

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

**California Independent System) Docket No. ER98-3594-000
Operator Corporation)**

**MOTION FOR CLARIFICATION AND
ALTERNATIVE REQUEST FOR REHEARING OF
THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

Pursuant to Rules 212 and 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 385.713, the California Independent System Operator Corporation ("ISO") requests clarification or rehearing of the Commission's August 2, 1999, Order in the above-captioned proceeding ("the August 2 Order").

I. Summary

In the August 2 Order, in response to a rehearing request of the California Department of Water Resources ("DWR"), the Commission directed the ISO to revise the ISO Tariff so that Participating Transmission Owners ("TOs") without transmission customers would not be required to develop an Access Charge,¹ a Transmission Revenue Requirement ("TRR"), or a Transmission Revenue Balancing Account ("TRBA"). DWR argued that it owned no transmission facilities, but merely held contractual rights to use to transmission facilities of others. As a result, according to DWR, it is not a transmission provider, but merely a transmission customer, and as a result has no revenue requirement on which to base a TRR and no customers to whom it would flow revenues through a TRBA.

Although an entity like DWR that has only contractual entitlements to transmission capacity may not have transmission customers prior to joining the ISO, it would have such customers – in the only meaningful sense of the term – once it

¹ Capitalized terms used in this pleading and otherwise not defined have the meanings given them in the ISO Tariff.

becomes a Participating TO and permits the ISO to make the capacity represented by its contract rights available under the ISO Tariff. Scheduling Coordinators whose transactions are scheduled using the transmission capacity converted to ISO service by the new Participating TO would effectively be transmission customers of that entity. The ISO Tariff specifically contemplates that Scheduling Coordinators wheeling energy through or out of the ISO Controlled Grid would pay Wheeling Access Charges that reflect the TRRs of the Participating TO's whose facilities *and contractual entitlements* make up the point of withdrawal. If one of those Participating TO's refuses to establish a TRR, the ISO cannot determine the appropriate Wheeling Access Charge for that Scheduling Point and the Participating TO cannot receive the compensation to which it otherwise would be entitled to defray a portion of the costs it incurs to obtain the converted contractual transmission rights.

The Commission should accordingly clarify the August 2 Order or, if necessary, grant rehearing of that order, to make it clear that a Participating TO whose transmission facilities or contractual entitlements are used by the ISO to schedule transactions under the ISO Tariff *has* transmission customers and therefore must establish a TRR and an Access Charge, against which revenues received by the Participating TO for Usage Charges and the proceeds of FTR auctions must be credited, either through a TRBA or another equivalent mechanism.

II. Background

On June 6, 1998, in compliance with the Commission's direction in earlier orders,² the ISO tendered for filing Amendment No. 9 to the ISO Tariff, adding Sections 9.1 through 9.8 to govern the creation, distribution and use of Firm Transmission Rights ("FTRs"). As defined in the amendment, FTRs have attributes both of financial contracts and of physical transmission rights. As financial contracts, FTRs entitle their owners to share in the distribution of Usage Charge revenues received by the ISO in connection with managing Inter-Zonal Congestion on the ISO Controlled Grid during the calendar year for which the FTR is issued.³ As physical rights, FTRs entitle the registered holder to priority in the Day-Ahead Market for the transmission of Energy across a congested Inter-Zonal Interface in the circumstances described in the amendment. FTRs are defined separately for each Inter-Zonal Interface and direction of flow combination on the ISO Controlled Grid. On September 29, 1998, the ISO filed a motion for an extension of time for the implementation of FTRs to March 31, 1999, which the Commission subsequently approved.⁴

² *Pacific Gas & Electric Co., et al.*, 81 FERC ¶ 61,122 at 61,486 (1997); *Pacific Gas & Electric Co., et al.*, 80 FERC ¶ 61,128 at 61,427 (1997).

³ Currently, the Usage Charge revenues are distributed to Participating Transmission Owners ("TOs") owning the transmission facilities or rights making up an Inter-Zonal Interface. Proceeds of the ISO's auction of FTRs will be distributed in the same manner.

⁴ *California Independent System Operator Corp.*, 85 FERC ¶ 61,405 (1998).

On December 4, 1998, the ISO tendered a revised version of Amendment No. 9, expanding Section 9.4 to include a detailed description of the auction process which was developed with the assistance of independent consultants. The revision also incorporated a number of other changes in response to comments received on the initial filing.

In an Order dated May 3, 1999, the Commission approved Amendment No. 9, with certain modifications. 87 FERC ¶ 61,143 (“the May 3 Order”). The Commission did not address, however, a March 10, 1999, letter and a March 26, 1999, motion filed with the Commission by the ISO, which indicated that, due to software and Y2K compliance concerns, the ISO would be unable to implement FTRs during the 1999 peak season if the Commission did not approve Amendment No. 9 (without substantial modification) by mid-April 1999.

In a Request for Rehearing and Clarification filed in this proceeding on June 2, 1999, the ISO requested rehearing and clarification of, inter alia, the Commission’s timing directives in the May 3 Order to permit the ISO to implement its initial release of FTRs effective February 1, 2000.

Other parties also submitted requests for rehearing, including DWR. Among other matters, DWR asserted that the Tariff should not require DWR to develop an Access Charge,¹ a TRR,² or a TRBA³ because it has no transmission customers, and

¹ Under the ISO Tariff, there are three types of Access Charges: the Non Self-sufficient Contract Demand Rate; the Wheeling Access Charge; and the End User Charge. See section 7.1 of the ISO Tariff.

² Prior to the ISO’s August 13 compliance filing, the ISO Tariff defined the TRR as the “total annual authorized revenues associated with transmission facilities turned over to the Operational Control of the ISO by a Participating TO, and for which FERC jurisdictional entities are permitted to include in their Access Charges for recovery from customers, or in the case of non-FERC jurisdiction entities, the equivalent revenue amount authorized by the appropriate jurisdictional regulatory authority.

³ Prior to the ISO’s August 13 compliance filing, the ISO Tariff defined the TRBA as a “mechanism to be established by each Participating TO which will ensure that all Transmission Revenue Credits flow through to its transmission customers.”

because it has no transmission facilities that it will turn over to the ISO, but only contractual rights to transmission.

On August 2, 1999, the Commission issued an order acting on the requests for rehearing and clarification in this proceeding.⁴ In the August 2 Order, the Commission granted the ISO's request for rehearing and clarification. In response to DWR's rehearing request, the Commission also directed the ISO to make the following change to the ISO Tariff:

. . . we clarify that any Participating Transmission Owner that has no transmission customers need not develop a Transmission Revenue Balancing Account, a Transmission Revenue Requirement, nor an Access Charge. We direct the ISO to modify its tariff accordingly

88 FERC ¶ 61,156 at 61,528 (1999). The Commission directed the ISO to submit these Tariff modifications within 14 days of the date of the August 2 Order. The Commission denied all other requests for clarification and rehearing.

On August 13, 1999, the ISO submitted revised Tariff sheets to comply with the Commission's directive. The ISO also noted, however, its intent to request rehearing of that aspect of the August 2 Order that directed revision of the Tariff regarding Participating Transmission Owners with no transmission customers.

III. Specification of Errors

In accordance with Rule 713(c)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(c)(1), the ISO specifies that the Commission should revise the August 2 Order to clarify that Participating TOs that turn over to the ISO's Operational Control transmission facilities or contractual rights for transmission capacity used by the ISO to provide transmission service under the ISO Tariff have transmission customers and therefore must develop an Access Charge, a TRR, and a TRBA.

⁴ *California Independent System Operator Corp.*, 88 FERC ¶ 61,156 (1999) ("August 2 Order")

IV. Discussion

A. Participating TOs Who Turn Over to the ISO's Operational Control Contractual Rights to Transmission Capacity Have Transmission Customers.

Although the ISO, in compliance with the Commission's August 2 Order, has amended the ISO Tariff to provide that Participating TOs without transmission customers do not need to develop an Access Charge, a TRR, or a TRBA, the ISO believes that the exception is rarely applicable. For practical purposes, only in rare circumstances, if at all, would a Participating TO have no transmission customers.⁵ In light of the circumstances asserted in the DWR's rehearing petition, however, the ISO is concerned that Participating TOs that turn Existing Contract rights over to the ISO's Operational Control may misunderstand the exception and fail to develop an appropriate TRR, TRBA, and Access Charge. The ISO therefore requests clarification, or if necessary rehearing, to ensure a correct interpretation of the August 2 Order.

When a Participating TO "place[s] its transmission assets and Entitlements under the ISO's Operational Control,"⁶ it makes the capacity available to the ISO for scheduling the transactions of transmission customers under the ISO Tariff. The Participating TO does not cede ownership of the physical facilities to the ISO, but merely the right to control the operation of the transmission facilities and to make their capacity available to transmission customers. This is true whether the Participating TO's rights arise from ownership of the physical transmission assets or from contractual rights to use those assets.

⁵ The ISO recognizes that there may be circumstances in which a Participating TO's Entitlements are limited to lines from the Scheduling Points of which no one except that Participating TO takes power from the ISO Controlled Grid. The ISO has not attempted to review all Existing Contracts to determine the extent to which this may occur. Even in such circumstances, however, the Participating TO has potential customers in connection with future interconnections.

⁶ See the definition of "Participating TO" in the ISO Tariff. The ISO Tariff defines "Operational Control" as the "rights of the ISO . . . to direct the Participating TOs how to operate their transmission lines and facilities and other electric plant . . . for the purpose

Thus, if an Investor Owned Utility (“IOU”) turns over a line with 1200 MW of transfer capacity to the ISO’s Operational Control, and there are Existing Contracts for 500 MW of capacity on the line, the ISO can only schedule 700 MW of transactions over that line. Any Scheduling Coordinators whose transactions are scheduled over that line by the ISO are de facto transmission customers of the IOU, taking service under the ISO Tariff. If the holder of the rights under the Existing Contracts subsequently turns over its Entitlements to the ISO, the ISO can schedule the entire 1200 MW. A Scheduling Coordinator whose transaction is scheduled over the line by the ISO is then a transmission customer both of the IOU and of the holder of the rights under the former Existing Contracts.

The transmission pricing framework under the ISO Tariff reflects this concept. If a Scheduling Coordinator wheels electricity out of the ISO Controlled Grid at a Scheduling Point on a line owned by one or more Participating TOs and at which another Participating TO has Entitlements that have been turned over to the ISO’s Operational Control, the Scheduling Coordinator is charged a blended rate based on the TRRs and TRBAs of the owner(s) of the facility and the holder of the Entitlement.⁷ The ISO Tariff explicitly recognizes that a Participating TO that has only Entitlements is nonetheless due payments from Wheeling customers. Wheeling revenues are thus distributed according to Participating TOs’ TRRs.⁸

of affording comparable and non-discriminatory transmission access and meeting Applicable Reliability Criteria.”

⁷ Under section 7.1.4.2 of the ISO Tariff, “To the extent that more than one Participating TO owns *or has a firm entitlement to* transmission capacity exiting the ISO Controlled Grid at a Scheduling Point, the Scheduling Coordinator shall pay . . . a rate for Wheeling . . . that reflects an average of the Wheeling Access Charge of those Participating TOs, weighted by the relative share of such ownership or firm entitlement to transmission capacity.” (Emphasis added.) Under section 7.1.4.1, the Wheeling Access Charge is based on the TRR and the TRBA of the Participating TO.

⁸ Section section 7.1.4.3 of the ISO Tariff.

Although the Commission directed the ISO to modify the ISO Tariff's requirements in response to DWR's petition for rehearing, DWR's circumstances actually illustrate the importance of requiring Participating TOs to develop an Access Charge. It is the ISO's understanding that DWR pays approximately \$20 million for contractual rights on facilities owned by Pacific Gas & Electric Company and Southern California Edison Company, including a significant portion of Path 15. The ISO further understands that much of this capacity is in excess of DWR's on-peak needs. If DWR becomes a Participating TO and turns its Entitlements over to the ISO, customers scheduling transactions over Path 15 or any other of DWR's Entitlements would effectively be transmission customers of DWR, as well as the other Participating TOs. If DWR does not create a Wheeling Access Charge, the ISO will be unable to determine the Wheeling Access Charge applicable to transactions that exit the ISO Controlled Grid at Scheduling Points where DWR has Entitlements. If DWR does not establish a TRR, the ISO's calculation of Wheeling Access Charge disbursements will not include DWR, and DWR will have no opportunity to recoup any portion of the payments it makes for that capacity from transmission customers scheduling transactions under the ISO Tariff.

B. The Circumstances Described in the Rehearing Petition that Gave Rise to the Commission Order Regarding Participating TOs Without Transmission Customers Do Not Support Exemption from the Requirement of an Access Charge, TRR, and TRBA.

1. The ISO Tariff's Treatment of Access Charges, TRR, and TRBA Is Fully Applicable to Agencies Such As DWR

As noted above, the Commission's Order that the ISO exempt Participating TOs "without transmission customers" from the requirement to develop an Access Charge, TRR, and TRBA was in response to a rehearing petition filed by DWR. Most of that petition is directed to an alleged showing that DWR is a unique entity, whose circumstances render much of the ISO Tariff structure irrelevant. DWR's arguments that the ISO Tariff provisions are not applicable to it, however, are misplaced.

First, DWR states that it "can have no "total annual authorized revenues associated with transmission facilities turned over" to ISO Control, because it will turn over Existing Contract rights – not transmission facilities – to ISO Control." Rehearing Request of the California Department of Water Resources at 32 (hereinafter, "Rehearing Request"). To the contrary, if DWR turns its Existing Contract rights over to the ISO's Operational Control, it will give the ISO control – i.e., the ability to schedule transactions – over transmission capacity otherwise unavailable to the ISO. DWR is currently paying for that capacity and, according to DWR's rehearing request, is authorized under state law to do so. The total annual authorized revenues associated with those facilities are thus the cost of those Existing Contracts.

DWR next asserts that it does not have a “revenue amount” approved by an “appropriate jurisdictional regulatory authority.” *Id.* It states that it is authorized under State law to enter into water supply contracts and to recover in this manner all of the costs of the State Water Project (“SWP”), and that no agency oversees its rates other than the Governor and the State Legislature. *Id.* at 33. DWR reads “appropriate jurisdictional regulatory authority” far too narrowly. If DWR sets its own rates, overseen by the Governor and the State Legislature, than the Governor and State Legislature operate as its regulatory authority in the same manner that FERC regulates public utilities when they set their rates, subject to FERC approval. Indeed, the ISO understands that the California Board of State Water Contracts annually approves the SWP budget, and therefore the rates paid by DWR customers. Moreover, DWR rates presumably do include a specific “revenue amount”: DWR’s bills to its water customers include a specific line item pertaining to power costs, including the costs for the transmission of electricity. One must assume that this line item is intended to provide the revenues necessary to cover DWR’s transmission costs.

At the heart of DWR’s argument, however, is its repeated argument that its only customers and rates relate to wholesale water deliveries;⁹

⁹ In fact, DWR’s customers are not restricted to its water contracts. DWR enters into power sales contracts under which it sells power that it does not use for pumping purposes to customers. *See, e.g., City of Vernon v. Southern California Edison Co.*, 43 FERC ¶ 61,523, *reh’g denied*, 44 FERC ¶ 61,377 (1988).

that it is only a transmission customer, not a provider; and that its entitlement to Usage Charge revenues, Wheeling revenues, and FTR revenues is only a form of refund or compensation to a customer. DWR is indeed a transmission customer, and the ISO does not contest that fact. The ISO Tariff, however, does not provide any entity *in its capacity as a customer* with entitlement to Usage Charge revenues, Wheeling revenues, or FTR revenues. Rather, these payments are made to entities *in their capacity as transmission providers* – i.e., entities who have legal rights to use transmission capacity and who *provide* that capacity to the ISO to enable the ISO to serve transmission customers. Although DWR may at this time be only a transmission customer, if DWR subsequently turns its Entitlements over to the ISO's control, DWR would then also be a Participating TO, i.e., a transmission provider. DWR would be no different in this regard than *any* holder of transmission rights converted to the ISO's Control.

Acceptance of DWR's interpretation of a Participating TO's role under the ISO Tariff would undermine the basic structure of the ISO Tariff, as accepted and approved by the Commission. Many potential Participating TOs have Existing Contract rights similar to those of DWR. The ISO Tariff treats these rights identically to physical ownership for purposes of collecting revenues (including determination of Self-Sufficiency and determination of Wheeling Access Charges) and the distribution of revenues (distribution of Wheeling revenues, Usage Charge revenues, and FTR auction revenues). DWR's proposal would consider these rights for the purposes of distributing revenues, but not for the purpose of collecting them, severely skewing the cost allocation system under the ISO Tariff.

C. Requiring Agencies Such As DWR to Abide by the ISO Tariff's Requirements for Participating Transmission Owners Raises No Jurisdictional Issues.

DWR finally asserts that requiring it to develop an Access Charge, TRR, and TRBA is beyond the Commission's and the ISO's jurisdiction:

California law does not authorize the ISO to require a transmission customer like DWR to establish an Access Charge. Nor does the Federal Power Act authorize the Commission to require DWR to develop an Access Charge. As a transmission customer, DWR need not develop its own rates in order to receive a refund. As a state agency, DWR is exempt from Federal Power Act regulation.

Rehearing Request at 37. The flaw with DWR's argument is in its premises. Neither the ISO nor the FERC proposes that a transmission customer develop rates. Rather, the ISO Tariff requires a Participating TO whose capacity is used by the ISO to serve customers to develop a rate. Despite DWR's claim that FTR auction revenues, Usage Charge revenues, and Wheeling revenues "most resemble refunds," they are not refunds; they are compensation for a Participating TO's capacity rights. The Federal Power Act's exemption of state agencies from Commission jurisdiction does not extend to an agency that voluntarily submits its facilities to the control of, and expects compensation through, a jurisdictional entity. *See Central Hudson Gas & Electric Corp.*, 86 FERC ¶ 61,213 (1999).

Although the ISO considers it in the best interest of all Market Participants for holders of Existing Contracts for firm capacity to either turn that capacity over to the Operational Control of the ISO or to terminate the contracts, so that the facility owner can turn the capacity over to the ISO Operational Control, neither the ISO Tariff nor the Commission requires such action. Absent such compulsion, there can be no impermissible interference with the independence of a state agency that holds such rights.

DWR also asserts that the ISO and FERC would be acting beyond their jurisdiction because they would be regulating DWR's water contracts by requiring DWR to ensure that Transmission Revenue Credits appear in DWR's water charges. The TRBA, however, is a mechanism for providing that Transmission Revenues Credits flow through to *transmission customers*. DWR's only specific transmission customers would be those taking service under the ISO Tariff, using Entitlements that DWR converts to the ISO's control. Ensuring that those customers receive an appropriate share of the Transmission Revenue Credits¹ would not implicate DWR's water rates in any manner.

¹ Presumably, DWR's TRBA would take into account DWR's own use (as its own end use customer) of the facilities on which it has contractual rights. The extent to which DWR passes these revenues on to its water customers is not of concern to the ISO.

V. Conclusion

For the reasons outlined above, the ISO requests that the Commission clarify or revise the August 2 Order to ensure that entities that have Existing Contracts for capacity on transmission lines that the ISO uses, or would use, to wheel energy, and who give the ISO Operational Control over those contractual capacity rights, need to develop an Access Charge, Transmission Revenue Requirement, and Transmission Revenue Balancing Account.

Respectfully submitted,

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

Kenneth G. Jaffe
Swidler Berlin Shereff Friedman, LLP
3000 K St., NW #300
Washington, DC 20007
Tel: 202-424-7588
Fax: 202-424-7645

Edward Berlin
Michael E. Ward

Date: September 1, 1999

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the forgoing document upon each person designated on the official service list compiled by the Secretary in this Docket No. ER98-3594-000 in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.2010 (1997).

Dated at Washington, D.C. on this 1st day of September, 1999.

Michael E. Ward