to the ISO Tariff, the ISO proposed a new rate methodology for recovery of its transmission Access Charge.<sup>2</sup> Amendment No. 27 also included provisions to enable New Participating TOs to qualify as MSSs to facilitate their continued operation as vertically integrated utility systems while also providing an alternative way to participate in the ISO's markets and to use the ISO Controlled Grid for transactions with their surplus resources. These changes were reflected in Section 3.3 of the ISO Tariff. The Commission accepted Amendment No. 27 subject to refund and hearing and suspended the hearing pending settlement procedures. These settlement proceedings are ongoing.

Following the Amendment No. 27 filing, only one governmental entity, the City of Vernon, California, has joined the ISO as a Participating Transmission Owner.<sup>3</sup> In the January 2002 Operational Audit sponsored by the Commission, the auditor identified the absence of broad municipal participation in the ISO as a significant problem that needed

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<sup>1</sup> Comments of NCPA in Docket No. ER02-1656-003 filed on July 19, 2002 at p. 3.

<sup>2</sup> Capitalized terms not otherwise defined herein have the meaning conained in the Master Definition Supplement, Appendix A to the ISO Tariff.

<sup>3</sup> Although recently, four additional governmental entities: the Cities of Anaheim, Azusa, Banning and Riverside, California have filed Notices of Intent to become Participating Transmission Owners effective January 1, 2003.

addressing. As explained below, the MSS agreements with NCPA, SVP, and Roseville, coupled with the recent applications of four municipal utilities to become Participating Transmission Owners, demonstrate that the ISO has made significant strides in this direction.

On August 30, 2001, PG&E filed a Notice of Termination of the Interconnection Agreement (“IA”) dated September 14, 1983 among it and the NCPA and ten of its member utilities, including the City of Roseville, and a proposed replacement Interconnection Agreement among PG&E, NCPA and nine of NCPA’s member utilities.<sup>4</sup> On November 16, 2001, PG&E filed a Notice of Termination of the 1983 Interconnection Agreement between it and the City of Santa Clara’s electric utility, SVP, and a proposed replacement Interconnection Agreement (“RIA”) between PG&E and SVP. On February 27, 2002, NCPA filed an Emergency Petition For Declaratory Order against PG&E and the ISO seeking, among other relief, a technical conference to resolve disputed issues regarding ongoing contractual rights under agreements other than the current NCPA IA and operational questions related to the change to ISO Tariff requirements.

On March 14, 2002, the Commission issued an order conditionally accepting the Notices of Termination and the RIAs, suspending their effectiveness until September 1, 2002. That order directed that a technical conference be held to resolve issues regarding the effect of terminating the current NCPA IA and the current SVP IA on other agreements involving transmission service to NCPA, Roseville and SVP.

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<sup>4</sup> Since Roseville is connected to the Western Area Power Administration and not PG&E, the replacement IA does not include Roseville.

Through the extensive efforts of all parties and greatly facilitated by Commission staff, the parties to these proceedings were able to reach a comprehensive settlement.

Section IV.E.5 of the Offer of Settlement states:

The Parties recognize that the ISO will, concurrent with the filing of this Settlement Agreement, make a filing pursuant to Section 205 of the Federal Power Act with FERC of the NCPA MSS Aggregator Agreement ..., the Roseville Metered Subsystem Agreement ..., the SVP Metered Subsystem Agreement ..., and the revised ISO Tariff language reflecting the changes in MSS terms and conditions.... The Parties to this Settlement Agreement agree to support or not oppose a filing that incorporates the ISO Tariff provisions and agreements in the form attached; however, the Parties may intervene and participate in any FERC or appellate proceeding regarding this filing.

To fully incorporate those changes, the ISO made a filing on July 15, 2002 in Docket No. ER02-2321 consisting of the proposed ISO Tariff amendments needed to implement the MSS agreements; the NCPA MSS Aggregator Agreement; the City of Roseville Metered Subsystem Agreement; and the Silicon Valley Power Metered Subsystem Agreement.

## **II. ARGUMENT**

### **A. MID Has Not Raised an Issue of Material Fact that Could Prevent Commission Consideration of the Offer of Settlement.**

Under Rule 602(f) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.602(f)(4), a party contesting an Offer of Settlement by alleging a dispute as to a genuine issue of material fact, "must include an affidavit detailing any genuine issue of material fact." MID neither demonstrated the existence of a genuine issue of material fact nor included such an affidavit. Its opposition to the Offer of Settlement therefore does not render the settlement contested within the meaning of the Commission's rules. Rather, MID's opposition is based solely on policy grounds. The Commission has held

that, if a party's opposition to a proposed settlement concerns a matter of policy, it can resolve the matter without development of a record. *Koch Gateway Pipeline Co.*, 74 FERC ¶ 61,088, 61,270-71 (1996). Accordingly, MID's comments do not prevent Commission consideration and acceptance of the Offer of Settlement.

**B. The ISO's Tariff Amendment Is a Necessary and Proper Means To Effectuate the Agreements Allowing NCPA, SVP, and Roseville To Transition From Their Historic Interconnection Agreements To the New ISO Market Structure While Still Protecting Their Core Interests.**

The Offer of Settlement resolved a number of difficult transitional issues concerning the termination of the IAs that existed prior to the formation of the ISO and the need to accommodate the business practices of these governmental entities within the framework of the new market and the transmission service protocols. It is the result of enormous efforts on the part of the Commission staff to facilitate a mutually acceptable outcome. That the Offer is an appropriate compromise is reflected by the fact that it is supported by the affected investor owned utility, PG&E, as well as NCPA, SVP, Roseville, and the ISO.

Most importantly, the settlement is a comprehensive package and the ISO's filing of a tariff amendment to implement the agreement is a necessary and proper means to effectuate the agreement. In accordance with the Section IV.A.1. of the Offer, "This Settlement is contingent upon Commission acceptance of ... the NCPA MSS Aggregator Agreement, the SVP Metered Subsystem Agreement, the Roseville Metered Subsystem Agreement, and the Metered Subsystem-related provisions of the ISO Tariff."

The ISO Tariff must be amended to effectuate the parties' intent as expressed in the Offer of Settlement. For example, under the existing ISO Tariff Section 3.3, only a New Participating TO could qualify as an MSS. Under the proposed amendment, any

entity that is determined by the ISO to qualify as an MSS and that undertakes in writing to comply with the applicable provisions of the ISO Tariff shall be considered an MSS Operator and shall have the rights and obligations set forth in a revised Section 23 of the ISO Tariff. (Section 23.1.1)

The tariff amendments also specify the cost responsibilities of the MSS. The ISO will assess the MSS Scheduling Coordinator ("SC") the neutrality adjustments and Existing Contracts cash neutrality charges pursuant to Section 11.2.9 (or collect refunds therefor) based on the net metered Demand and exports of the MSS. (Section 23.15.1) If the ISO is charging SCs for summer reliability or demand programs, the MSS Operator may petition the ISO for an exemption from these charges provided the MSS Operator can show that it has its own peaking and/or demand programs. The ISO will grant an exemption from these charges if the MSS Operator demonstrates by November 1 that it has secured generating capacity<sup>5</sup> for the following year at least equal to 115% of the peak Demand responsibility of the MSS Operator.<sup>6</sup> (Section 23.15.2). If the ISO is compensating Generating Units for emissions and start-up costs, and if an MSS Operator charges the ISO for the emissions and start-up costs of the MSS's Generating Units serving the Load of the MSS, then the MSS Scheduling Coordinator shall bear its proportionate share of the total amount of those costs incurred by the ISO based on the MSS gross metered Demand and exports, and the Generating Units shall be made available to the ISO through the submittal of Supplemental Energy bids. If the

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<sup>5</sup> Eligible generating capacity for such a demonstration may include on-demand rights to Energy, peaking resources, and Demand reduction programs.

<sup>6</sup> The peak Demand responsibility of the MSS Operator equals the annual peak Demand Forecast of the MSS Load plus any firm power sales by the MSS Operator, less interruptible Loads, and less any firm power purchases.

MSS Operator chooses not to charge the ISO for the emissions and start-up costs of the MSS's Generating Units serving its Load, the MSS SC will bear its proportionate share of the total amount of those costs incurred by the ISO based on the MSS's net metered Demand and exports. The MSS Operator must make the election whether to charge the ISO for these costs on an annual basis on November 1 for the following calendar year. (Section 23.15.3). The MSS SC will be responsible for transmission losses only within the MSS, at any points of interconnection between the MSS and the ISO Controlled Grid, and for the delivery of Energy to the MSS or from the MSS, provided the MSS Operator fulfills its obligation to provide for transmission losses on the transmission facilities forming part of the MSS. (Section 23.15.4) For internal Generation serving internal Load, the ISO will be using a GMM of 1.0. If internal Generation is used to serve Load outside the MSS boundary, then the ISO will assign a GMM in accordance with the ISO Tariff requirements.

Additionally, the proposed tariff amendment addresses a concern in California regarding blackouts needed solely because one or more Scheduling Coordinators have made an economic decision not to procure sufficient resources to meet their Load responsibility and the ISO's BEEP stack is insufficient to meet all of the Control Area needs. Thus, a distinction will be made between System Emergencies associated with an entity's resource deficiency or failure to maintain an Approved Credit Rating, and System Emergencies associated with operational contingencies, which will be set forth in part in the agreements and in part in proposed ISO Tariff amendment provisions. The agreements will provide that a UDC or MSS will not be obligated to shed Load or commit excess generating capacity or Energy in the case of System Emergencies

associated with an entity's resource deficiency or failure to maintain an Approved Credit Rating, subject to compliance with market mitigation requirements. Thus, this addition impacts the entire Control Area, not just the new MSSs.<sup>7</sup> The ISO Tariff amendment provisions provide that if the ISO must curtail Load, and an entity is short of resources to serve its Load because it did not procure sufficient resources, then only that entity will be required to shed Load. The ISO's filing letter in Docket No. ER02-2321 more fully discusses the scope and basis of the proposed tariff modifications.

**C. The Specific Concerns Raised by MID Are Without Merit**

1. MID's Insistence that the ISO Must Proceed By Means of Bilateral Contracts Instead of Generally-Applicable Tariff Requirements Should Be Rejected

MID argues that "generically imposing ISO Tariff rules is unnecessary and harmful to the market." MID Comments at 3. This contention fundamentally misperceives the function of the ISO Tariff. Ensuring non-discriminatory open access through a tariff of general applicability is the ISO's core mission. Moreover, the issues addressed in the proposed tariff amendment -- eligibility, cost responsibility, and curtailment -- are not the type of issues that should be addressed in bilateral agreements. Instead, to ensure comparable treatment for all transmission customers, they are appropriately included in the ISO Tariff.

Furthermore, MID's cite to the recent D.C. Circuit case<sup>8</sup> as a limit on the Commission's authority to require uniformity is inapposite. In this instance, the

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<sup>7</sup> Currently the ISO has 8 UDCs, consisting of PG&E, Edison, SDG&E, Vernon, Anaheim, Riverside, Pasadena, and Lassen.

<sup>8</sup> MID comments at 4 citing *Atlantic City Electric Co. v. FERC*, No. 97-1097 (D.C. Cir., Decided July 12, 2002).



Commission is not imposing uniformity on regulated public utilities. To the contrary, it is the ISO -- the regulated public utility with the Section 205 filing rights, that is proposing to employ uniform rules, as set forth in its tariff, to provide assurances to transmission customers that they will not suffer undue discrimination. Nothing in the D.C. Circuit's decision, or any other appellate ruling, limits the ability of a regulated public utility to propose and implement tariff provisions for that purpose. Additionally, with the Commission's recent rule making on Revised Public Utility Filing Requirements, Order No 2001, 67 FR 31043 FERC ¶ 31,127, the Commission is moving to a paradigm of standard agreements where terms and conditions are included in a public utilities' tariff and bilateral contracts are replaced by *pro forma* service agreements.

2. MID Appears More Intent on Repeating Its Old Protests Regarding the ISO's Amendment No. 27 Filing Without Recognizing the Actions the ISO has Taken To Address Its Concerns

MID is correct that the ISO is significantly modifying the MSS provisions filed in Amendment No. 27. However, MID's contention that the combination of approval of the Offer of Settlement and Amendment No. 46 could prejudice their protest of Amendment No. 27 is groundless. MID Comments at 10. There is nothing in the Federal Power Act or the Commission's regulations or precedents that precludes a public utility from presenting revised proposals that address concerns raised about previous, pending tariff amendments. MID appears more concerned with rehashing its protest to Amendment 27 than in recognizing the additional accommodations the ISO has made to facilitate the participation of governmental entities.

Although Amendment No. 27 was submitted following an extensive stakeholder process, the ISO agrees that the MSS provisions in Amendment 27 were not a

"consensus product." MID Comments at 7. Amendment No. 46, however, is explicitly incorporated in the Offer of Settlement supported by a broad coalition of municipal utilities as well as an investor owned utility. The Offer of Settlement and the companion ISO Tariff amendments demonstrate that the ISO has worked with interested parties to develop an effective means of addressing the concerns of municipal utilities.

MID's complaint that Amendment No. 27 "failed to accommodate the special needs of municipal utilities" (MID Comments at 7) is thus beside the point. The subject of the instant proceedings is not Amendment No. 27 but Amendment No. 46 and the Offer of Settlement. That package has the overwhelming support for the affected entities. As NCPA recently stated:

It is important not to lose sight of the fact that in the MSS Agreements, the CAISO, NCPA, SVP, and Roseville have found a means of coexisting which preserves the ability of the MSS entities to perform essential utility functions to serve their customers. These functions include the ability to follow load, to control our own generation for the benefit of our customers and the ability to protect our customers from curtailments in situations when our utilities are fully and prudently resourced and others are not because they cannot or will not pay the costs of doing so.<sup>9</sup>

Similarly, MID's complaint that Amendment No. 27 required municipal utilities to "convert" their existing transmission contracts and "join" the ISO to obtain MSS status (MID Comments at 7) fails to acknowledge is that the Amendment No. 46 and the Offer of Settlement do *not* include this requirement. The current proposal thus accommodates concerns expressed by MID and others regarding this aspect of Amendment No. 27. MID's repetition of this objection to the earlier proposal plainly presents no basis for rejecting Amendment No. 46 or the Offer of Settlement.

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<sup>9</sup> Comments of NCPA in Docket No. ER02-1656-003 filed on July 19, 2002 at 3.

MID also contends that governmental entities, like other market participants, would be subject to service under a contract that has the potential to be modified after FERC approval, pursuant to Section 205. MID Comments at 7. The possibility that a transmission tariff could be modified is not a new concept. Indeed, it is incorporated in the Commission's own pro forma open access tariff in Order No. 888.<sup>10</sup> A reservation of tariff modification rights is of particular importance as the industry moves to regional markets and standardized market design. If experience over the first few years of restructured electricity markets proves anything, it is that flexibility to respond to changing conditions and unforeseen developments must be preserved. Furthermore, even under a bilateral contract, the transmission provider can preserve the right to propose changes unilaterally to the Commission. MID incorrectly presumes that the ISO would waive these Section 205 rights in a bilateral contract.

With regard to MID's principles (MID Comments at 8-10),<sup>11</sup> the ISO notes:

- (1) The revised MSS program accomplishes Principle 1 by allowing the MSS to remain vertically integrated and not requiring ETC conversion.
- (2) The amendment reaches an accommodation on which charges should be charged on a net basis and which should be assessed on a gross basis. MID's position that all charges should be net (MID Comments at 9) has been expressly rejected by the Commission.<sup>12</sup>

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<sup>10</sup> See Section 9 of the Order No. 888 *pro forma* tariff.

<sup>11</sup> These principles are as follows: (1) The form of the MSS shall reflect the right of the publicly owned utility to operate as a full service utility within the ISO's control area; (2) all ISO charges should be on a net basis; and (3) the amount of MSS resources available to the ISO shall be limited to the amount of MSS resources actually reserved by the ISO for that time.

<sup>12</sup> See, for example, the Commission's order of May 15, 2002,

We will deny intervenors request for rehearing that the Commission erred in its decision to accept Control Area Gross Load as a billing determinant. As we stated in the December 19 Compliance Order, the use of total gross load is the most appropriate method to assess emissions and start-up costs because all users of the transmission grid

(3) The revised MSS program accomplishes Principle 3.

MID's only remaining concerns appear to be that the MSS Operator must comply with the ISO Tariff as it may be amended, following Commission approval, from time to time and that MID will have to have its resources "processed through the ISO Markets". MID Comments at 11 and 12. As noted above, the possibility that a transmission tariff could be modified is not a new concept and that a reservation of tariff modification rights is of particular importance given the ongoing market redesign and market standardization activities. With regard to MID's protest that the agreement requires resources -- even self-supply -- to be processed through the ISO market, the ISO disagrees that the ISO Tariff impairs, in any way, MID's or any other entities' ability to meet its responsibilities under or receive the benefits of bilateral transactions.

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will be assigned these costs consistent with ISO markets performing a reliability function.  
*San Diego Gas and Electric Company, et al.*, 99 FERC ¶ 61,159, slip op. at 12-13.

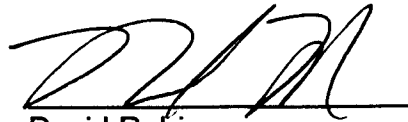
### III. CONCLUSION

Wherefore, for the foregoing reasons, the ISO respectfully requests that the Commission reject MID's comments and accept both the Offer of Settlement in the above-captioned docket and the ISO's companion filing of Amendment No. 46 in Docket No. ER02-2321-000, without modification.

Respectfully submitted,



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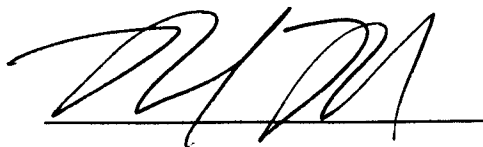
Counsel for the California Independent  
System Operator Corporation

Date: August 5, 2002

## CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing documents upon each person designated on the official service list compiled by the Secretary in this proceeding, in accordance with Rule 385.2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Washington, D.C., on this 5th day of August, 2002.

A handwritten signature in black ink, appearing to read 'DRB', is written over a horizontal line.

David B. Rubin