

No Argument Date Set

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

California Independent System Operator Corporation))	
and California Electricity Oversight Board,))	
Petitioners))	
)	
v.))	Nos. 98-1225 and
)	98-1226
Federal Energy Regulatory Commission,))	(related Docket
Respondent))	No. 98-1384)

**PETITIONER CALIFORNIA INDEPENDENT SYSTEM OPERATOR
CORPORATION’S RESPONSE IN SUPPORT OF OVERSIGHT BOARD’S
APPLICATION FOR A STAY PENDING APPEAL**

On December 21, 1998, Petitioner, the California Electricity Oversight Board (Oversight Board) filed an Application for Stay pending appeal of the November 24, 1998 order¹ of the Federal Energy Regulatory Commission (FERC). That order requires the California Independent System Operator Corporation (ISO) to amend its Bylaws to remove provisions relating to 1) the Oversight Board’s authority to appoint ISO Governing Board members; 2) the right of ISO Governing Board members to appeal majority decisions of the ISO to the Oversight Board; 3) the requirement that ISO Governing Board members be California residents; and 4) the requirement that the Oversight Board approve certain amendments to the ISO Bylaws. The ISO files this response in support of the Oversight Board’s request for a stay pending appeal. Without the stay, the ISO will suffer irreparable injury because 1) it will be operating in a manner that is contrary to the state’s electric restructuring law; and 2) it will either be impeded in conducting necessary legal, regulatory and financial business or will be forced to operate dual

¹ Order Finding Noncompliance, Denying Request for Public Conference, Clarifying Prior Orders and Granting Complaint in Part. *California Power Exch. Corp.*, 85 FERC ¶ 61,263 (1998). (Copy attached to the Oversight Board’s Application for a Stay, as Att. A to Declaration of Erik Saltmarsh.)

forms of governance pending resolution of this appeal. Therefore, the ISO respectfully requests that the Court issue the stay pending review.

I. BACKGROUND

A. Procedural Background

The ISO is a nonprofit public benefit corporation incorporated in California. The ISO operates the electric transmission system belonging to the three investor-owned utilities in the State. Although the investor-owned utilities still own the transmission facilities, the ISO operates them independent of the utilities' control. The ISO was created by the electric restructuring statute as an entity to operate the transmission system in an independent manner as part of a new market structure to increase competition and to provide low cost and reliable electric service in California.

The restructuring effort began in April 1996 with the Phase I filings, which consisted of the application by the three investor-owned utilities in the State requesting FERC's authorization to transfer operation of the transmission facilities to the not-yet established ISO. The Phase I filings included provisions enacted by the California Legislature, requiring that the ISO be governed by a Governing Board whose participation is limited to California residents and that an Oversight Board be established to oversee certain aspects of the ISO's governance and operations.² At the time of the Phase I filings, neither the ISO nor the Oversight Board was yet in existence.

On November 26, 1996, FERC issued its Phase I order conditionally authorizing the establishment of the ISO and the transfer to the ISO of the investor-owned utilities' jurisdictional

² Assembly Bill 1890, signed by Governor Wilson on Sept. 23, 1996, codified as Cal. Pub. Util. Code §§ 337 and 339 (West 1998).

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transmission facilities. *Pacific Gas & Elec. Co.*, 77 FERC ¶ 61,204, at 61,837 (1996) (“November 26, 1996 order”). In that order, FERC rejected certain aspects of the proposed governance structure of the ISO, including the proposals that all members of the ISO Governing Board be residents of the State of California, that the Oversight Board appoint ISO Governing Board members, that the ISO Governing Board members have the right to appeal majority decisions of the ISO Governing Board to the Oversight Board, and that the Oversight Board approve certain amendments to the ISO Bylaws. FERC stated that once the ISO was established, the Oversight Board’s continued participation in the ISO governance and operations would conflict with FERC’s statutory responsibilities, and that the Oversight Board would only be allowed to serve in a start-up capacity. *Id.*

In accordance with the California State Legislature’s directive in the restructuring legislation, the Phase II filings (this time filed by the ISO Restructuring Trust instead of the three investor-owned utilities) carried forward the California residency requirement for members of the respective Governing Boards, and included provisions implementing the legislation’s mandate of an ongoing role for the Oversight Board. In the Phase II filings, the ISO requested that FERC reconsider the determination it made in its November 26, 1996 order with regard to the residency requirement and the Oversight Board appointment and dispute resolution provisions.

In its Phase II order, on October 30, 1997, FERC again rejected the proposed residency requirement and the provisions regarding the Oversight Board. FERC concluded that these provisions were inconsistent with its November 26, 1996 order and that neither the ISO (which did not yet exist) nor any entity that was a party to the proceeding had filed a request for rehearing of its rejection of these provisions within thirty days following the issuance of the

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November 26, 1996 order. *Pacific Gas & Elec. Co.*, 81 FERC ¶ 61,122, at 61,451 (1997)
("October 30, 1997 order")

The ISO and the Oversight Board filed timely requests for rehearing of FERC's October 30, 1997 order – the first order issued by FERC on the governance issues after either entity came into existence. On March 4, 1998, FERC reaffirmed its earlier determination that the prior requests for rehearing in the Phase II filings were not timely because neither the ISO (which did not yet exist) nor any entity that was a party to the proceeding had requested rehearing of the November 26, 1996 order. *Pacific Gas & Elec. Co.*, 82 FERC ¶ 61,223, at 61,868 (1998) (March 4, 1998 order).³ FERC also adhered to its rejection of the residency requirement and the ongoing Oversight Board governance provisions. *Id.*

On April 30, 1998, the ISO and the Oversight Board filed petitions for judicial review in this Court, seeking review of both the FERC's denial of the rehearing requests and its rejection of the California residency requirement and the ongoing role of the Oversight Board. On June 18, 1998, FERC filed a motion to dismiss the ISO's and Oversight Board's petitions for lack of jurisdiction. On August 20, 1998, in response to FERC's motion to dismiss, a motions panel bifurcated the jurisdictional issue (assigning it to Docket No. 98-1384) and holding the remaining issues on the merits in abeyance until the jurisdictional issue was resolved. On September 11, 1998, the oral argument on the jurisdictional issue was set for May 4, 1999. On November 5, 1998, the ISO requested that the Court consolidate the jurisdictional issue with the merits and hear the full case on May 4, 1999 or expedite the May 4, 1999 oral argument date.

³ Also in the March 4, 1998 order, FERC denied the ISO's motion for a stay of the October 30, 1997 order. 82 FERC at 61,871.

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The ISO stated that because it is subject to conflicting state and federal directives regarding its governance structure, expedition of the appeal was necessary.

On December 7, 1998, this Court granted the ISO's motion to expedite oral argument on the jurisdictional issue and ordered that a new date be set for the oral argument. While the ISO's motion was pending, FERC issued its November 24, 1998 order directing the ISO to amend its Bylaws as directed in the November 26, 1996 and October 30, 1998 orders within 45 days of the date of the order.

B. FERC's November 24, 1998 order

The November 24, 1998 order was issued in response to a complaint filed against the ISO and the Oversight Board in connection with the Oversight Board's action in declining to appoint Eric Woychik as a member of the ISO Board of Governors. In that order, FERC ordered the ISO to file revisions to its Bylaws by January 8, 1999 to remove 1) references to the Oversight Board in the process of appointing Governing Board members, 2) the California residency requirement 3) the requirement that the Oversight Board approve certain changes to the Bylaws and 4) the role of the Oversight Board in hearing appeals of ISO Governing Board decisions. 85 FERC ¶ 61,263, slip op. at 13-14. The Commission also directed the ISO to seat Mr. Woychik as an ISO Governing Board member immediately either (1) for a full term or (2) on an interim basis and conduct another Governing Board election for all members of the Governing Board elected since ISO start-up, consistent with the revised Bylaws.⁴

The November 24, 1998 order was also issued in response to an August 31, 1998 Bylaw-related compliance filing by the ISO requesting that FERC delay enforcement of its November

⁴ On December 16, 1998, the Oversight Board appointed Mr. Woychik to the ISO Governing Board for a full term.

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26, 1996 and October 30, 1997 orders requiring amendments to the Bylaws. *Bylaw Informational Filing at 3 (August 31, 1998)*. The Commission denied the request to defer enforcement of its prior orders and instead directed the ISO to make the required changes by January 8, 1999.

**II. ABSENT A STAY, THE ISO WILL SUFFER IRREPARABLE INJURY
BECAUSE IT WILL BE OPERATING IN A MANNER THAT IS
CONTRARY TO STATE LAW.**

The ISO supports the Oversight Board's application for a stay pending appeal of FERC's November 24, 1998 order. In determining whether a stay should be granted the Court must balance four factors: (1) the likelihood that the party seeking the stay will prevail on the merits of the appeal; (2) the likelihood that the moving party will be irreparably harmed absent a stay; (3) the prospect that others will be harmed if the court grants the stay; and (4) the public interest in granting the stay. *Virginia Petroleum Jobbers Ass'n v. FPC*, 259 F.2d 921, 925 (D.C. Cir. 1958); *Washington Metro. Area Transit Comm'n v. Holiday Tours, Inc.* 559 F.2d 841, 843 (D.C. Cir. 1977). The Oversight Board has met these requirements. The ISO files this pleading in support of that application and to show the irreparable harm the ISO will suffer if FERC's order is not stayed.

A. The ISO is Subject to Conflicting State and Federal Directives Regarding Its Governance Structure.

As a result of FERC's orders, the ISO is subject to conflicting state and federal directives. FERC has ordered the ISO to amend certain provisions of its Bylaws regarding the ISO's current governance structure that were mandated by the California Legislature. But, under the express provisions in its Bylaws, the ISO cannot, without Oversight Board approval, either appoint Governing Board members or change the provisions of its Bylaws dealing with appointment of the Governing Board. Moreover, the ISO's Articles of Incorporation state that "[a]ny bylaws of

this corporation shall be adopted, and amended as necessary, so as to conform to requirements of the Statute [AB 1890] and to written decisions of the Oversight Board made pursuant to the Statute.”

The Oversight Board is precluded from approving the changes ordered by FERC. In compliance with the restructuring legislation, the ISO Bylaws currently require that all appointments to the Governing Board be made by the Oversight Board.⁵ Any changes to the appointment section of the Bylaws require Oversight Board approval. In addition, the Oversight Board is to serve as the appeal board for majority decisions of the ISO Governing Board.⁶ Because the Oversight Board’s powers and duties are codified in California law, the Oversight Board cannot approve the changes requested by the FERC (*e.g.*, remove the Oversight Board appointment authority) without acting in violation of the California Public Utilities Code. Under Article III, Section 3.5, of the California State Constitution, the Oversight Board is required to follow state law until an appeals court upholds the federal preemption. Thus, by law the Oversight Board cannot approve the FERC-ordered amendments the ISO makes unless there is the necessary resolution by a court of appeals.⁷ Because the ISO’s Articles and Bylaws prohibit

⁵ Cal. Pub. Util. Code §§ 335(b) and 337 (West 1998).

⁶ Cal. Pub. Util. Code §§ 335(c) and 339 (West 1998).

⁷ Art. III, Section 3.5(c) states that an administrative agency has no power:

[t]o declare a statute unenforceable, or to refuse to enforce a statute on the basis that federal law or federal regulations prohibit the enforcement of such statute unless an appellate court has made a determination that the enforcement of such statute is prohibited by federal law or federal regulations.

Cal. Const. Art. III, § 3.5(c) (West 1983). *See generally*, *Delta Dental Plan, Inc. v. Mendoza*, 139 F.3d 1289, 1296 (9th Cir. 1998); *Southern Pac. Transp. Co. v. Cal. Public Utils. Comm’n*, 716 F.2d 1285, 1290 (9th Cir. 1983) *cert. denied*, 466 U.S. 936 (1984); *Reese v. Kizer*, 251 Cal. Rptr. 299, 302 (Cal.

certain changes without Oversight Board approval, to make the Bylaw changes required by FERC, the ISO would be acting beyond its corporate powers as prescribed by state law and the ISO's organic documents. Any change would therefore have questionable legal effect.

B. Without the Stay, the ISO Will Suffer Irreparable Injury.

If FERC's order is not stayed, the ISO will have to change its Bylaws as directed in the order to remove the provisions relating to 1) the Oversight Board's authority to appoint Governing Board members; 2) the right of Governing Board members to appeal majority decisions of the ISO to the Oversight Board; 3) the requirement that Governing Board members be California residents; and 4) the requirement that the Oversight Board approve certain amendments to the ISO Bylaws.

Making these changes will cause the ISO to suffer irreparable harm because it will be operating in a manner that is contrary to state law and will either be impeded in conducting necessary legal, regulatory and financial business or will be forced to operate dual forms of governance pending resolution of the appeal.

1. The ISO Will Suffer Irreparable Injury Because the ISO Will Be Operating in a Manner that is Contrary to California State Law.

If the ISO amends its Bylaws according to the FERC order and the Oversight Board does not approve the changes, the ISO will be operating in a manner that is contrary to its organic corporate documents (Bylaws and Articles of Incorporation), and, if, for example, a non-resident is seated on the ISO Governing Board, the ISO will be operating in violation of the California Public Utilities Code. A violation of the California Public Utilities Code (including the now-

1988) (purpose of Section 3.5 was to preclude agencies "from using their own interpretation of the Constitution or federal law to thwart the mandates of the Legislature").

codified sections of AB 1890) is a misdemeanor punishable by a fine of up to \$1000 or imprisonment for up to one year or both. Cal. Pub. Util. Code § 2110 (West 1983). If the Court denies the stay and the state law is upheld on appeal, the Court will have determined that FERC acted beyond its authority. If FERC has acted beyond its authority, the ISO would have been denied its right to due process and therefore would have suffered irreparable harm. *Southern Ohio Coal Co. v. Office of Surface Mining Reclamation & Enforcement*, 831 F. Supp. 1324, 1338 (S.D. Ohio 1993), *rev'd on jurisdictional grounds*, 20 F.3d 1418 (6th Cir. 1994) (finding that action by a federal agency beyond its authority is *per se* irreparable harm); *see also Claridge House, Inc. v. U.S. D.H.H.S.*, 795 F. Supp. 1393, 1405 (S.D. Ohio 1991); *Leedom v. Kyne*, 358 U.S. 184, 189 (1958) (federal courts can enjoin agency action that is outside the jurisdiction of the agency). Moreover, in the event the State's restructuring law is later upheld, the ISO's corporate actions, taken without Oversight Board consent while the appeal was pending, will be under a legal cloud as a matter of state law, making the ISO a target for potential private lawsuits.

2. The ISO Will Suffer Irreparable Injury Because the ISO Will Be Impeded in Conducting Necessary Legal, Regulatory and Financial Business.

The ISO, as a nonprofit public benefit corporation, has a duty to ensure that it serves the interests of electricity ratepayers in California, including a duty not to pass through excessive costs. The ISO has no shareholders or shareholder equity. All of the ISO's costs ultimately have to be collected from its customers – electricity ratepayers. The ISO recently retained a financial advisor and is currently planning to refinance its start-up debt and eliminate a line of credit the ISO has had since the ISO was created. The three investor-owned utilities created the ISO Restructuring Trust to begin the process of creating the ISO. The Restructuring Trust

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obtained a \$310 million line of credit from the Bank of America (BofA) for the purchase of computer and communications equipment and to hire staff for the ISO's (and PX's) start up. The line of credit was guaranteed by the three investor-owned utilities. Currently, the ISO has issued its own bonds and has partially retired the BofA line of credit. The ISO's plan (approved by the ISO Governing Board in November 1998) is to eliminate the BofA line as soon as possible to eliminate unnecessary financing costs. Jacobs Affidavit at 2. Elimination of the line of credit will save the ISO – and electricity ratepayers – more than \$100,000 per month.⁸

To eliminate the BofA line of credit, the ISO will have to execute new financing documents and deliver a standard form of legal opinion stating that the ISO's actions in the refinancing have been validly authorized by the ISO Board of Governors. Jacobs Affidavit at 3. According to the ISO's bond counsel, compliance with FERC's order will prevent the firm from issuing its standard form of legal opinion for the bond issuance absent the ISO maintaining dual forms of governance. Jacobs Affidavit at 3.⁹ As a result, without a stay of the FERC order, the ISO will be unable to refinance its bonds, or undertake other corporate actions absent obtaining an expensive and likely ineffective dual governance structure.

Here, there is no adequate compensatory relief that would be available to redress this harm after the appeal is resolved. The injury to the ISO – and ultimately to rate payers – will be caused by FERC. FERC cannot adequately compensate the ISO after the appeal is resolved.

⁸ In addition, elimination of the BofA line of credit is necessary to ensure that the ISO is completely financially independent of the three investor-owned utilities.

⁹ The ISO's bond counsel stated that the firm would possibly be able to issue the opinion if the ISO were to maintain a "dual track" governing board system. This dual track would require the ISO to maintain two ISO Governing Boards: "Board A," constituted under the FERC-ordered Bylaws, and "Board B," constituted under the State-mandated Bylaws. As discussed in the Affidavit of Richard L. Jacobs, this dual track governance system would likely paralyze the ISO's ability to operate. Jacobs Affidavit at 3.

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Indeed, the ISO's higher costs of doing business, which could continue through the year 2000, will be irreparable because they will not be recoverable from any entity at a later date.

Population Inst. v. McPherson, 797 F.2d 1062, 1081 (D.C. Cir. 1986) (finding that appellant will suffer irreparable harm because this Court will be unable to grant effective relief); *Flechter v. HMW Indus.*, 879 F.2d 1111, 1119 (3d Cir. 1989) (stating that equitable remedies are available once legal remedies are found to be inadequate). Electricity ratepayers in California will have no recourse for their higher electricity costs. *NAACP Legal Defense & Educ. Fund v. Horner*, 636 F. Supp. 762, 765 (D.D.C.), *vacated and remanded on other grounds*, 795 F.2d 215 (D.C. Cir. 1986) (finding that harm is irreparable where loss is incalculable, cannot be recovered from the government and would affect entities performance of services to clients).

CONCLUSION

For the foregoing reasons, the California ISO respectfully requests that this Court grant the Oversight Board's application for a stay pending review of the FERC orders in Docket Nos. 98-1225 and 98-1226.

Respectfully submitted,

N. Beth Emery
Vice President and General Counsel
California Independent System Operator
Corporation
151 Blue Ravine Road
Folsom, CA 95630
Tel: (916) 351-2334
Fax: (916) 351-2350

Stephen Angle
Jerrold J. Ganzfried
Linda L. Walsh
Howrey & Simon
1299 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
Tel: (202) 783-0800
Fax: (202) 383-6610

Counsel for the California Independent System Operator Corporation

December 23, 1998