

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

San Diego Gas & Electric Company,)	
)	
Complainant,)	
)	
v.)	Docket No. EL00-95-000
)	
Sellers of Energy and Ancillary Service Into)	
Markets Operated by the California)	
Independent System Operator Corporation)	
and the California Power Exchange,)	
)	
Respondents.)	
)	
)	
Investigation of Practices of the California)	Docket No. EL00-98-000
Independent System Operator and the)	
California Power Exchange)	

**REPLY COMMENTS OF THE
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION ON
ALLOCATION OF COST RECOVERY OFFSETS**

Pursuant to Rule 212 of the Federal Energy Regulatory Commission's ("Commission") Rules of Practice and Procedure, 18 C.F.R. § 385.212 (2005), and the Commission's September 28, 2005 "Order Granting Motion to Compel and Establishing Schedule for Filing Comments on Cost Allocation Methodology," issued in this docket, the California Independent System Operator ("ISO") submits the following response to comments filed on October 31, 2005,¹ concerning the appropriate method for allocating any Commission-approved cost-based offsets.

¹ The following parties filed initial comments on October 31, 2005: Pinnacle West/Arizona Public Service Company ("APC"); Automated Power Exchange ("APX"); California Parties ("Cal Parties"); Competitive Supplier Group ("CSG"); Constellation New Energy ("Constellation"); and Salt River Project ("Salt River").

I. STATEMENT OF ISSUES

1. The Commission should adopt an allocation methodology that can be feasibly implemented within the ISO's anticipated timeframe for completing the financial adjustment phase
2. Certain of APX's proposals concerning the allocation of cost-recovery offsets are reasonable, but several should be rejected because they would require significant additional effort on the part of the ISO, and are unnecessary.

II. REPLY COMMENTS

As the Commission is well aware, the ISO, along with the California Power Exchange ("PX"), will be responsible for allocating to its market participants any cost-based offset amounts approved by the Commission. In doing so, the ISO is fully committed to supporting the Commission's efforts to complete the refund process as expeditiously as possible. Consequently, the ISO has a strong interest in the adoption of a methodology that is compatible with the ISO's systems and can be implemented efficiently and accurately, preferably within the timeframe contemplated by the ISO for the completion of the financial adjustment phase of the rerun process.² The ISO's comments, therefore, focus on these goals.

A. The Commission Should Adopt an Allocation Methodology that Can be Feasibly Implemented within the ISO's Anticipated Timeframe for Completing the Financial Adjustment Phase

In their initial comments, several parties propose methodologies for allocating approved cost-based offsets to market participants in the ISO and PX markets. The

² The ISO believes that it can complete the calculations relating to the financial adjustment phase in approximately two months, but plans to publish a different, more detailed schedule for completion of the financial adjustment phase in its next rerun status report.

ISO does not take a position on the relative substantive merits of these various proposals – that is, how the various methods would advantage or disadvantage the final result for the different parties. Rather, as noted above, the ISO's concern is that the Commission adopt a methodology that the ISO can implement efficiently and accurately. With that in mind, the ISO offers the following comments on the various proposed methodologies:

First, the California Parties contend that the cost offsets should be allocated based on each purchaser's proportionate share of the total gross ISO and PX refunds, before such refunds are netted against those refund amounts that are owed by each purchaser based on its sales into the ISO/PX markets. Cal Parties at 7. This method would be feasible for the ISO to implement. The ISO's only concern with the California Parties' proposed methodology is their proposal to split the allocation of the cost offsets into pre- and post-CERS periods. Cal Parties at 9. The ISO does not anticipate that this would be a problem, so long as the ISO receives the offset data in a manner that clearly identifies which offsets are associated with which periods. However, if the offset data that the ISO receives is not formatted in this manner, than the ISO would have no logical way of allocating the offsets between the two periods.

CSG contends that the Commission-approved cost-recovery amounts should be allocated so as to simply reduce the level of refunds that would otherwise flow to purchasers that were net purchasers over the Refund Period. CSG at 5-6. The ISO could implement a methodology that allocated cost offset amounts to reduce the refunds owed to net purchasers during the Refund Period. However, the ISO does not agree with CSG's statement that the most "straightforward" way of accomplishing this

would be to take the total refunds resulting from the application of the MMCP, less the cost recovery amounts, and then allocate such net refunds to entities that were net purchasers during the Refund Period. *Id.* This approach would essentially reverse the ISO's intended process of first calculating refunds owed and owing based on the application of the MMCP, which has already been done, taking the amount in cost offsets that each qualifying entity is owed, reflecting that amount as a credit to the entity who made the approved cost filing, and then allocating those amounts to participants that transacted in the ISO markets during the Refund Period. CSG's proposed mechanism would complicate the ISO's calculations and could add more time to the ISO's schedule for completing the financial adjustment phase. Therefore, although the ISO does not object to the basic principle of CSG's proposed allocation methodology -- that is, allocating cost-recovery offsets to entities that were net purchasers during the Refund Period, it does not support CSG's proposed mechanism for applying that methodology. If the Commission were to determine that it was most appropriate to allocate cost-recovery amounts to net purchasers during the Refund Period, then the ISO submits that the most expedient way to implement this methodology would be to reflect those amounts as credits to the entities making the cost filings, and then allocating those amounts to purchasers as offsets to their already calculated refund amounts.

Constellation advocates a methodology that is similar to the one advanced by CSG: cost offsets should be assigned to purchasers that relied on spot sales to serve load, based on their net purchases over the refund period, as offsets to those purchasers' nominal refunds. Constellation at 3-5. This methodology appears to be

generally feasible from an implementation perspective, insofar as its reference to “spot sales to serve load” does not mean that Constellation intends the ISO to differentiate between different “types” of net purchasers in the ISO’s markets. Although some *sales* into the ISO markets during the Refund Period do not meet the Commission’s definition of spot sales, because of the nature of the ISO’s markets, there is no way to match those sales with discrete purchasers, and therefore, there is no way to differentiate between purchasers in the ISO markets based on spot/non-spot sales. The ISO is not certain whether Constellation meant to imply that any such differentiation should be attempted, but the ISO believes it nevertheless important to clarify this issue.

Finally, Salt River proposes that cost offsets be allocated to all purchasers on a gross basis. Salt River at 5. This appears to be a variation on the methodologies proposed by CSG and Constellation, and could be implemented by the ISO. However, the ISO strongly disagrees with Salt River’s contention that the “allocation methodology should very precisely match transactions by . . . scheduling interval.” *Id.* Matching specific transactions, as contemplated by Salt River, would be a very labor-intensive and time-consuming process that would significantly extend the ISO’s timeframe for completing the financial adjustment phase. The ISO estimates that such a process could easily require four to six months to complete, and therefore, submits that such a requirement would be unreasonable given the strong desire of the parties, the Commission, and Congress to complete the refund process as quickly as possible.

B. The ISO Has No Objection to Certain of APX’s Proposals, but Several Should be Rejected as they Would Require Significant Additional Effort, and Are Unnecessary

Rather than proposing a discrete methodology, APX raises a number of subsidiary issues concerning the allocation of cost offset amounts. A number of these issues address directly the manner in which the ISO would process and allocate the offsets, and therefore, the ISO offers the following comments on these matters:

First, APX states that the Commission should require the ISO and PX to explain clearly and in detail how they allocate any offsets to market participants. APX at 3. The ISO has no objection to APX's request, although it appears unnecessary. The ISO will provide a detailed explanation of how it allocates the cost offsets, along with all other adjustments, as part of its compliance filing to be made at the close of the financial adjustment phase.

Next, APX argues that the ISO and PX should establish unique charge types for each category of the financial adjustment phase in "order to provide a transparent breakdown of offsets due to cost-based filings." APX at 4. For the same reason, APX contends that the ISO and PX should not aggregate the offsets into a single charge type, but instead, provide "interval level settlement data for each unique charge type."

Id. The Commission should decline to adopt these suggestions. Developing and implementing new charge types for each of the offsets that the ISO will process as part of the financial adjustment phase would require a significant amount of time and resources, because the ISO would need to modify its settlements software in order to accommodate the new charge types. Therefore, creating new charge types could possibly require an extension in the schedule for completing the refund process. Moreover, such an effort is unnecessary in order to meet the goal articulated by APX – that is, providing market participants with a transparent breakdown of the offsets. The

ISO already plans to include in the settlement statements that include the offsets appropriate comment fields so as to indicate to market participants which specific charges are associated with the various offsets. Also, the ISO plans to distribute to the parties CDs pertaining to each individual offset type (*i.e.* emissions offsets, fuel cost allowance offsets, cost-based offsets). Therefore, market participants should be able to easily and expeditiously review the ISO's allocation of the offsets, without the need for the ISO to spend additional time and resources in developing new charge types. For the same reason, there is no good cause for the ISO to abstain from placing the offsets into a single charge type.

APX contends that the ISO and PX should publish new records for Scheduling Coordinators to process the adjustments relating to the financial adjustment phase, instead of republishing records that have already been processed. APX at 4. APX also states that that the ISO and PX should "flag any interest adjustments that will result from implementation of the cost-based offset filings." APX at 5. The ISO has no objection to these requests, as it already had planned to do both.

II. CONCLUSION

The ISO respectfully requests that the Commission accept these reply comments, and rule consistent with the arguments presented herein.

Respectfully Submitted,

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Certificate of Service

I hereby certify that I have this day served a copy of this document upon all parties listed on the official service list compiled by the Secretary in the above-captioned proceedings, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated this 7th day of November, 2005 at Folsom in the State of California.

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