



CALIFORNIA ISO

California Independent
System Operator

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FEDERAL ENERGY
REGULATORY COMMISSION

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

Re: Pacific Gas and Electric Company
Docket Nos. ER98-2358-002, ER97-2358-003, ER97-2358-004,
ER98-2351-001, ER98-2351-002, ER98-2351-003

Southern California Edison Company
Docket Nos. ER97-2355-002, ER97-2355-004, ER97-2355-006,
ER98-2322-000, ER98-2322-001, ER98-2322-002

San Diego Gas & Electric Company
Docket Nos. ER97-2364-002, ER97-2364-004, ER97-2364-005,
ER97-4235-002, ER97-4235-003, ER97-4235-004, ER98-497-002,
ER98-497-003, ER98-497-004, ER98-2371-000, ER98-2371-001,
ER98-2371-002

Dear Secretary Salas:

Enclosed for filing, please find an copy of a signed original and 15 additional copies of a letter addressed to Commissioners Wood, Brownell, Kelliher and Kelly by California ISO President and Chief Exective Officer Terry M. Winter. The letter addresses FERC Opinions 458 and 458-A, issued in the above captioned dockets.

Please return one file-stamped copy in the self-addressed, stamped envelope provided. Thank you for your assistance in this matter.

Respectfully submitted,

Beth Ann Burns
Litigation Counsel

California Independent System
Operator Corporation



CALIFORNIA ISO

California Independent
System Operator

Terry M. Winter
President and Chief Executive Officer

March 3, 2004

The Honorable Pat Wood III, Chairman
The Honorable Nora M. Brownell
The Honorable Joseph T. Kelliher
The Honorable Suedeen G. Kelly
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

Re: Opinion Nos. 458 and 458-A

Dear Chairman Wood and Honorable Commissioners:

On February 12, 2004, the U.S. Court of Appeals for the D.C. Circuit issued an order that granted the Commission's motion and remanded back to the Commission the record in Southern California Edison Company, et al., v. Federal Energy Regulatory Commission, Case No. 02-1374. In its motion, the Commission indicated that it was seeking remand to permit issuance of a further order that considers and explains the issue of transmission cost recovery under the Tariff provisions of the California Independent System Operator Corporation ("California ISO"). As you reconsider that issue and review the decisions subject to the appeal, I respectfully urge the Commission to reverse its holding in Opinion Nos. 458 and 458-A¹ and on remand permit recovery of the transmission cost differentials by Pacific Gas & Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company (collectively "Companies").

Opinion Nos. 458 and 458-A denied recovery by the Companies of substantial, ongoing cost differentials that represent a disparity between the charges the California ISO assesses under its Tariff for Transmission Losses and Ancillary Services requirements on Schedules submitted under Existing Contracts and the amounts the Companies receive under the Existing Contracts, which were executed before restructuring and contemplate a different paradigm and cost structure. The Companies have calculated these cost differentials, in the aggregate, to date, to be at least \$100 million; and they continue to accrue.

It has been the consistent position of the California ISO, before this Commission and the Court of Appeals, that the Commission's October 30, 1997 order² expressly provided for the

¹ *Pacific Gas and Elec. Co.*, 100 FERC ¶ 61,156 (2002) ("Opinion No. 458") and *Pacific Gas and Elec. Co.*, 101 FERC ¶ 61,151 (2002) ("Opinion No. 458-A").

² *Pacific Gas and Elec. Co.*, 81 FERC ¶ 61,122 (1997).

recovery of such cost differentials by approving two provisions of the California ISO Tariff -- the definition of Transmission Revenue Credits and Section 7.1 regarding Access Charges. More specifically, the Tariff defines Transmission Revenue Credits as including "the shortfall or surplus resulting from any cost differences between Transmission Losses and Ancillary Service requirements associated with Existing Rights or Non-Converted Rights and the ISO's rules and protocols."³ Section 7.1 provides, in pertinent part, that:

All Market Participants withdrawing Energy from the ISO Controlled Grid shall pay Access Charges in accordance with this Section 7.1 and Appendix F, Schedule 3. . . . The Access Charge shall comprise of [sic] two components, which together shall be designed to recover each Participating TO's Transmission Revenue Requirement. . . . *The second component shall be based on the Transmission Revenue Balancing Account (TRBA), which shall be designed to flow through to [sic] the Participating TO's Transmission Revenue Credits* calculated in accordance with Section 5 of the TO Tariff and other credits identified in Sections 6 and 8 of Schedule 3 in Appendix F of the ISO Tariff. (emphasis added.)

These provisions, when read together, are clear that the Transmission Revenue Balancing Account is intended to recover the Transmission Revenue Credits, which in turn include the cost differentials in question. On remand, the Commission should give effect to the plain intent of these operative tariff provisions and to the sound policy underlying the Commission's 1997 order, and should reverse Opinion Nos. 458 and 458-A.

In addition, I ask the Commission to consider developments since the Opinions were issued, where the Commission has provided additional guidance regarding the opportunity to seek recovery of "trapped costs" associated with the transition to Regional Transmission Organizations. These recent decisions justify reconsideration of the Opinions. In an Order dated February 24, 2003, for example, the Commission provided transmission owners in the Midwest Independent System Operator, Inc. ("MISO") the opportunity to seek recovery of unrecoverable or "trapped" costs associated with MISO services provided to their existing transmission customers. That Order stated that:

...if a party can demonstrate that such costs are unrecoverable, the Commission will permit it [*i.e.* the transmission owner] to book such costs as a regulatory asset under the Commission's Uniform System of Accounts....⁴

A similar MISO order issued on March 12, 2003 emphasized the Commission's commitment to market development and its intent to provide an opportunity for the recovery of "trapped" costs.⁵

³ California ISO Tariff, Master Definitions Supplement, Appendix A.

⁴ *Midwest Independent System Operator, Inc.*, 102 FERC ¶ 61,193 at P 16 (2003). See also *Midwest Independent System Operator, Inc.*, 102 FERC ¶ 61,192 at P 30 (2003).

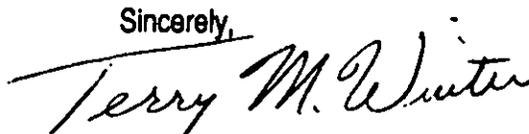
⁵ *Midwest Independent System Operator, Inc.*, 102 FERC ¶ 61,279 at P. 15 (2003).

These cases permitting recovery of cost differentials in two other transmission organizations suggest there are ways to resolve the trapped-cost issues faced by the Companies in California. Moreover, denying such recovery in California but permitting it elsewhere would be unfair, and could aggravate the difficult "seams" issues among adjoining regional systems.

In sum, it appears that Opinion Nos. 458 and 458-A contradict the Commission's current thinking and conflict with its policy to encourage the voluntary formation and expansion of ISOs. I hope that, on further consideration of those orders, the Commission will conclude that such costs are properly recoverable under the tariffs as filed

Thank you for your consideration of this matter.

Sincerely,

A handwritten signature in black ink that reads "Terry M. Winter". The signature is written in a cursive style with a long horizontal stroke at the beginning.

Terry M. Winter
President & Chief Executive Officer

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in the above-captioned dockets.

Dated at Folsom, California, on this 3rd day of March, 2004.


Beth Ann Burns