UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Pacific Gas and Electric Company	)	**Docket No. ER04-688-000**
	)	
	)	**Docket No. ER04-689-000**
	)	
	)	**Docket No. ER04-690-000**
	)	
	)	**Docket No. ER04-693-000**
	)	**(Not Consolidated)**

REPLY COMMENTS ON OFFER OF SETTLEMENT OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION

Pursuant to Rule 602 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (the "Commission"), 18 C.F.R. § 385.602 (2004), and the Notice Shortening Comment Period issued in the captioned dockets on October 19, 2004, the California Independent System Operator Corporation ("ISO") hereby submits its reply comments to the Comments of Southern California Edison Company ("SCE") and Powerex Corp. ("Powerex"). As explained herein, the comments of SCE and Powerex are without merit and should be rejected. The Commission should accept the comprehensive settlement agreement filed in these matters, including the new Transmission Exchange Agreement ("TEA"), without modification.

I. Background

The background to these proceedings is summarized in the Offer of Settlement and accompanying Explanatory Statement filed in the captioned dockets. In addition, the initial comments of the Western Area Power Administration – Sierra Nevada Region

("Western") provide a detailed explanation of the history behind the agreements terminating in these dockets and the need for a comprehensive series of agreements to serve as replacements.[1]

II. Response to Comments

A. SCE's Comments Regarding the TEA Are Without Merit

1. SCE's Claim that the ISO Lacks Authority to Enter Into the Transmission Exchange Agreement Is Unfounded

SCE claims that neither the ISO Tariff nor the Transmission Control Agreement ("TCA") grants the ISO authority to enter into the TEA or procure transmission service from a non-Participating Transmission Owner ("TO"). SCE Comments at 2-3. SCE *construes the ISO's, and this Commission's, authority far too narrowly.*

As an initial matter, the ISO's authority to enter contracts derives from its status as a California corporation and a public utility, not from its tariff. To the extent that those contracts affect transmission service and rates, they are subject to the approval by the Commission. The only issue, then, is whether either the ISO Tariff or the TCA in any manner precludes Commission approval of the TEA. They do not.

SCE misses the point when it quotes the definition of Operational Control in the TCA (and the ISO Tariff) as the basis on which the ISO's authority to enter into the TEA rests. The ISO concedes that it mentioned Operational Control as the springboard for its authority, but SCE's limited focus on the rights of the ISO to direct Participating TOs how to operate their transmission lines and facilities- fails to consider application of this principle in this context. Indeed, consistent with its responsibilities as an Independent

[1] Western sees the TEA as a critical component in the global settlement of these dockets. Western Comments at 18, 21.

System Operator, the ISO must use its rights of Operational Control to optimize the use of the facilities made available to it by the Participating TOs. In this case, that meant working with Pacific Gas and Electric Company ("PG&E") to develop the TEA, with which the ISO will provide the same transmission capacity of nondiscriminatory access as existed previously under Contract 2947A and without which would be available only to California's consumers at pancaked transmission rates.

One could view an agreement such as the TEA as a new Encumbrance on PG&E's facilities. Section 4.4.3 of the TCA specifically authorizes the creation of new Encumbrances with the consent of the ISO. That the TEA is consistent with this approach is reflected in the fact that under Section 6.10 of the TEA PG&E assumes all rights and obligations of the ISO if the ISO ceases to have Operational Control of the facilities. The ISO remains the provider of service until and unless the ISO ceases to have Operational Control of the facilities.

Furthermore Commission approval of the TEA is consistent with the ISO's existing authority to exercise Operational Control over PG&E's facilities. No party to these proceedings would question the significance of the expiration of Contract 2947A and the overriding question of how to preserve that contract's benefits with regard to facilities owned in part by Western, a non-jurisdictional federal entity, and facilities owned in part by PG&E, a Participating TO. In fact, SCE recognizes these unique characteristics and simply asks that the Commission recognize them in any order accepting the TEA. SCE Comments at 15-16. The ISO sympathizes with SCE on this point and understands that its authority to enter into the TEA may necessarily be limited

to the specific benefits outlined below. The ISO, however, entirely disagrees with SCE with that the ISO lacks the authority to request Commission approval of the TEA.

The ISO's authority to exercise Operational Control over facilities owned by Western could also by analogy be compared to an ISO Entitlement as recognized by the TCA and the ISO Tariff. The ISO again would rather characterize the TEA as an extension of its Operational Control in addition to the TCA that enables the ISO to gain access to 1200 MW of transmission capacity made available by Western on the California-Oregon Intertie, a critical transmission path between California and the Pacific Northwest. Since Western has decided not to become a Participating TO, there is no mechanism absent the TEA to make this capacity available for use by the ISO's Market Participants. Moreover, the CAISO's Scheduling Coordinators will not be required to go through the Western, or some other, OASIS to purchase transmission on this path at pancaked transmission rates because of the benefits received in the TEA. As discussed above, the ISO recognizes the unique circumstances presented here and does not seek authority to enter into any arrangement similar to the TEA. Moreover, there is nothing in the ISO Tariff or the TCA that prevents the ISO from requesting Commission approval of the TEA as part of the settlement.

2. SCE's Claim That It Lacked Notice Does Not Withstand Scrutiny

SCE states that neither the ISO nor PG&E can file "a new jurisdictional rate schedule for the first time in the context of a settlement," and that PG&E's "Notice of Filing does not include any mention of the potential replacement agreement." SCE Comments at 4, 14.

SCE's claims are disingenuous. The whole genesis of Docket No. ER04-688-000 was the termination of Contract No. 2947A. PG&E stated in the filing letter specifically that it was requesting a technical or settlement conference "as a vehicle for resolving any issues that may arise concerning what service will be available and under what circumstances following the termination of Contract No. 2947A." PG&E Filing Letter at 2. PG&E also noted that it had met with Western to discuss a successor agreement and "there is good reason to expect substantial benefit if a successor transmission exchange agreement involving Western and the CAISO can be worked out." *Id.* at 5-6. PG&E went on to note that "[s]uch an arrangement could look much like the current Transmission Exchange Agreement." *Id.* at 6. SCE never challenged these representations in its intervention in Docket No. ER04-688. For SCE, after participating in the numerous settlement conferences held in this matter over a five-month period, to claim surprise that a settlement would be reached in this docket that is in accord with the proposal discussed in PG&E's initial filing letter, is unfounded, and SCE's citation to *MCI Telecommunications Corp. v. FCC*, on page 15 of its Comments is without relevance.[2]

Of particular significance, the public notice of a technical conference issued in the captioned dockets and dated May 21, 2004 specifically identified successor agreements as matters to be considered as part of this proceeding. There can be no reasonable issue of lack of notice. The matter is now before the Commission as a settlement. The Commission routinely accepts agreements as part of a settlement of ongoing proceedings without requiring parties to initiate new proceedings.

---

[2] In addition to numerous technical conferences at the Commission, SCE was advised of various meetings and conference calls in California so that they could participate to the extent desired.

3. The Settlement Is In the Public Interest and Should be Accepted

In the Offer of Settlement, the ISO, PG&E, and Western described the benefits associated with the TEA. These benefits include the following:

> The new Transmission Exchange Agreement continues to provide services that benefit a broad range of California end-use customers and offers some benefits unavailable under its predecessor. It will enable the CAISO to access nominally 1,200 MW of import-export service to the Pacific Northwest (less in the south-to-north direction) as part of its open-access service to utilities serving the substantial majority of California's electric customers; this access will be direct to the CAISO instead of via the expiring entitlements of PG&E, SCE and San Diego Gas & Electric Company (collectively, "the Companies") under Contract 2947A. This access will eliminate the possibility of transmission service customers having to pay a pancaked Western rate as well as a CAISO rate to move power between the regions, thus promoting more efficient electricity markets. It will assure the continued location of Western's 500-kV Malin-Round Mountain line, built as part of the Pacific Northwest–Pacific Southwest Intertie in the late 1960s, in the control area operated by the CAISO. It will allow Western to continue to move nominally 400 MW of power between the southern terminus of this 500-kV line and its Central Valley Project transmission lines. And it will give Western operational control of certain facilities, in a major substation owned mostly by PG&E, necessary for the effective, reliable operation of the new sub-control area Western is forming in the control area operated by the Sacramento Municipal Utility District. Approval of the Settlement will avoid unnecessary and costly litigation, avoid regulatory uncertainty and, by avoiding continued uncertainty in the California and western electricity markets concerning how and by whom transactions between California and the Pacific Northwest will be transmitted, promote economic efficiency.
>
> * * *
>
> In addition to the benefits identified above, the Sponsoring Parties note that termination of Contract 2947A without the immediate transition to the Transmission Exchange Agreement will result in more expensive transmission service to the CAISO, Western and PG&E and their respective customers:
>
> - The Western Malin-Round Mountain 500-kV line would not necessarily be part of the ISO Controlled Grid;

- Western would charge its own transmission rates for service between southern Oregon and northern California in addition to the rates charged by the CAISO for transmission within California, and therefore customers in the CAISO control area would pay pancaked rates for transactions with the Pacific Northwest where only one rate is paid currently;

- Western proposed to collect substantial amounts annually in rates for the use of its Malin-Round Mountain 500-kV line; 1,200 MW currently available north-to-south for service to CAISO customers in accordance with the ISO Tariff, including as FTRs, would not be available;

- Due to the lack of CAISO transmission access charge revenues currently associated with Western's Malin-Round Mountain 500-kV line, there would be a net increase in CAISO's access charge because the associated foregone costs would be lower than the lost revenue;

- The CAISO control area boundary might not have continued to be the northern terminus of the California-Oregon Intertie, which is a major trading hub for the West;

- The implementation of Western's decision to form a sub-control area within the control area operated by the Sacramento Municipal Utility District ("SMUD") will be facilitated by the operational control of certain facilities at Cottonwood Substation provided under the Transmission Exchange Agreement; and

- In order to have a complete path for power transfers between the Pacific Northwest and central California, Western was planning to acquire or, if necessary, condemn major PG&E facilities, something the Transmission Exchange Agreement avoids by providing that path under mutually agreeable terms.

Offer of Settlement at 2, 7.

SCE does not dispute these benefits. SCE Comments at 2. To the contrary, in its intervention in Docket No. ER04-693, SCE recognized that "continued coordination pursuant to the OCOA will provide several benefits . . . . The parties who own various parts of the system, will more easily facilitate reliable operation . . . . Coordinated operation results in more efficient use of the major interconnection between California

and the Pacific Northwest, thus enhancing access to competitive wholesale power markets in furtherance of Commission policy." Motion to Intervene of SCE (filed Apr. 22, 2004), at 4.

SCE's claims that the TEA conflicts with the Commission's policy and precedent concerning open access. SCE Comments at 9. To the contrary, the TEA preserves the ISO's current transmission capacity link to vital resources in the Pacific Northwest without the difficulty of making arrangements though multiple transmission providers at pancaked transmission rates. As Western explained in its comments, it is an artifact of history that the lines were constructed so that ownership for different segments was divided between Western and the California investor-owned utilities ("IOUs"). These unique circumstances justify the TEA as being fair and reasonable and consistent with the public interest.

Moreover, the circumstances of the TEA are easily distinguishable from the example of SMUD cited by SCE on page 10 of SCE's Comments. Even SCE recognizes such a "principled distinction" is enough to justify acceptance of the TCA. SCE Comments at 12. The Commission has found that there is no absolute rule as to what constitutes undue discrimination. Rather, the Commission has stated that this question must be evaluated on a case-by-case basis.[3] It should be noted that even SMUD recognizes it is not similarly situated to Western.[4] Rather than filling in a vital link

---

[3] *See, e.g., Southern California Edison Company*, 46 FERC ¶ 61,052, at 61,243 (1989) ("[T]he particular showing required [to prove undue discrimination] will necessarily turn upon the facts of each case, including the characteristics of the customer class involved and the service requested, as well as myriad other potentially relevant factors.")

[4] *See* Affidavit of Brian Jobson filed on October 28, 2004 with SMUD's Supplemental Protest in Docket No. ER04-698, at 7 ("SMUD is not in a position to swap capacity of this magnitude.").

in a transmission path, SMUD simply wanted to "pay PG&E's filed transmission rate in lieu of providing the exchange service offered by Western."[5]

B. Powerex's Comments Should Be Rejected

Under Section 8.1.1 of the TEA, Western notes its desire to sell any excess transmission capacity it is provided under the TEA to third party purchasers, who will enjoy the same cost treatment that Western has under Section 7.4 of the TEA. In order to accomplish this objective, the ISO committed to develop the required systems by January 1, 2006 and, if unable to do so, to implement a manual process to accomplish the same goal. In advance of that timeline, Western committed to "be responsible for scheduling the use of the transmission with the CAISO on behalf of the purchasers for the same cost treatment afforded Western . . . ."

Powerex states that the ISO should be required to use a manual process for allowing third-party purchasers of Western capacity to schedule under Section 8.1.1 of the TEA effective January 1, 2005. Powerex's comments should be rejected. All the agreement establishes is for the first year of operation, Western has agreed to be the Scheduling Coordinator for the transactions across the PACI-W[6] and, if the transaction continues in the ISO Control Area, to perform an Inter-SC Trade with its purchaser.[7] Moreover, while the ISO understands the desire to have this feature available at the earliest possible date, the system change must be integrated with other high-priority

---

[5] *Id.*

[6] The "Pacific AC Intertie ("PACI") comprises the two 500-kV AC lines of the Pacific Northwest-Pacific Southwest Intertie located in northern and central California, and contains the "PACI-W" owned by Western and the "PACI-P" owned by PG&E.

[7] However, it should be noted, that if the transaction does continue in the ISO Control Area and uses ISO Controlled Grid facilities that are not part of the Western Capacity (Malin - Round Mountain - Tracy), then all ISO charges apply in accordance with Section 7.1 of the TEA.

improvements and market redesigns. January 1, 2006 was the earliest date to which the ISO could commit for having the software changes implemented. Manual workarounds are not feasible at the present time given the significant demands on resources to support the California refund proceeding, the market redesign, and ongoing market operations.

III. Conclusion

Wherefore, for the reasons discussed above, the ISO respectfully requests that the settlements in these proceedings be approved without modification.

Respectfully submitted,

/s/ David B. Rubin

David B. Rubin
Robert M. Ivanauskas
Swidler Berlin Shereff Friedman, LLP
3000 K Street, NW
Suite 300
Washington, DC 20007

Charles F. Robinson
General Counsel
John Anders
Corporate Counsel
California Independent System
Operator Corporation
151 Blue Ravine Road
Folsom, CA 95630

Attorneys for the California Independent
System Operator Corporation

Date: November 2, 2004

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 proceedings, in accordance with Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, CA, on this 2nd day of November, 2004.

/s/ John Anders
John Anders