

Memorandum

To: Western Energy Markets Governing Body
From: Ryan Seghesio, Vice President, Chief Financial Officer and Treasurer
Date: April 21, 2026
Re: Decision on Financial Planning Initiatives: Cost-of-Service Study Extension and Revenue Requirement Cap Increase

This memorandum requires action by the Western Energy Markets Governing Body (primary authority) and the ISO Board of Governors (consent agenda).

EXECUTIVE SUMMARY

This memorandum presents two components of the Financial Planning Initiatives: (1) extension of the Cost-of-Service Study timeline and (2) updates to the Grid Management Charge (GMC) revenue requirement cap. These proposals are intended to ensure that the ISO's cost recovery framework remains aligned with evolving market conditions, including the implementation of the Extended Day-Ahead Market (EDAM), while maintaining financial stability, transparency, and cost-causation alignment.

The ISO conducts a Cost-of-Service Study every three years to determine the ISO's revenue requirement and how ISO administrative costs are allocated. Under the current tariff, the next Cost-of-Service Study would be conducted in 2026. However, because EDAM is expected to begin operations in 2026, a study conducted now would rely primarily on pre-EDAM data and may not accurately reflect future operational conditions and cost drivers. The ISO therefore proposes to extend the timing of the next study to 2028, when a full year of EDAM operational data will be available. Conducting the study on this timeline will improve the accuracy of cost allocation outcomes and reduce the likelihood that subsequent adjustments would be required. The ISO will rely on the 2023 Cost-of-Service Study in the meantime, which Management believes is still reliable.

Separately, the ISO proposes to increase the GMC revenue requirement cap for 2027 and 2028 to ensure that the tariff provides sufficient headroom to recover projected costs. The ISO currently has a revenue requirement cap of \$250 million. Although the existing cap is sufficient for 2026, inflation, forecasted increases in operations and maintenance costs, the re-inclusion of cash-funded

capital beginning in 2027, reduced revenue offsets, and evolving market participation necessitate increases in the cap. These increases will avoid the need to exhaust reserves or risk losses. The increase in 2027—approximately 20 percent relative to 2026—is primarily driven by the re-inclusion of capital costs that were funded through reserves in 2026 and therefore reflects a timing shift rather than a structural increase in ongoing costs. Following this transition, revenue requirement growth is expected to return to levels more consistent with historical trends.

Although the total revenue requirement is projected to increase, this does not necessarily translate to higher rates or costs for market participants. As EDAM expands participation and increases billing determinants, costs are expected to be spread across a broader base, which may mitigate or offset rate impacts.

Stakeholders generally supported both proposals. Comments focused primarily on requests for additional transparency regarding cost drivers, assurance that the Cost-of-Service Study will be completed in 2028 without further delay, and clarification of the factors contributing to the 2027 revenue requirement increase and its potential rate impacts. The ISO has addressed these comments by providing additional detail on cost drivers, reaffirming its commitment to complete the study in 2028, and clarifying the distinction between overall revenue requirement and rates.

Management recommends approval of the proposed extension of the Cost-of-Service Study and the updates to the GMC revenue requirement cap to ensure continued alignment with evolving market conditions, financial sustainability, and transparency.

Moved, that the Western Energy Markets Governing Body approves the extension of the Cost-of-Service Study and approves the increases to the GMC annual revenue requirement cap as described in the memorandum dated April 21, 2026, and requests that Management place this initiative on the ISO Board of Governors' consent agenda; and

Moved that the Western Energy Markets Governing Body authorizes Management to make all necessary tariff revisions and appropriate filings with the Federal Energy Regulatory Commission to implement the changes proposed in the memorandum dated April 21, 2026.

BACKGROUND

Cost-of-Service Study Extension

The ISO conducts a Cost-of-Service Study every three years to determine the ISO's revenue requirement and how ISO administrative costs are allocated to market participants. The Cost-of-Service Study generally informs the ISO's GMC, which the ISO assesses on market participants' supply, demand, ancillary services, and congestion revenue rights. Under the current tariff, the next study would be conducted this year using historical data from the preceding year. The Cost-of-Service Study is a significant yearlong effort for the ISO, requiring thousands of man-hours across departments.

Because EDAM is expected to begin operations in 2026, a study conducted now would rely largely on data that predates EDAM implementation. Conducting the study prior to the availability of meaningful EDAM operational data could result in cost allocations that do not fully reflect the post-EDAM market structure and may require subsequent revisions. In simple terms, the benefits of a 2026 Cost-of-Service Study are low: the data could be so misleading that the ISO would need to conduct another study as soon as it would have a complete data set for a full year of EDAM. Extending the study to 2028 allows the ISO to incorporate a full year of EDAM operations from 2027, resulting in more representative cost allocation outcomes. This timing supports improved alignment with cost-causation principles and enhances the durability of the study results. During the interim period, the cost allocation framework established in the 2023 Cost-of-Service Study will remain in effect, and no changes to the underlying cost allocation methodology are proposed as part of this initiative. Although the ISO proposes increases to its self-imposed revenue cap, the ISO has no cause to believe the cost allocation structure of the existing GMC warrants change.

GMC Revenue Requirement Cap Increase

The GMC revenue requirement cap establishes the maximum level of costs that may be recovered under the tariff. The current cap is sufficient to meet the ISO's revenue requirement in 2026, but projected conditions in 2027 and 2028 require additional headroom.

**Table 1: GMC Revenue Requirement and Rates
(2025-2026 Actual; 2027-2028 Projected)**

	Actual	Actual	Projected	Projected
Revenue Requirement (\$ in millions)	2025	2026	2027	2028
Operations and Maintenance Budget	\$ 275.9	\$ 290.3	\$ 304.9	\$ 320.1
Debt Service (including 25% Reserve)	14.7	14.7	14.7	14.7
Cash Funded Capital	25.0	-	31.0	31.0
Other Costs and Revenues	(68.6)	(51.3)	(50.0)	(50.3)
Operating Cost Reserve Adjustment	(8.6)	(3.9)	(2.4)	(0.7)
Total Revenue Requirement	\$ 238.4	\$ 249.8	\$ 298.2	\$ 314.9
Revenue Requirement Cap (\$ in millions)				
Revenue Requirement Cap	\$ 245.0	\$ 250.0	\$ 305.0	\$ 320.3
Variance between Cap and Total	\$ 6.6	\$ 0.2	\$ 6.8	\$ 5.4
Rates (\$/MWh)				
Market Services Charge	\$ 0.1611	\$ 0.1416	\$ 0.1513	\$ 0.1389
System Operations Real-Time Dispatch Charge	\$ 0.1144	\$ 0.0901	\$ 0.0960	\$ 0.0879
System Operations Balancing Authority Area Services Charge	\$ 0.1293	\$ 0.1356	\$ 0.1619	\$ 0.1690
Congestion Revenue Rights Services Charge	\$ 0.0076	\$ 0.0109	\$ 0.0134	\$ 0.0142

The proposed increases to \$305 million in 2027 and \$320.3 million in 2028 are driven by several identifiable factors. These include approximately 5 percent annual growth in operations and maintenance expenditures required to support ongoing market and grid operations, the re-inclusion of cash-funded capital beginning in 2027, reduced revenue offsets associated with evolving market design, and changes in market participation as EDAM is implemented. A significant portion of the ISO's growth in recent years reflects investments and capabilities developed in response to stakeholder-supported initiatives and expanding market participation.

The higher increase in 2027 relative to prior years is primarily attributable to the re-inclusion of cash-funded capital. In 2026, capital expenditures were funded using

existing reserves to maintain fiscal balance. In 2027, the ISO returns to a more typical funding approach in which capital expenditures are included in the revenue requirement. Following this transition, growth in the revenue requirement is expected to return to levels more consistent with historical trends.

Over a longer time horizon, the ISO's revenue requirement growth has remained moderate, reflecting disciplined financial management.

Although the overall revenue requirement is projected to increase, this does not necessarily translate to higher rates or costs for market participants. As EDAM expands participation and increases billing determinants, costs are expected to be spread across a larger base, which may mitigate or offset rate impacts.

The proposed cap levels include modest headroom above projected revenue requirements to accommodate potential variability in market participation and revenue offsets, thereby reducing the likelihood of an out-of-cycle tariff filing.

POSITIONS OF THE PARTIES

The ISO conducted a stakeholder process that included a February 12 stakeholder meeting and a March 19 stakeholder meeting on the draft final proposal; both meetings were followed by a written comment period.

Stakeholders generally supported the proposal to extend the Cost-of-Service Study to 2028, recognizing that conducting the study in 2026 would rely on pre-EDAM data and may not produce representative results. Stakeholders requested assurance that the study will be completed in 2028 without further delay and emphasized the importance of maintaining transparency regarding cost drivers during the interim period.

With respect to the GMC revenue requirement cap, stakeholders did not express opposition to the proposed increases but requested additional transparency regarding the drivers of the projected increase, particularly the approximately 20 percent increase in 2027 relative to historical trends. Stakeholders also sought clarification regarding the impact of changing market participation, including transitions into EDAM, on revenue offsets, billing determinants, and rate impacts.

In response, the ISO enhanced the draft final proposal by providing additional explanation of operations and maintenance cost drivers, clarifying the role of cash-funded capital in driving the 2027 increase, and providing historical context demonstrating moderate long-term growth. The ISO also clarified how EDAM participation may affect both revenue offsets and billing determinants and emphasized the distinction between total revenue requirement and participant rates.

No stakeholder opposed the overall structure of the proposals. Stakeholder feedback primarily resulted in refinements to improve transparency and clarity rather than changes to the underlying approach.

CONCLUSION

The proposed extension of the Cost-of-Service Study and the updates to the GMC revenue requirement cap are necessary to ensure that the ISO's cost recovery framework remains aligned with evolving market conditions and operational requirements. Extending the timing of the Cost-of-Service Study will allow the ISO to incorporate EDAM operational data, improving the accuracy and durability of cost allocation outcomes, while the proposed cap increases provide appropriate flexibility to recover projected costs in 2027 and 2028.

These updates are time-sensitive and align with the development of the 2027 revenue requirement and associated tariff processes. Approval will support continued financial stability, enhance transparency, and ensure effective cost recovery as the ISO's markets evolve.

Importantly, approval of these initiatives does not replace or preempt the ISO's annually recurring revenue requirement stakeholder process, which will continue to serve as the primary forum for reviewing the ISO's annual budget, cost drivers, and revenue requirement assumptions, ensuring ongoing transparency and stakeholder engagement.