

May 18, 2005

The Honorable Magalie Roman Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, DC 20426

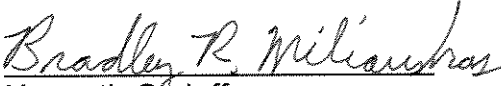
**Re: California Independent System Operator Corporation
Docket No. ER03-683-___**

Dear Secretary Salas:

Enclosed please find the Refund Report of the California Independent System Operator Corporation ("ISO") that will be released to the public, submitted in the captioned docket.

Simultaneous with the instant filing, the ISO is submitting a version of the Refund Report that contains confidential information. In the instant version of the Refund Report, the confidential information, *i.e.*, Attachment B, has been redacted. In all other respects, the version of the Refund Report to be released publicly is identical to the version of the Refund Report that contains confidential information.

Respectfully submitted,


Kenneth G. Jaffe
Bradley R. Miliauskas

Counsel for the California
Independent System Operator
Corporation

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System)
Operator Corporation) Docket No. ER03-683-____

REFUND REPORT OF THE CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CORPORATION

In compliance with the Commission's April 18, 2005 order in the captioned proceeding, 111 FERC ¶ 61,074 ("April 18, 2005 Order"), the California Independent System Operator Corporation ("ISO")¹ submits this refund report.

I. Background

In the Commission's May 30, 2003 order in the captioned proceeding, the Commission required the ISO to "use reference prices for dec[remental] bids to be administered by an independent entity" and directed "the independent entity that determines the reference prices for the AMP [Automated Mitigation Procedures] to develop this decremental bid reference price." *California Independent System Operator Corporation*, 103 FERC ¶ 61,265, at PP 41, 54. On July 18, 2003, the ISO submitted a filing that informed the Commission that it and the independent entity, Potomac Economics ("Potomac"), had agreed on a methodology for calculating decremental reference prices, and in that same filing, the ISO included the methodology in proposed Tariff Section 7.2.6.1.1. Addendum to June 30, 2003 ISO Compliance Filing, Docket No. ER03-683-003

¹ Capitalized terms not otherwise defined herein have the meanings set forth in the Master Definitions Supplement, Appendix A to the ISO Tariff, as filed August 15, 1997, and subsequently revised.

(filed July 18, 2003). As relevant here, Section 7.2.6.1.1 provides for decremental bid reference levels to be determined based on “the accepted decremental bid, or the lower of the mean or the median of a resource’s accepted decremental bids if such a resource has more than one accepted decremental bid in competitive periods over the previous 90 days” Tariff Section 7.2.6.1.1(a)(1).

Potomac proceeded to specify its interpretation of the ISO Tariff² regarding when “competitive periods” exist for purposes of the ISO’s application of Section 7.2.6.1.1 (and thus the circumstances in which the limit on decremental bid reference levels in Section 7.2.6.1.1(a)(1) applies).³ Potomac explained its interpretation of the ISO Tariff in a January 16, 2004 memorandum to the ISO Market Monitoring Unit: it stated that the standard would “clarify when an offer would be deemed to have been accepted in competitive periods.” ISO Compliance Filing, Docket No. ER03-683-005 (filed May 17, 2004), at Attachment A. The ISO informed Market Participants of Potomac’s interpretation of the “competitive periods” standard in the ISO Tariff and its application of this standard in a market notice issued January 20, 2004. *See id.*

² In the present filing, this is also referred to as Potomac’s standard.

³ As Potomac has explained, the term “competitive periods” is not defined in the ISO Tariff; rather, it is a term of art in economics. Comments of Potomac Economics Ltd. to the Supplemental Protest of Coral Power, L.L.C., Energia Azteca X, S. de R.L. de C.V. and Energia de Baja California, S. de R.L. de C.V., Docket No. ER03-683-003 (filed Feb. 17, 2004) at 6. Normally, competitive periods are defined as those in which offers are accepted in sequence, that is, units are accepted (or curtailed) in order of their relevant cost (across the relevant zone). *Id.* Potomac stated that it developed its standard in order to address concerns about the application in the ISO markets of the normal definition of competitive periods. *Id.*

In an order issued April 16, 2004, the Commission accepted proposed Section 7.2.6.1.1 to determine decremental reference bid levels. *California Independent System Operator Corporation*, 107 FERC ¶ 61,042, at PP 44-46 and ordering paragraph (A) (“April 16, 2004 Order”). The Commission also “direct[ed] the CAISO to incorporate the new test [for determining competitive periods] in section 7.2.6.1.1 of its tariff,” and directed the ISO to submit a compliance filing within thirty days. *Id.* at P 62 and ordering paragraph (B). To comply with this mandate, the ISO proposed changes to Section 7.2.6.1.1(a)(1) in a May 17, 2004 compliance filing that reflected Potomac’s standard.

On January 6, 2005, the Commission issued an order that recognized that in the April 16, 2004 Order it directed the ISO to file Potomac’s standard in a compliance filing. *California Independent System Operator Corporation*, 110 FERC ¶ 61,007 (“January 6, 2005 Order”). However, in the January 6, 2005 Order, the Commission also stated that the Potomac standard would not be effective until (1) the ISO filed tariff changes incorporating the standard in a filing pursuant to Section 205 of the Federal Power Act (“FPA”), to be effective on a prospective basis, and (2) the Section 205 filing was accepted by the Commission. January 6, 2005 Order at P 31. The Commission stated that “[b]ecause the implementation of the Potomac-proposed tariff revision without prior Commission approval has resulted in rates that are not currently on file with the Commission,” the ISO was directed to provide refunds for the period starting January 20, 2004 (the date the ISO issued a market notice stating that Potomac was going to start applying the standard) through the effective date of the

prospective filing submitted pursuant to Section 205 of the FPA. *Id.* The Commission also directed the ISO to submit an assessment of refund amounts owed to or owing by each Market Participant and a proposal for processing the refunds." *Id.* at P 32.

On February 7, 2005, the ISO submitted a request for rehearing and clarification of the January 6, 2005 Order on, *inter alia*, the Commission directives described immediately above concerning the Potomac standard. On February 17, 2005, the ISO submitted the filing pursuant to Section 205 of the FPA that the Commission directed in the January 6, 2005 Order. On April 18, 2005, the Commission issued an order accepting the Section 205 filing, effective February 18, 2005. *California Independent System Operator Corporation*, 111 FERC ¶ 61,073.

In the April 18, 2005 Order, the Commission denied the ISO's February 7, 2005 request for rehearing and clarification as to the Potomac standard. The Commission stated:

[W]e find that the January 6 Order correctly required the CAISO to provide refunds for charging a reference level rate that was not on file for all periods prior to the effective date of the section 205 filing, as accepted for filing by the Commission. We also remind the CAISO that an assessment of the amount owed to and owing by each market participant and a proposal for the processing of the refunds, including an estimated timeline highlighting the major milestones of such a process as directed in the January 6 Order, are due within 30 days of the date of issuance of this order.

April 18, 2005 Order at P 27 (citations omitted).

II. Refund Report

A. The Period Relevant to This Refund Report

As stated in Section I, above, the April 18, 2005 Order affirmed the finding in the January 6, 2005 Order that the ISO should provide refunds for the period from January 20, 2004 until the effective date of the Section 205 filing submitted by the ISO and accepted by the Commission (*i.e.* February 18, 2005). However, in light of the January 6, 2005 Order, Potomac independently decided to stop using the Potomac standard in its calculation of decremental reference prices, effective January 21, 2005.⁴ Therefore, no refunds are required for the days from January 21, 2005 through February 18, 2005, and the relevant period for determining refunds in accordance with the April 18, 2005 Order runs from January 20, 2004 through January 20, 2005.⁵

B. Methodology for Determining Refunds

The refund estimate presented herein consists solely of the energy decremented between P_{\max} and P_{\min} .⁶ Since the implementation of the Potomac

⁴ An ISO market notice announcing Potomac's decision is contained in Attachment A to the present filing.

⁵ Potomac did not reinstitute the use of the Potomac standard until April 23, 2005. The ISO will conduct a settlement adjustment for the period from February 18, 2005 through Friday April 22, 2005, because the Potomac standard was not used during that period. The settlement adjustment is not part of this refund report.

⁶ P_{\max} is a generating unit's maximum load level and P_{\min} is a generating unit's minimum load level. Generating units' "shut-down" reference levels (see *California Independent System Operator Corporation*, 108 FERC ¶ 61,193, at PP 10-13 (2004)) and capacity between P_{\min} and zero are not relevant to this refund report and are therefore not considered here. They are not relevant because the Potomac standard is only applied to bid-based reference levels. Potomac has explained to the ISO that the shut-down reference levels generated by Potomac have not been subject to the Potomac standard. There are no bids available for the capacity between P_{\min} and zero and therefore there is no basis for bid-based reference levels with regard to that capacity.

standard, Potomac has provided the ISO with reference levels that reflect the use of the Potomac standard. Consequently, the ISO's internal decremental reference level files reflect the Potomac standard. When Potomac began using the Potomac standard it did not keep a record of which segments of which reference levels had been altered by the standard. Potomac merely provided the ISO with the requisite reference levels, which the ISO used. As a result, there was no historical record of which reference levels had been changed due to the use of the Potomac standard. Consequently, the ISO asked Potomac to produce the following two files:

1. A file that provided the reference levels for all generating units that were decremented during the refund period, with the Potomac standard "switched on." This file is essentially a replica of what is available within the ISO system.
2. A file that provided the reference levels for all generating units that were decremented during the refund period, with the Potomac standard "switched off."

To determine which generating units are due refunds, the ISO compared these two Potomac files. This comparison produced a list of 39 generating units that had had their reference levels changed due to the presence of the Potomac standard. The ISO then created a single file that listed the days and hours when these reference levels were changed due to use of the Potomac standard, with regard to each generating unit. For ease of calculation the ISO then calculated the average reference price it actually charged each generating unit (the ISO

average reference price) as well as the average Potomac reference price with the Potomac standard “switched off.” The difference between these two average reference prices was then multiplied by the decremental dispatches above P_{\min} for each generating unit to produce the estimate of the refund owing to each Market Participant.

The ISO would like to emphasize the fact that the figures shown in Section II.C, below, are a preliminary assessment of the amounts due. Prior to developing a final settlement, the ISO will undertake additional analysis and communications with Potomac to verify the accuracy of the revised decremental reference prices. In addition, the actual amounts that will be refunded to Market Participants will be determined by the ISO Settlements system and will be at a finer level of detail than the assessments shown here. Therefore, the final refunds may vary due to potential corrections to the revised decremental reference prices used to produce these assessments as well as the use of a more precise computational methodology. The ISO is willing to discuss this issue with any Market Participants that may have questions concerning it.

C. Results of the ISO’s Refund Calculations

The estimated total amount of refunds owed is \$2,128.221. An itemization of the generating units as to which refund amounts are owed and owing is contained in a confidential attachment to the present filing, Attachment B. The Scheduling Coordinators affected are: Calpine Energy Services, Coral Power, L.L.C., Reliant Energy Services, Pacific Gas and Electric Company, and Southern California Edison Company. These Scheduling Coordinators should

contact their ISO Client Representatives for specific information concerning the refund amounts owed and owing.

D. Timeline for Providing Refunds

The ISO will provide refunds as described above in either the third quarter or the fourth quarter of 2005. The ISO is already committed to calculating a number of reruns of its Settlements system in other proceedings, most notably the California refund proceeding in Docket Nos. EL00-95, *et al.* The refund rerun conducted pursuant to the present filing will be conducted along with other reruns for the period subsequent to the refund period of the proceeding in Docket Nos. EL00-95, *et al.*

III. Conclusion

Wherefore, for the foregoing reasons, the ISO requests that the Commission accept the ISO's refund report in this proceeding.

Respectfully submitted,

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Dated: May 18, 2005

ATTACHMENT A

From: CRCommunications [CRCommunications@caiso.com]
Sent: Wednesday, January 26, 2005 11:29 AM
To: ISO Market Participants
Subject: CAISO: Market Operations / Methodology Change in Calculation of Decremental Reference Levels

CAISO MARKET NOTICE

Requested Client Action: Information Only

Categories: Market Operations

Subject: Methodology Change in Calculation of Decremental Reference Levels

Summary: Potomac Economics will no longer use a competitiveness screen when calculating Decremental Reference Levels. Effective from January 21, 2005.

Main Text:

On January 20, 2005 the California ISO was informed by Potomac Economics, the independent entity that calculates the decremental reference levels, will no longer be using the competitiveness screen when calculating decremental reference prices. The competitiveness screen is a test (the ratio of energy decremented out-of-sequence to energy decremented in sequence) to determine what constitutes "competitive conditions". This action was taken pursuant to a Federal Energy Regulatory Commission (FERC) "Order on Rehearing and Clarification Requests and Compliance Filing" (Dockets ER03-683-004 and ER03-683-005) issued on January 6, 2005. The decremental reference price calculations for January 21st and subsequent days are not subject to the competitiveness screen. The decremental reference price is used in managing intra-zonal congestion as set forth by the May 30, 2003 order of the Federal Energy Regulatory Commission (FERC) in Docket No. ER03-683, 103 FERC ¶ 61, 265.

For More Information Contact:

Please contact Mr. David Patton at Potomac Economics at 703-383-0720 or Pallas LeeVanSchaick at 703-383-0719.
Potomac Economics' web site is located at <<http://www.potomaceconomics.com>> .

Client Relations Communications.1026

CRCommunications@caiso.com <<mailto:CRCommunications@caiso.com>>

The California ISO strives to be the preferred provider of superior electrical transmission services for the benefit of our customers in California and the West.

ATTACHMENT B

**Privileged Information Has Been Redacted
Pursuant to 18 C.F.R. § 388.112**

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list for the captioned proceeding, in accordance with Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, California, on this 18th day of May, 2005.

Anthony Ivancovich ^{BRM}
Anthony Ivancovich