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

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| California Independent System Operator Corporation | Docket No. ER04-115-000 and Docket No. EL04-47-000 |
| Pacific Gas and Electric Company | Docket No. ER04-242-000 and Docket No. EL04-50-000 |

**MOTION FOR CLARIFICATION, OR, IN THE ALTERNATIVE,**
**REQUEST FOR REHEARING OF**
**THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

## I. INTRODUCTION

Pursuant to Section 313(a) of the Federal Power Act, 16 U.S.C. § 251(a) (2001), and Rules 212 and 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212 and 385.713, the California Independent System Operator Corporation ("ISO") hereby submits this Motion for Clarification, or, in the Alternative Request for Rehearing of the Commission's December 30, 2003 Order issued in the above-captioned docket.[1] In support thereof, the ISO states as follows:

## II. BACKGROUND & SUMMARY

The ISO is a California non-profit public benefit corporation, organized pursuant to the Nonprofit Public Benefit Corporation Law for the charitable purposes set forth in Chapter 2.3, Part 1, Division 1 of the Public Utilities Code of the State of California. The ISO, created at the direction of the California Legislature, is charged with assuring open access to the electric

[1] *California Independent System Operator Corporation*, 105 FERC ¶ 61,406 (2003) ("December 30 Order").

transmission grid in the State of California and was organized specifically to ensure efficient use and reliable operation of that grid. *See* Cal. Pub. Util. Code § 300, *et seq.* (West Supp. 1998); CPUC Decision No. 95-12-063 (Dec. 20, 1995), *as modified by* Decision No. 96-01-009 (1996), 166 PUR4th 1 (1996). The ISO is a "public utility" as that term is defined in Section 201 of the Federal Power Act ("FPA"), 16 U.S.C. § 824(e) (2000). The ISO has no stockholders and no rate base on which to earn a return. As a result, the ISO has only one source of revenues -- its Grid Management Charge ("GMC").

The ISO originally filed the 2004 GMC at the Commission on October 31, 2003, as an automatically adjusting formula rate. As such, the 2004 GMC included specific detailed allocation factors that, when applied to the ISO's cost centers and capital projects in each annual budget, would automatically establish the seven charges comprising the GMC for the following year. The ISO acknowledged that should it desire to modify any of these allocation factors, or any other aspects of the GMC rate formula, it would be obliged to submit an application under section 205 of the FPA, 16 U.S.C. § 824d. The ISO also proposed to submit annual informational filings to show the charges resulting from the application of the GMC rate formula to the ISO's budget.

The 2004 GMC filing was noticed by the Commission on November 7, 2003, and numerous parties intervened in response to the ISO's filing. On December 8, 2003, the ISO submitted an answer to intervenors' protests to the Commission, and on December 18, 2003, the ISO submitted an amendment to its answer to the Commission, indicating that it did not support suspension of the GMC rate other than a nominal suspension.

On December 30, 2003, the Commission accepted the ISO's unbundled GMC filing to be effective January 1, 2001, subject to refund.[2] The December 30 Order directed that most of the issues raised in the intervenors' protests be addressed in a settlement conference, and in a subsequent administrative hearing if they remained unresolved in settlement discussions.

With respect to the proposed formula rate mechanism for the 2004 GMC, the December 30 Order acknowledged that "adjustments . . . [to the GMC charges would] result automatically from the operation of the GMC formula."[3] Consistent with its failure to impose such requirements on other utilities and independent system operators with formula rates for the recovery of their costs, the Commission declined to require that the ISO submit "yearly informational filings with the Commission to describe adjustments that result automatically from the operation of the GMC formula," but reminded the ISO that it would have to "make Section 205 filings to implement any future GMC changes."[4]

The ISO reads the foregoing statements in the December 30 Order, which do not reject the automatic operation of the GMC formula and do not indicate that the GMC proposal failed in any respect to satisfy the Commission's requirements for automatically adjusting formula rates, as approving the proposal to employ an automatic GMC formula rate, modified to eliminate the requirement for an annual informational filing. Because the language that the Commission used to approve the ISO's treatment of the GMC as a formula rate was somewhat ambiguous, however, the ISO seeks clarification that it is reading the Commission's order correctly.

In the event, however, that the Commission did not intend to approve the treatment of the 2004 GMC as a formula rate, a decision that is both inconsistent with Commission precedent and

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[2] December 30 Order at P. 17.

[3] *Id.*

[4] *Id.*

for which the Commission did not offer any explanation, the ISO respectfully requests rehearing. In such instance, the ISO believes that upon further consideration, the Commission should approve the GMC as a formula rate. At the very least, the Commission should offer an explanation for its decision, and provide guidance regarding how the ISO could modify the 2004 GMC rate formula so that it may function as an automatically adjusting formula rate (as the Commission Staff offered during the 2001 GMC proceeding).

## III. CONCISE STATEMENT OF ISSUES FOR CLARIFICATION AND SPECIFICATIONS OF ERROR

The ISO respectfully requests that the Commission clarify that it approved the treatment of the ISO's GMC rate as a formula rate that satisfies the requirements the Commission has established for automatically adjusting formula rates. If the Commission declines to grant the requested clarification, the ISO respectfully submits that the Commission erred if it rejected the treatment of the 2004 GMC as an automatically adjusting formula rate, because the 2004 GMC is consistent with Commission policy, which allows for the use of formula rates, and with the requirements the Commission has established for formula rates; because the 2004 GMC rate formula is sufficiently detailed, specific and definitive to addresses the concerns raise by the Commission staff when it opposed the operation of an earlier, less specific GMC rate formula as a formula rate, and because the ISO addressed each of the issues raised by intervenors that could have represented an obstacle to the approval of a formula rate. Moreover, the Commission has approved previously formula rates for other system operators and independent transmission companies that operate less openly and transparently than the ISO's 2004 GMC proposal. Accordingly, the ISO respectfully requests that the Commission grant rehearing to approve the treatment of the 2004 GMC as a formula rate.

## IV. REQUEST FOR CLARIFICATION OR, IN THE ALTERNATIVE, REQUEST FOR REHEARING

In its GMC filing, the ISO added additional specificity to the existing GMC provisions of the ISO Tariff to enable the GMC to function as a fully automatic formula rate that will allow the ISO to eliminate the current requirement for an annual Section 205 filing. That requirement requires the submission of annual rate cases that are costly and time consuming, require resources to be employed by the ISO, stakeholders, and the Commission that could best be devoted to other endeavors, and that create uncertainty each year regarding the ISO's ability to recover its administrative and operating costs. In contrast, recovering the GMC through a formula rate provides greater rate predictability for customers and for the ISO, reduced regulatory risk and reduced regulatory lag, lower filing expenses, reduced administrative expenses, and reduced levels of litigation. *See Southern Company Services, Inc*., 60 FERC ¶ 63,013, 65,151 (1992). To obtain these benefits for the ISO and its customers, consistent with Commission policy, the ISO devised its proposed GMC as a formula rate that satisfies the requirements the Commission has established for such rates.

### A. REQUEST FOR CLARIFICATION

In its December 30 Order, the Commission appeared to approve the treatment of the GMC as a formula rate. However, as the language employed in the December 30 Order is susceptible to different interpretations, the ISO seeks clarification of that Commission decision.

In the Order, the Commission acknowledged that "the operation of the GMC formula"[5] would result automatically in annual adjustments to the GMC. The Commission did not disapprove the automatic operation of the 2004 GMC or find fault with any aspect of the GMC

[5] *Id.*

rate formula. Neither did the Commission direct the ISO to modify the GMC to remove the provisions providing for the automatic updating of the unbundled component charges to reflect the ISO's new annual budget.

Rather, the Commission declined to require that the ISO make annual informational filings at the Commission to show the constituent GMC charges that would result during the following year from the application of the formula to the ISO budget for the year. The ISO had proposed making such filings, in which it would identify the coming year's revenue requirement and budget by cost center, and provide a detailed explanation of how the costs would be allocated among the seven GMC charges, consistent with the detailed allocation formulae in the ISO Tariff. Nevertheless, in declining to require that the ISO make annual informational filings, the Commission's order was consistent with those other instances in which the Commission has approved the use of formula rates by other utilities and independent system operators, but did not require the utility or independent system operator to make annual informational filings to the Commission. The Commission appears to be satisfied with the ISO's commitment to make its annual revenue requirements and detailed budget publicly available, so that market participants may examine the budget and the rates and seek redress from the Commission pursuant to Section 206 of the Federal Power Act if appropriate.

The Commission then ordered that the ISO "make Section 205 filings to implement any future GMC changes."[6] This directive was consistent with the ISO's acknowledgment in its Answer that "[o]nce the Commission accepts the GMC formula rate, [the ISO] cannot modify any element of the approved formula, including the allocation factors included in it, without a

[6] *Id.*

filing under Section 205."[7] The ISO thus views this statement as entirely consistent with its proposal for an automatically adjusting GMC rate formula, which formula can only be changed through a section 205 filing.

The ISO believes the Commission's decision to accept the 2004 GMC as an automatic formula rate is well-founded. As the ISO explained in its Answer to comments and protests:

- the Commission has the authority to approve formula rates;
- the 2004 GMC formula rate satisfies the Commission's requirements for automatic formula rates and addresses concerns identified by the Commission Staff in its review of the proposed 2001 GMC formula rate; and,
- the ISO addressed in its December 8 Answer the concerns raised by intervenors in their protests to the October 31 filing.[8]

The ISO is concerned, however, that the language employed by the Commission is somewhat ambiguous in one respect. The Commission's directive that the ISO file under section 205 "to implement any future GMC changes" could be read to require filings each year for the new charges that result from the application of the GMC formula that the Commission accepted, even though no change is proposed to the GMC itself. The ISO believes such an interpretation of the December 30 Order would be erroneous and inconsistent with the Commission's overall treatment of the ISO's formula rate proposal. The December 30 Order should be clarified to prevent such a misreading. As noted above, the December 30 Order did not identify any inconsistency with the Commission's applicable requirements or any other shortcoming in the proposed 2004 GMC formula rate and did not require the ISO to modify those portions of the 2004 GMC formula that provide for its automatic operation. Nevertheless, the uncertainty created by this ambiguity could impair the ISO's ability to implement GMC charges for 2005.

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7 ISO Answer at 52.

8 ISO Answer at 44-55.

Accordingly, the ISO seeks clarification that the Commission approved the operation of the 2004 GMC as a formula rate so that both the ISO and the participants in the California electricity market may benefit from the increased certainty and decreased administrative costs of annual GMC filings.

### B. ALTERNATIVE REQUEST FOR REHEARING

In the event that the Commission declines to clarify that it intended to approve the treatment of the GMC as a formula rate, the ISO respectfully requests that the Commission grant rehearing. The ISO, like other independent system operators and regional transmission operators, should be permitted to employ an automatically adjusting formula rate to recover its operating and administrative costs. The Commission has the authority to approve formula rates, and the 2004 GMC represents an appropriate case for it to exercise that authority. The proposed 2004 GMC formula rate satisfies the Commission's requirements for formula rates and addresses the concerns identified by the Commission Staff in its review of the proposed 2001 GMC formula rate, as well as those raised by intervenors in their protests to the October 31 filing.

#### 1. The Commission's Authority to Approve Formula Rates is Clear

The Commission's power to authorize the ISO to employ a formula rate is clear, as acknowledged by the Court of Appeals for the District of Columbia, which stated that that "[i]t can hardly be doubted at this late date that the Commission 'need not confine rates to specific, absolute numbers but may approve a tariff containing a rate 'formula' or a rate 'rule,''" as "[t]he Commission has been accepting formula rates since the early 1970s." *Public Utilities Comm'n of California v. FERC*, 254 F.3d 250, 254 (D.C. Cir. 2001) (citations omitted). The Commission has long “recognized the advantages afforded by the use of automatically adjusting cost-of-service formula rates,”[9] and has approved their use in a wide variety of circumstances.[10]

The Commission’s acceptance of formula rates “is premised on the rate design’s ‘fixed, predictable nature,’ which both allows a utility to recover costs that may fluctuate over time and prevents a utility from utilizing excessive discretion in determining the ultimate amounts charged to customers.” *Public Utilities Comm'n of California v. FERC*, 254 F.3d 250, 254 (D.C. Cir. 2001) (citations omitted). Accordingly, the Commission has found that “formula rates that are not specific are unacceptable,”[11] requiring that a formula rate “provide details of all formula calculations,”[12] although there is no “absolute prescribed standard literally set forth in the statute and regulations” regarding the level of detail in a formula rate. *Public Utilities Comm'n of California v. FERC*, 254 F.3d 250, 255 (D.C. Cir. 2001) (citations omitted).

The ISO’s proposed 2004 GMC formula rate “provide[s] details of all formula calculations,” as the Commission’s precedents require.[13] The formula rate includes both the description of the costs that are recoverable and the specific allocation factors used to allocate

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9 *Louisiana Public Service Commission v. Arkansas Power & Light Co.*, 44 FERC ¶ 61,392, 62,270 (1988); *see also, e.g, Central Power & Light Co.*, 11 FERC ¶ 61,102 (1980); *Middle South Services, Inc., Opinion No. 124*, 16 FERC ¶ 61,101 (1981), *aff'd, Louisiana Public Service Commission v. FERC*, 688 F.2d 557 (1982), cert. denied, 460 U.S. 1082 (1983).

10 *See., e.g.*, Midwest ISO, FERC Electric Tariff, Second Revised Volume No. 1, at Schedule 10 (approved formula rate used by RTO); PJM Interconnection, L.L.C., FERC Electric Tariff Sixth Revised Volume No. 1, at Schedule 9 (approved formula rate used by RTO); *Avista Corporation, et al*., 100 FERC ¶ 61,274, 62,071 (2002) (Commission approval of use of formula rate by RTO); New York Independent System Operator, Inc., FERC Electric Tariff, Original Volume No. 2, Rate Schedule 1 (approved formula rate used by ISO); *TRANSLink Development Co*., 103 FERC ¶ 61,208 (2003) (Commission approval of use of formula rate by ITC); *San Diego Gas & Electric Company*, 105 FERC ¶ 63,026 (2003) (Commission approval of use of formula rate by integrated utility).

11 *Maine Yankee Atomic Power Company*, 42 FERC ¶ 61,307, 61,923 (1988) (“Maine Yankee”).

12 *Maine Yankee*, 42 FERC at 61,923.

13 *Maine Yankee*, 42 FERC at 61,923.

each cost center in the ISO's budget among the various GMC charges. The individual GMC charges therefore may be calculated by applying the allocation formulae incorporated in the tariff to the ISO's annual budget by cost center. The inclusion of a detailed matrix of allocation factors to allocate 175 cost centers to seven GMC charges provides not only a greater degree of precision and specificity than the current GMC formula, but greater precision and specificity than other formula rates that the Commission has already approved elsewhere.[14] In addition, as explained above, the ISO recognized and acknowledged that approval of the GMC as a formula rate would not authorize the ISO to make changes *to* the GMC formula without a section 205 filing. The ISO thus could not eliminate one of the seven GMC charges, add a new one, or modify the allocation of costs among them, without a section 205 filing. Accordingly, the ISO submits that the formula rate is sufficiently precise, is explained in sufficient detail and is sufficiently accurate to meet the Commission's requirements so that the Commission may approve the formula rate.

In fact, the ISO's proposal exceeded the Commission's requirements for implementation of formula rates, by committing the ISO to submit annual informational filings with the Commission which would include both the ISO's annual budget by cost center and an application of the allocation factors in the ISO's OATT to the budget. This filing would facilitate both market participants' and the Commission's review of the ISO's costs and the manner in which such costs were applied to each of the GMC charges through application of the formula contained in the OATT. Such a requirement, as already noted, exceeds the requirements imposed on other system operators by the Commission. For instance, the Commission approved

[14] *See*, *e.g.*, *TRANSLink Development Co*., 103 FERC ¶ 61,208 (2003) (approval of formula rate with all costs allocated to only two separate administrative charges adjusted for over or under collections in previous years).

TRANSLink's proposed formula rate, in which TRANSLink simply committed to posting its budget and the calculation of its rates for the forthcoming year on its web site each fall, so that market participants would be apprised of the new rates before they went into effect.[15] The Commission has approved similar practices for PJM and the American Transmission Company.[16] While, consistent with its decisions in these other cases, the Commission deemed annual informational filings by the ISO to be unnecessary in the December 30 Order, it does not follow that the only alternative to annual informational filings is annual filings under section 205. Rather, the Commission should authorize the ISO to employ the fixed, detailed 2004 GMC rate as an automatic formula rate.

### 2. The ISO's 2004 GMC Formula Rate Complies With the Commission's Requirements for Formula Rates

The December 30 Order did not identify any respect in which the 2004 GMC formula rate fails to comply with the Commission's requirements for formula rates. In fact, the ISO carefully designed the GMC formula rate to provide the detail and specificity that the Commission requires for formula rates and to address shortcomings that were identified by the Commission Staff in the ISO's previous GMC formula rate proposal.

#### a. In Designing the 2004 GMC Formula Rate, the ISO Addressed Concerns Identified by the Commission Staff in its Criticism of the ISO's Proposed 2001 GMC Formula Rate

In developing the proposed formula rate, the ISO directly addressed concerns raised by Commission Staff in the 2001 GMC proceeding. In the 2001 GMC proceeding, the Commission's Staff witness discussed the ISO's proposed formula rate, and identified a number

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15 *See*, *Midwest ISO OATT,* Attachment O – TRANSLink, Exhibit 4, at Original Tariff Sheet 399Z.10.

16 *See*, *Midwest ISO OATT*, Attachment O – ATC, Original Tariff Sheet 394; *See PJM OATT*, Schedule 9, item d) at Original Sheet 250, Schedule 9, item i) at Original Sheet 252.

of shortcomings. He stated that while the "CAISO formula calculations are not reduced to writing in the ISO Tariff," the "Commission believes that a proposed formula rate should show *all details of formula calculations in the rate schedule* (*i.e.*, ISO Tariff) because a lack of computational specificity permits the company to revise the calculation (and the charges to the customer), at its discretion without a proper filing with the Commission."[17] He went on to state that "[i]f the CAISO wants to use a formula rate in a FERC-jurisdictional rate schedule, it needs to comply with Commission precedent concerning formula rates," which requires that "all details of formula calculations . . . be included in the rate schedule so that the company is not permitted to revise the calculations at its discretion."[18]

In direct response to the Commission Staff's critique of the 2001 proposed GMC formula rate, the ISO developed for the 2004 GMC a detailed formula rate that included specified allocation factors, and incorporated the detailed formula rate directly into its tariff. Because the ISO's proposal incorporated the formula rate, including all allocation factors, into the ISO Tariff, the ISO would not be able to modify it without Commission approval in a subsequent Section 205 filing, consistent with Commission policy and Staff's testimony. *See also* 16 USC § 824d(d). The deficiencies identified in the ISO's previous formula rate proposal have thus been remedied in the 2004 GMC formula rate.

b. The ISO Addressed in its December 8th Answer Each Concern <u>Raised By Intervenors in Their Protests to the October 31 Filing</u>

In its December 8 Answer, the ISO responded to each of the concerns raised by intervenors in their protests to the October 31 Filing.

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17 Prepared Written Direct Testimony of Stephen D. Pointer, June 21, 2001, Exhibit S-6 in Hearing in Dockets ER01-313-000, et al., at 15 (Emphasis in original.)

18 *Id.* at 15-16.

(i) The GMC Formula Rate Is Detailed and Specific

Intervenors suggested that the ISO's formula rate is not sufficiently detailed. In its Answer, the ISO explained that its proposed formula rate is sufficiently detailed that using the data provided in the 2004 budget by cost center included GMC filing (and in the budgets that the ISO will prepare in forthcoming years), the exact GMC charges may be calculated by allocating the costs assigned to each cost center across each of the seven GMC charges based on the percentages stated in Schedule 1, Part E, Table 1 of ISO OATT. Tab B; Exh. Nos. ISO-20 and 21. The sum of the portion of each cost center allocated to each category represents the total GMC costs recoverable through that category. Given that the rate may be calculated simply by applying allocation factors that are contained in the tariff to budgets that will be included in annual informational filings at the Commission, there can be no question that the proposed revisions to the GMC formula do not contain ample detail to meet the Commission's requirements.

The formula rate incorporated into the tariff also is significantly more precise than the rate approved by the Commission in 2001. To calculate the previously approved GMC, the ISO allocated its costs across three different functions in an attempt to base customer charges on the underlying costs related to the services provided to those customers. The allocation factors were not specified in the GMC formula previously approved by the Commission and incorporated in the ISO Tariff. The proposed 2004 GMC Rate formula, in contrast, allocates the ISO's costs across seven different functions using the matrix of allocation factors included in the ISO Tariff, ensuring a greater degree of transparency and of alignment between cost causation and customer charges. The ISO's submission of a GMC rate formula that assigns its costs to seven functions, in accordance with detailed allocation factors set out in the tariff, certainly meets the Commission's standards for precision and definitiveness in formula rates.

Finally, to the extent that intervenors expressed concerns that that the allocation factors incorporated into the ISO's OATT were simply incorrect, their concerns were misplaced. As explained in the testimony of Ms. Catherine Yap, the costs attributable to each cost center were directly assigned to different functions in instances where, "upon completion of a detailed cost study, there is evidence that demonstrates the direct connection between the costs and the functional activities." Exh. No. ISO-3 at 29:8-10. Where there is no direct linkage, "costs are allocated using an allocation factor that best associates the costs with the various functional areas." Exh. No. ISO-3 at 29:10-12. In order to improve the precision of the GMC, the ISO significantly increased the percentage of costs that were directly assigned (rather than allocated) over the percentage in the 2001-2003 GMC structure. Exh. No. ISO-3 at 29-30. In any event, the intervenors will be able to pursue any concerns about particular allocation factors in the proceedings the Commission has prescribed. For present purposes, what matters is that the allocation factors are set forth in the ISO Tariff to enable the GMC rate formula to operate with precision and clarity.

The formula rate is incorporated into the tariff with sufficient detail that when applied to an ISO budget by cost center (which, as discussed above, was included in the ISO's filing this year and will be made available for public comment in subsequent years), the resulting rates may readily be calculated and the calculations audited. The assignment of the revenue requirement to seven, instead of three categories represents an improvement in the precision of the link between cost causation and customer charges. Also, the calculation of allocation factors based on the detailed analysis described by Ms. Yap ensures that the calculation is as accurate as possible. Accordingly, the ISO's formula rate unquestionably meets the Commission's standards that a formula rate be sufficiently detailed.

(ii) The GMC Formula Rate May Not Be Amended Without Subsequent Section 205 Filing

One intervenor contended that the ISO's GMC filing sought approval for the right to alter the rate formula without a Section 205 filing.[19] As noted above, such an assertion simply is not true, as the ISO has incorporated the formula rate directly into its tariff in order to meet the Commission's requirements that "the specific formula calculations be reduced to writing and incorporated into the rate schedule," *Maine Yankee Atomic Power Company*, 42 FERC ¶ 61,307, 61,923 (1988) , and to address concerns raised by Commission staff in the review of the 2001 GMC. *See*, Exh. No. ISO-89 at 15-19.[20] To make any change to the allocations or other elements of the GMC rate design, the ISO will be required to seek Commission approval pursuant to Section 205 of the Act.

(iii) A Formula Rate Is Particularly Appropriate for the Recovery of Administrative and Operating Costs by Independent System Operators

One intervenor claimed that formula rates were not appropriate for an independent system operator or regional transmission organization, because such entities are, in principle, servants of the market and market participants.[21] While the ISO agrees that its objective is to operate a reliable and efficient transmission platform and market structure, this premise does not support the intervenor's conclusion. In fact, the claim that ISOs and RTOs should not employ

[19] TANC at 8.

[20] That the ISO recognized that it cannot modify any element of the approved formula, including the allocation factors included in it, without a filing under Section 205 is clear from the testimony of Ms. Catherine Yap, who explained that, if the basis of any of the cost allocation factors changes significantly, the ISO would have to "file modifications to the table of allocators under Section 205," Exh. No. ISO-3 at 45:2-3, which states in part that "[u]nless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public." 16 USC § 824d(d).

[21] MID at 34.

formula rates is belied by the Commission's acceptance of formula rates for the recovery of costs by other independent system operators.[22]

(iv) Market Participants Will Retain Ability to Examine the ISO Budget and the Resulting GMC Charges and Seek Relief From the Commission if the GMC Formula Rate Results in Unjust and Unreasonable Charges

Several intervenors stated that the Commission should not approve a formula rate because doing so would undermine the ability of market participants to ensure that the ISO's future expenditures were not excessive.[23] These intervenors ignore the other mechanisms that are available to provide that the ISO's costs are just and reasonable. First, as described in Ms. Yap's testimony, market participants will have the opportunity to participate in the development of the ISO's annual budget and to review both the outcome and basis of the ISO's budget and the charges that will result from the application of the proposed GMC formula rate to each annual budget in a budget process that "includes the publication of a proposed budget, workshops in which the proposed budget is explained to stakeholders, who are given opportunities to ask questions and raise concerns, and adoption o the final budget by the ISO Governing Board in a public session." Exh. No. ISO-3 at 45: 7-12. Then ISO also proposed making an annual informational filing, which would "contain the information needed to update the ISO's GMC formula rate for the upcoming year, presented in conformance with FERC's uniform system of accounts." Exh. No. ISO-3 at 45:14-16. Subsequently, if any market participant believes that the application of the GMC formula rate to an approved ISO budget results in excessive charges, it will have access to the information necessary to frame a request for relief from the

[22] *See e.g.*, New York Independent System Operator, Inc., FERC Electric Tariff, Original Volume No. 2, Rate Schedule 1.

[23] MID at 33; TANC at 8; SWP at 11-12.

Commission. As discussed above, the Commission declined to require such a filing, consistent with the requirements imposed on other parties with Commission-approved formula rates.

The usual approach taken by parties seeking to challenge a utility's expenditures is to file a complaint pursuant to Section 206 of the Act. Approval of the GMC will in no way affect market participants' Section 206 rights -- market participants will retain their rights to file a complaint pursuant to Section 206 of the FPA to challenge the justness and reasonableness of the charges produced by the GMC rate formula, if they raise substantial questions about the reasonableness of the ISO's budgeted costs. Those rights are adequate and appropriate. In addressing the issue of whether Section 206 of the Act provides market participants adequate protection against unjust and unreasonable rates, the Court of Appeals for the District of Columbia stated that

> [i]n approving formula rates, the Commission has relied on [Section] 206 as a mechanism to ensure that the rates are just and reasonable, and its reliance on [Section] 206 has survived judicial scrutiny,

*Public Utilities Comm'n of California v. FERC*, 254 F.3d 250, 257 (D.C. Cir. 2001) (citations omitted), noting that the availability of Section 206 means that the "Commission's acceptance of the ISO's formula rate without additional [Section] 205 filings does not leave CALPUC or ratepayers without any statutory recourse." *Id*. If the market participants identify and document any meaningful concerns that the ISO's budget that forms the basis of the charges under the Revised GMC Rate formula includes excessive costs, they have the right and ability to bring those concerns to the Commission's attention and to obtain relief.[24] Morevoer, the Commission

[24] As an aside, the ISO notes that notwithstanding much carping by market participants concerning the ISO's expenses, the intervenors, who were first presented with the ISO's 2004 budget on September 25, 2003, have yet to identify a significant volume of inappropriate expenses in support of their contention that the ISO's budget is excessive. In fact, the ISO's 2004 GMC revenue requirements is approximately $20 million lower than its 2003 revenue requirement.

apparently has relied on Section 206 of the Act as the appropriate mechanism through which market participants may challenge expenditures of utilities with Commission-approved formula rates.

(v) The Forthcoming Implementation of Locational Marginal Pricing is no Impediment to Adoption of GMC Formula Rate

One intervenor contended that the Commission should not approve the 2004 GMC as a formula rate because it will have to be redesigned when locational marginal pricing ("LMP") is introduced into the California market.[25] The pending implementation of LMP, however, does not render the proposed Revised GMC Rate formula inappropriate *now*. The ISO acknowledges that when LMP is introduced to the California market, the ISO may need to make changes to the GMC rate formula. Because the detailed structure of the LMP mechanism that will be implemented by the ISO has not yet been established, however, it is unclear exactly what, if any, changes may need to be made to the GMC rate formula. Moreover, although the ISO anticipates that LMP may be introduced to California as soon as next fall, the ISO recognizes that this timetable is subject to delay.

The ISO does not believe that the possibility of a forthcoming change in the California energy market, which may require some modification to the GMC, justifies delaying implementation of a formula rate now, and at a minimum, should permit the avoidance of a new rate case for 2005, when ISO staff will be fully dedicated to the MD02 implementation effort and other important matters. When the ISO does submit a filing setting forth the detailed revisions to the ISO Tariff required to implement LMP, it will include any necessary changes to the GMC rate formula.

[25] MID at 35.

## V. CONCLUSION

WHEREFORE, the ISO respectfully requests clarification or, in the alternative, rehearing of the issue discussed above.

Respectfully submitted,


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Dated: January 29, 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 proceeding.

Dated at Folsom, CA, on this 29th day of January, 2004.

/s/ *Stephen A.S. Morrison*
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