UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

California Independent System Operator Corporation	Docket Nos. ER00-2019-015 ER01-819-008 ER03-608-005

ORDER DENYING REHEARING AND GRANTING CLARIFICATION

(Issued June 2, 2005)

1. In Opinion No. 478,[1] the Commission for the most part affirmed an Initial Decision concerning the California Independent System Operator Corporation's (ISO) Transmission Access Charge (TAC),[2] but reversed it on the issue of cost shift caps; affirmed a related Partial Initial Decision;[3] denied requests for rehearing of earlier orders in this proceeding; deferred decision on the issue of whether there should be a behind the meter exception to the assessment of the TAC on a gross load basis; and dismissed the ISO's compliance filing as premature. Various parties filed timely requests for rehearing and/or clarification of Opinion No. 478. In this order, we grant requests to clarify certain aspects of Opinion No. 478, and deny the requests for rehearing.

Background

2. On March 31, 2000, the ISO filed Amendment 27 to its tariff, proposing the TAC, which the Commission accepted and suspended in an order issued in May 2000.[4] Until the ISO's filing, the access charge consisted of three separate zone rates based on the revenue requirements of the Participating Transmission Owners (TO).[5]

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[1] *Cal. Indep. Sys. Operator Corp.*, 109 FERC ¶ 61,301 (2004) (Opinion No. 478).

[2] *Cal. Indep. Sys. Operator Corp.*, 106 FERC ¶ 63,026 (2004) (Initial Decision).

[3] *Cal. Indep. Sys. Operator Corp.*, 105 FERC ¶ 63,008 (2003) (Partial Initial Decision).

[4] *Cal. Indep. Sys. Operator Corp.*, 91 FERC ¶ 61,205 (2000) (May 2000 Order), *order on reh'g*, 104 FERC ¶ 61,062 (2003) (July 2003 Order).

[5] The three original Participating TOs are Pacific Gas and Electric Company

With Amendment 27, the ISO proposed a ten-year transition period during which High Voltage Access Charges for the TAC areas[6] would merge to form a single grid-wide access charge. This would be accomplished by blending a cumulative ten percent per year of the individual High Voltage Transmission Revenue Requirements (TRR) for each TAC area with the sum of the TRRs of the Participating TOs.

3. In the May 2000 Order, the Commission accepted the proposed tariff amendment with effective date of June 1, 2000, subject to refund, suspended it for a nominal period, and established settlement judge procedures. Additionally, the May 2000 Order, in order to assist settlement efforts, discussed the major issues that would have to be set for hearing. Among these issues were whether the ten-year transition period and proposed limits on cost shifts, as well as the proposed treatment of Firm Transmission Rights (FTR) were just and reasonable, and whether the ISO's exception from gross load billing for existing Qualifying Facilities was non-discriminatory.

4. Settlement negotiations continued for the next two and a half years, but proved to be unsuccessful. In December 2002, the Commission's Chief Administrative Law Judge therefore terminated the settlement judge procedures and initiated hearing procedures.

5. On March 11, 2003, the ISO filed Amendment 49 to its tariff, proposing certain modifications and clarifications to Amendment 27 concerning the TAC rate design. In an order issued on May 30, 2003,[7] the Commission accepted in part and rejected in part the ISO's proposed tariff amendment, and consolidated the hearing on the amendment with the ongoing Amendment 27 proceeding.

6. Meanwhile, the hearing procedures continued under the auspices of the presiding judge. In the course of the proceeding, SoCal Edison filed a motion for partial summary disposition on the issue of what facilities should be placed under the ISO's operational control and thus included in the TRRs of the Participating TOs. On October 21, 2003, the judge issued the Partial Initial Decision, excluding that issue from this case.

7. Subsequently, the presiding judge conducted the hearing in these proceedings, and on March 11, 2004, issued the Initial Decision.

8. On December 21, 2004, the Commission issued Opinion No. 478. In Opinion No. 478, the Commission affirmed the Initial Decision on the issues of phantom

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(PG&E), Southern California Edison Company (SoCal Edison), and San Diego Gas & Electric (SDG&E).

[6] The TAC areas correspond to the historical control areas of the three original Participating TOs.

[7] *Cal. Indep. Sys. Operator Corp.*, 103 FERC ¶ 61,260 (2003) (May 2003 Order).

congestion, FTRs, and high-low-voltage split; reversed the Initial Decision on the issue of cost shift caps; and deferred decision on the issue of whether there should be a behind the meter exception to assessment of the TAC on a gross load basis. Additionally, the Commission summarily affirmed the findings made by the presiding judge with respect to (1) the relevant factors informing the decision, (2) time-of-use rates, (3) treatment of existing contracts, and (4) evidentiary determinations. The Commission also affirmed all other findings and conclusions of the presiding judge.

9. Rehearing requests of Opinion No. 478 were filed by the Cities of Anaheim, Banning, Colton, and Riverside, California (Southern Cities); Northern California Power Agency (NCPA); City of Vernon, California (Vernon); State Water Contractors and Metropolitan Water District of Southern California (SWC/Metropolitan); and the California Department of Water Resources State Water Project (DWR).[8] SoCal Edison, Modesto Irrigation District (Modesto), and City of Santa Clara, California d/b/a Silicon Valley Power (Silicon Valley Power) timely requested rehearing and/or clarification.

10. On February 7, 2005, the ISO filed a motion for leave to file a response and a response to Silicon Valley Power's request for clarification or rehearing and to the requests for rehearing of SWC/Metropolitan and Vernon. On February 22, 2005, DWR and SWC/Metropolitan filed responses to the ISO's answer.

Discussion

Procedural Matters

11. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 213(a)(2) (2004), prohibits an answer to a request for rehearing unless otherwise ordered by the decisional authority. We are not persuaded to accept the ISO's answer, and will, therefore, reject it. Accordingly, we dismiss the responses by DWR and SWC/Metropolitan as moot.

Cost Shift Cap

Opinion No. 478

12. As part of its TAC rate design, the ISO proposed an annual limitation or "cap" on the increase in payment responsibility applicable to gross loads in the service area of an original Participating TO during the proposed ten-year transition period. In Opinion No. 478, the Commission reversed the presiding judge's ruling to eliminate the cost shift

[8] DWR has sometimes been referred to in this proceeding as SWP.

cap.[9] Therefore, the Commission did not reach alternative cost shift cap proposals submitted by PG&E and SoCal Edison. Opinion No. 478 affirmed the presiding judge's ruling regarding the exclusion of High Voltage transmission facilities from the transition charge and the immediate inclusion of High Voltage transmission facilities in the grid-wide component of the TAC for the reasons discussed in the Initial Decision.

13. The Commission found that, in the Initial Decision, the presiding judge had misinterpreted our May 2000 Order, which required that "the record *include*, on a broader level, information on the overall impact of changes in transmission costs on the overall cost of electricity," basing her finding solely on this criterion.[10] In our view, the standard used by the presiding judge was contrary to the Commission's long-standing practice of measuring transmission rate increases against the transmission component of rates.

14. Accordingly, Opinion No. 478 discussed the merits of certain exhibits that evaluated the ISO-proposed, annual $32-32-8 million dollar cost shift cap (totaling $72 million annually during the transition period) for SoCal Edison, PG&E, and San Diego, respectively, on actual transmission costs. Based on the relevant portions of the record, we concluded that: (1) cost shifts from the implementation of the TAC proposal have occurred and will continue to occur; (2) these cost shifts to the customers of the Participating TOs are potentially significant; and (3) the ISO-proposed cost shift cap is crucial in balancing the benefits and burdens of ISO participation reasonably among the new and original Participating TOs.

Requests for Rehearing

15. While SoCal Edison agrees that the record clearly supported a finding that some cap is necessary, it disagrees with the magnitude of the Commission-approved cap. In particular, SoCal Edison states "that the Commission correctly noted that the TAC methodology adopted in this proceeding, including the costs that such methodology shifts to the ratepayers of the original Participating TOs and the caps on these shifts, must be evaluated under the just and reasonable standard of the Federal Power Act [FPA] and

[9] The presiding judge similarly eliminated the hold harmless provision. The hold harmless provision protects new Participating TOs from any increase in transmission rates during the transition period as a result of their ISO participation. As NCPA correctly notes in its rehearing request, the "Initial Decision struck the 'hold harmless' provision in tandem with the cost shift caps. No party opposed this linkage." NCPA Rehearing at 8 & n.4 (citing Initial Decision, 106 FERC ¶ 63,026 at P 359). Thus, Opinion No. 478 restored the hold harmless provision when it restored the cost shift cap. This aspect of the decision has not been contested on rehearing.

[10] Opinion No. 478, 109 FERC ¶ 61,301 at P 64 & n.50 (quoting May 2000 Order, 91 FERC at 61,725 (emphasis added)).

must reflect the appropriate balance of costs and benefits among original and new Participating TOs."[11]

16. However, SoCal Edison seeks rehearing because it believes that the Commission's adoption of the 32-32-8 cost shift cap "did not take into account [the Commission's] prior order that eliminated the buy-down provision, which had served to modify the relative costs and benefits from the levels adopted by the ISO Board through the stakeholder process."[12] SoCal Edison further states that "the Commission has concluded that deference to the conclusions reached by the ISO Board is appropriate, given the record evidence; yet, in an action inconsistent with this ruling, the Commission has not reduced the caps from the amounts approved by the [ISO] Board to reflect that the Commission itself modified the Board's proposed balance of costs and benefits when it rejected the buy-down component of the Board proposal."[13] Alternatively, SoCal Edison believes that the record evidence actually supports its proposed cap of $20 million for SoCal Edison, $20 million for PG&E, and $5 million for San Diego.[14]

17. NCPA argues emphatically that the Initial Decision properly concluded that the ISO-proposed cost shift cap was unjustified because the record evidence does not support the existence of rate shock. Furthermore, NCPA states that "Opinion No. 478 disregards the fact that the rate impact of the alleged cost shifts will be trivial at most, and completely ignores the fact that the cap will function as a deterrent to the goal of expanded [ISO] membership."[15] NCPA further contends that, "in choosing to defer to the [ISO] stakeholder process, the Commission deprives NCPA and other similarly-situated entities of the fair consideration of the impact these TAC proposal[s] would have on their ability to recover their revenue requirements."[16] Finally, NCPA argues that "the Commission's misguided adoption of a 'balancing' approach that, in effect, imposed an

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[11] SoCal Edison Rehearing at 3 (citing Opinion No. 478, 109 FERC ¶ 61,301 at P 64 and 68).

[12] Under the proposed "buy-down" provision, new Participating TOs would have been required to use any cost-shifting benefits they received solely to reduce their transmission plant investment, which, in effect, would lower their transmission revenue requirements over time. The Commission's May 2000 Order rejected the buy-down provision, finding it to be unsupported and potentially discriminatory.

[13] SoCal Edison Rehearing at 3.

[14] *Id.* at 6 (citing Ex. SCE-5 at 13-22).

[15] NCPA Rehearing at 4.

[16] *Id*. at 20.

irrebuttable presumption that both the original proposal and the process that spawned it were just and reasonable" will not withstand judicial scrutiny.[17]

18. The Southern Cities claim that, in Opinion No. 478, the Commission relied entirely on a rate impact standard in its acceptance of the ISO-proposed cost shift cap. Moreover, they state that the Commission ignored arguments that the cost shift cap should be rejected as being unnecessary, arbitrary, discriminatory, and inconsistent with Commission precedent and policy on network pricing principles and Regional Transmission Organization (RTO) formation. Southern Cities also argue that the Commission erred in reinstating the cap without revising the methodology for calculating cost shifts to include the costs of post-January 1, 2001 transmission investments in the calculation of average transmission costs. Southern Cities further contend that "the inappropriately static cut-off date [January 1, 2001] for assessing average transmission costs in the cost shift calculation inures to the particular detriment of the publicly-owned utilities who have either recently joined the ISO or are contemplating doing so," and undermines the Commission's goal in Order No. 2000 of including public power in its RTO-formation policy.[18]

19. Vernon contends that the Commission erred: (1) in granting deference to the stakeholder process because, among other things, this process did not reach a conclusion as to caps; (2) in finding that the cap does not appear to produce an unreasonable result and, if exceeded, it is reasonable for the new Participating TOs to continue to recover their respective TRRs from their ratepayers; (3) in finding that the cost shift cap is not unduly discriminatory; (4) in finding that the elimination of the buy-down provision in the May 2000 Order supports the cost shift cap; (5) in departing from the May 2000 Order, which determined that the cap should be evaluated against total-delivered-energy-costs; and (6) in determining that balancing benefits and burdens of the new and original Participating TOs supports a finding that the cost shift cap is just and reasonable.[19]

Commission Determination

20. We deny the parties' requests for rehearing concerning this issue; however, we clarify further our position as discussed below.

21. In Opinion No. 478, the Commission considered the presiding judge's ruling in the Initial Decision and reviewed the record to evaluate whether cost shifts resulting from implementation of the TAC proposal were significant enough to warrant a cap, and determined that abrupt costs shifts have occurred and will continue to occur throughout

[17] *Id*. at 4.

[18] Southern Cities Rehearing at 12 and 13.

[19] Vernon Rehearing at 2 and 3.

the transition period. Accordingly, Opinion No. 478 found the ISO-proposed cap to be a reasonable interim mechanism to mitigate these cost shifts. In this order, we will further explain why Opinion No. 478 (1) reverses the presiding judge's ruling in the Initial Decision, (2) found the increased cost to the grid via the TAC methodology warranted a cost shift cap, (3) found the ISO-proposed 32-32-8 cap reasonable, and (4) granted deference to the stakeholder process with regard to the "balancing approach" concept, which was devised to ensure that benefits and burdens for all ratepayers were reasonably imparted. However, we note that most of the parties' claims on rehearing are virtually identical to those raised in the earlier proceeding and, therefore, we will not attempt to revisit arguments (*e.g.*, regarding new versus existing High Voltage transmission facilities) adequately resolved in the Initial Decision and/or Opinion No. 478.

22. First, some parties incorrectly have presumed that the *only* factor used by the Commission in its analysis of the cost shift cap issue was the impact of the increase on the actual cost of transmission. This is not the case. The Commission considered several factors (*e.g.*, whether, pursuant to traditional ratemaking principles, rate shock was evident, record evidence regarding the significance of this rate shock, the factors delineated in the May 2000 Order, and whether imposing a cost shift cap would hinder RTO expansion) before determining that any cap was appropriate.

23. It is important to note that the *only* factor used by the presiding judge in her ruling on cost shifts was the portion of the guidance provided in the May 2000 Order that required the record to *include* data on the overall impact of changes in transmission costs (i.e., how *all* ratepayers are affected by these changes) on the overall cost of electricity. Because the Initial Decision was contrary to long-standing Commission precedent in this regard – by considering only the rate impact to the total delivered energy costs – we were compelled to analyze the portion of the record rejected by the presiding judge as "beyond the scope of the proceeding." This evidence was considered along with the evidence highlighted in the Initial Decision that determined the cost shift to be a *de minimis* increase as compared to the total cost of electricity, which is logical because, traditionally, the cost of transmission is relatively small as compared to the total cost of delivered energy. Nevertheless, both of these components were necessary in evaluating the impact of the cost shift on both sets of ratepayers of the original and new Participating TOs. We further note that comparison of the rate impact as it relates to both of these sets of ratepayers constitutes the "balancing" consideration the Commission refers to in Opinion No. 478.

24. Accordingly, Opinion No. 478 relied on record evidence in this proceeding ignored by the presiding judge that certain ratepayers will bear increases of twenty to fifty percent in High Voltage Access Charges over the costs that they would otherwise pay for transmission under utility-specific rates if the TAC proposal is approved without

imposing cost shift caps.[20] We further emphasized that "SoCal Edison's witness Cullier concluded in his cross-answering testimony that seventy to eighty percent of the new Participating TOs' High Voltage transmission costs are being paid by the original Participating TOs and, therefore, the original Participating TOs must collect eleven to sixteen percent in higher rates from their own retail ratepayers."[21] Even Trial Staff Witness Patterson, who recommended the elimination of the cost shift cap on a prospective basis, conceded that the effect of this increase on just the transmission component of rates is significant.[22] Thus, we affirm our conclusion in Opinion No. 478 that some cost shift cap was indeed warranted for a transition period.

25. Next, the Commission had to decide what cost shift cap level to impose. Some parties claim that the ISO-proposed 32-32-8 level, which was ultimately approved by the Commission in Opinion No. 478, was not agreed to by all parties to the stakeholder process and, therefore, the Commission should not view this amount, along with the proposed package of benefits and burdens, as the product of compromise. We find that the purpose of the stakeholder process is to allow all interested parties the ability to collaborate on market redesign and development issues. According to the record, the ISO Board of Governors approved the TAC proposal by a 16-5-1 vote.[23] While unanimous consent on every issue by the California parties would be ideal, it is highly unlikely and a wholly unreasonable expectation under any stakeholder process.

26. We note, however, that no party to this proceeding has raised any objections here or in the instant proceeding regarding the integrity of the stakeholder process, but only that the minority view was not approved. We believe that the stakeholder process here worked in the manner intended and believe it is appropriate to defer to the cost shift cap level that emanated from this process as a mitigation measure. Moreover, as we explained in Opinion No. 478, selection of a specific dollar cap and accompanying ratio is by its nature inherently arbitrary. Finally, SoCal Edison is correct that our finding that the 32-32-8 cost shift cap is reasonable did not consider the Commission's prior elimination of the "buy-down" provision. The Commission's previous orders and the Commission's findings on various issues in the instant order altered other aspects of the rate design produced by the stakeholder process and, as such, each aspect has been reviewed independently. The fact that we endorse a specific provision from the stakeholder process simply means that, based on the record before us, it was the most reasonable resolution of that particular aspect of the rate design. Thus, we deny SoCal

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[20] Opinion No. 478, 109 FERC ¶ 61,301 at P 66-71.

[21] *Id.* P 66 (citing Ex. SCE-13).

[22] Tr. at 2740.

[23] *See* ISO Governing Board March 22, 2000 Resolution, Docket No. ER00-2019-000.

Edison's request for a downward adjustment of the rate cap in light of our previous elimination of the "buy-down" provision.

27. The Commission denies rehearing with respect to SoCal Edison's alternate 20-20-5 cap proposal. As noted by the presiding judge in this proceeding, "Commission precedent provides that [proposals] must first be found to be unjust, unreasonable, or unduly discriminatory before alternative proposals are ripe for consideration."[24] Opinion No. 478 determined, pursuant to traditional ratemaking principles, the existence of rate shock resulting from the original Participating TOs' subsidization of the new Participating TOs via the rate incentives and hold harmless provision granted to the new Participating TOs during the transition period. In prior orders, the Commission has allowed license-plate rates to be implemented under RTO regimes for a fixed term, coupled with certain transition mechanisms to mitigate any abrupt cost shifts that may occur as these entities move towards a postage-stamp rate. Likewise, we find the mitigation measure proposed here, through the stakeholder process, to be a reasonable and appropriate interim method of addressing this concern. Thus, in this instance, the Commission is not required to examine SoCal Edison's alternative proposal.

28. The new Participating TOs argue that they are entitled to full rate recovery and that a cap will deprive them of the opportunity for full TRR recovery. We disagree. The recovery of a new Participating TO's TRR in the presence of a cost shift cap does not lead to under-recovery of the TRR. The cost shift cap is a separate and distinct feature of the rate design. Once the cap in an original Participating TO's TAC area is exceeded, the retail ratepayers of the new Participating TO will contribute through the Transition Charge part of their net benefits received in joining the ISO in order to limit cost shifts.[25] Therefore, we deny rehearing on this issue as we find that new Participating TOs will continue to realize full rate recovery of their TRRs with the presence of a cap.

Phantom Congestion

Opinion No. 478

29. The Commission affirmed the Initial Decision's finding that phantom congestion exists and that it is caused by a disparity between the ISO's scheduling timeline's in the day-ahead and hour-ahead scheduling timelines and the scheduling timelines of existing rights holders. The Commission rejected the theory that the ISO is the cause of phantom congestion, concluding that the ISO is not responsible for problems resulting from the misalignment of the ISO's protocols with the terms and conditions of the previously-existing contracts. Finally, the Commission agreed with the presiding judge that the TAC

[24] Initial Decision 106 FERC ¶ 63,026 at P 346.

[25] *See* Ex. ISO-3 at 47-48.

proceeding is not the appropriate vehicle to remedy the phantom congestion problem, that there are other proceedings in which the problem is more appropriately addressed.

Request for Rehearing

30. Modesto seeks rehearing, stating that Opinion No. 478 accepts at face value the ISO's bald assertion that phantom congestion exists without giving due consideration of substantial factual evidence to the contrary, and requests the further consideration of its arguments. Modesto contends that Opinion No. 478 was arbitrary in finding that Existing Transmission Contracts (ETC) are the cause of phantom congestion. Modesto argues that the ISO deliberately and without apology misaligned its protocols with the terms and conditions of previously existing contracts.

Commission Determination

31. The Commission finds that Modesto's request does not raise any new issues. In Opinion No. 478, the Commission considered Modesto's arguments, but was not persuaded that phantom congestion did not exist. In any event, as we explained in Opinion No. 478, we find that the TAC proceeding is not the appropriate vehicle to remedy the phantom congestion problem, and that there are other proceedings in which the problem is more appropriately addressed. On December 8, 2004, in Docket No. ER02-1656-021, the ISO filed its Market Redesign Technology Upgrade proposal for honoring existing contracts (MRTU proceeding), which defined phantom congestion in terms of the scheduling disparity between the ISO's day-ahead and hour-ahead scheduling timelines and the scheduling timelines of existing rights holders. There, the ISO has conducted an extensive market participant process on ETC-related issues to make the market design function without abrogating existing contracts. This process resulted in an ISO proposal that addresses, among other things, a procedural resolution that overcomes phantom congestion, while continuing to honor the rights under existing contracts.

32. On February 10, 2005, the Commission found that the ISO's proposal fully preserves the ETC holders' scheduling rights.[26] The proposal also makes additional capacity available in the day-ahead and subsequent markets for use by other users of the system, reduces the likelihood and magnitude of phantom congestion, and promotes the convergence of day-ahead and real-time prices. Thus, the problem of phantom congestion is being addressed in the MRTU proceeding and does not have to be addressed here. Accordingly, we deny Modesto's request for rehearing.

[26] *Cal. Indep. Sys. Operator Corp.*, 110 FERC ¶ 61,113 (2005).

Firm Transmission Rights

Opinion No. 478

33. The Commission denied the proposed netting of usage charges against usage charge revenues across all hours, finding the use of FTRs under section 9.4.3 of the ISO Tariff to provide Participating TOs a financial hedge against such usage charges to be just and reasonable.[27] The Commission found that this temporary incentive of allocating "free," unauctioned FTRs, appropriately conveys no financial advantage beyond its particular and limited purpose; namely, to approximate the benefits new Participating TOs held under their existing contracts, not to protect them from all market risk or congestion costs. In fact, the Commission concluded that, under the ISO's proposal, the former use-it-or-lose-it right to capacity under the Existing Transmission Contracts would be replaced by an arguably more advantageous crediting mechanism for unused FTR revenue, under which unused FTRs would be credited to the entity's TRR.

34. The Commission found the termination of the award of such free FTRs under section 9.4.3 of the ISO Tariff at the earlier of the end of the transition period or of an Existing Transmission Contract to be just and reasonable. With regard to the methodology of such allocation, the Commission found section 9.4.3 and section 4.5 of Appendix F, Schedule 3, of the ISO Tariff to provide sufficient detail for the allocation of FTRs to new Participating TOs, with the provision that the ISO file simultaneously with the Commission the amendment to the Transmission Control Agreement regarding each new Participating TO. The Commission affirmed all other findings and conclusions of law of the presiding judge concerning FTRs.

35. The Commission directed the ISO to clarify that ISO Tariff section 9.4.3 does not permit the allocation of section 9.4.3 FTRs to the new Participating TO whose High Voltage transmission facilities were built after becoming a Participating TO, finding that such allocation is inconsistent with the limited purpose of encouraging expansion of the ISO. The Commission also directed amendments to section 7.3.1.6 of the ISO Tariff, with regard to the disbursement of usage charges relating to a jointly-owned interface with an original Participating TO, and to section 7.3.1.7, the definition of Transmission Revenue Credits.

[27] According to the ISO Tariff, the term usage charge is defined as the amount of money per kilowatt of scheduled flow that the ISO charges a Scheduling Coordinator for use of a specific congested inter-zonal interface during a given hour.

Requests for Rehearing

36. DWR contends, in its request for rehearing, that FTRs granted upon contract conversion should be coterminous with the Existing Transmission Contracts upon which they are based; otherwise, DWR would be required to pay both dollars and unique in-kind reliability support for converted contract rights for a four-year period after the ten-year term when its section 9.4.3 FTRs would expire. Moreover, DWR maintains that if it is subject to pure ISO discretion to downgrade its FTRs below the full contract demand amount upon contract conversion, DWR should either be excused from continuing to provide reliability support or such support should be unbundled and compensated.

37. SoCal Edison seeks clarification that the Commission ruling regarding section 9.4.3 FTRs means that no new Participating TO can receive section 9.4.3 FTRs for facilities placed in service after the TAC transition date of January 1, 2001. SoCal Edison states that it believes that the Commission's language in Opinion No. 478 is intended to adopt the position that SoCal Edison has advocated since the inception of this case and adopted by the Initial Decision, that no section 9.4.3 FTRs would be awarded to new Participating TOs for any facilities placed in service after the transition date. Alternatively, SoCal Edison requests rehearing, contending that an approach that would provide section 9.4.3 FTRs for facilities constructed by non-Participating TOs after January 1, 2001, would only discourage potential new Participating TOs that are considering construction of transmission facilities from joining the ISO until after such facilities were built. According to SoCal Edison, there is no evidence supporting this approach reflected in the literal words of Opinion No. 478, nor did any party in the proceeding below support such an approach.

Commission Determination

38. The Commission denies rehearing with respect to DWR's contention that FTRs granted upon contract conversion should be coterminous with the Existing Transmission Contracts. We previously found it reasonable that FTRs be limited to the lesser of the ten-year transition period or the life of the contract if its term is less than ten years. We recognized the importance of the provision of free, unauctioned FTRs as a temporary incentive, but stated that the disparate treatment of original and new Participating TOs eventually should end. We further stated that such new Participating TOs must ultimately participate in the same FTR auction process as the original Participating TOs.

39. The termination of the award of section 9.4.3 FTRs at the earlier of the end of the transition period or of an Existing Transmission Contract is reasonable in order to ensure finality in the rate design. Once these periods end, the playing field would be level among Participating TOs. We note that DWR has provided no further evidence to persuade the Commission to modify the limited purpose of section 9.4.3 of the ISO Tariff. Therefore, we deny rehearing.

40. We also deny on rehearing DWR's contention either that it be excused from continuing to provide reliability support under its existing contracts with PG&E or that such support be unbundled and compensated if DWR becomes a Participating TO. We continue to find this issue premature because, at this time, DWR has not made a commitment to become a Participating TO.

41. We deny SoCal Edison's request for rehearing on the issue of whether FTRs should be allocated for facilities that were placed in service after January 1, 2001. We clarify that the ISO Tariff provides that a new Participating TO will receive FTRs commensurate with the transmission capacity that it places under the ISO's operational control at the time it becomes a Participating TO. We find this standard is reasonable because it fully represents the intent of the ISO, which is to encourage market participants to transfer operational control of their facilities to the ISO. We believe that SoCal Edison's request to establish January 1, 2001, as the date by which existing facilities must be in place will have an adverse effect on potential Participating TOs with regard to joining the ISO, because they would be precluded from receiving FTRs associated with their planned investments of transmission capacity placed in service after January 1, 2001, at the time that they joined the ISO. We also note that the process of planning, construction, and placing of such facilities in service requires a significant amount of time, and could not readily be deliberately timed in order to receive FTRs under section 9.4.3. Thus, we deny rehearing.

High-Low Split Methodology Implementation

Opinion No. 478

42. In Opinion No. 478, the Commission noted that the Initial Decision failed to address PG&E's proposal for the appropriate division of the Transmission Revenue Balancing Account between High and Low Voltage TRRs and directed the ISO to file revised tariff sheets that reflect PG&E's proposal.

43. Additionally, the Commission affirmed the Initial Decision with respect to several issues. First, the Commission affirmed the allocation of system interconnections, concluding that system interconnections below 200kV should be included in a Participating TO's Low Voltage TRR and system interconnections 200kV and above should be included in a Participating TO's High Voltage TRR. Second, the Commission affirmed the presiding judge's finding that the ISO's procedures for the division of costs between High and Low transmission charges must be included in the ISO Tariff. Finally, the Commission affirmed the Initial Decision with respect to the proper allocation of costs for substations and substation equipment. Specifically, the ISO had originally proposed that the division of costs for substations and substation equipment (except step-down transformers) would adhere to a three-step test and that step-down transformers would be allocated on a 50/50 basis. In this regard, the Initial Decision, as affirmed by

the Commission in Opinion No. 478, stated that where there is insufficient information available to allocate step-down transformer costs between High Voltage TRR and Low Voltage TRR, these costs should be allocated in the same manner as other substation facilities.

Request for Rehearing

44. SoCal Edison seeks clarification that in adopting a different methodology for differentiating certain High Voltage facilities from Low Voltage facilities, the Commission did not intend that such new split methodology be applied retroactively, or applied to any specific, existing Participating TO prior to the filing of such Participating TO's next base TRR rate case. SoCal Edison states that the Commission does not address the timing of the implementation of the new split methodology, nor did the Commission order any refunds or surcharges, which it would have, had it intended the new split methodology to have retroactive effect. SoCal Edison concludes that the Commission failure to issue such orders reflects an intention that the new split methodology is to have prospective effect only.

45. If the Commission intended for the new split methodology to become effective retroactively, SoCal Edison seeks rehearing of that decision. SoCal Edison argues that it is the Commission's policy not to alter transmission rate design on a retroactive basis, as rate design changes cause the need for both refunds and surcharges. SoCal Edison states that the change in split methodology would require Participating TOs to reallocate costs between their High and Low Voltage TRRs, which in turn would trigger several resettings of the ISO's Access Charges and Wheeling Access Charges. SoCal Edison also states that the administrative burden of resetting such rates would drive up ISO costs and impose an undue burden and cost on all of the Participating TOs. SoCal Edison concludes that the appropriate and reasonable time for a Participating TO to apply the new split methodology is when a Participating TO files its next TRR rate case.

Commission Determination

46. The Commission clarifies that the new split methodology should be made effective prospectively. In the Initial Decision, the presiding judge concluded that the revised allocation be applied prospectively and no parties filed exceptions to this aspect of judge's decision. Thus, Opinion No. 478 affirmed the judge on this issue without discussion.

47. We therefore will require any new Participating TO to follow the new split methodology when it files its initial TRR filing as a result of joining the ISO. Additionally, we will require any existing Participating TO to recalculate its High and Low Voltage TRRs using the new split methodology when that Participating TO submits

its next base TRR rate case.[28] Because the Commission has thus clarified its decision, SoCal Edison's alternative request for rehearing is moot.

Behind the Meter Exception to Allocation on a Gross Load Basis

Opinion No. 478

48. In the July 2003 Order, the Commission established an exception to the ISO's proposal to allocate the TAC on a gross load basis for behind the meter generation,[29] reflecting a similar exception established in Opinion No. 463 for the ISO's Grid Management Charge.[30] Several parties requested rehearing of the July 2003 Order on this issue. In Opinion No. 478, the Commission noted that, since the rehearing requests had been filed, there had been several developments with respect to the Grid Management Charge exception to gross load allocation. First, in Opinion No. 463-A,[31] the Commission had revisited the issue and established an exception to gross load for behind the meter generation based on a different concept than the one we had previously approved in Opinion No. 463. Second, we explained that, upon consideration of the rehearing requests of Opinion No. 463-A concerning this issue, we had determined that the record in the Grid Management Charge proceeding was insufficient to reach a decision on the issue, and set the matter for an expedited hearing.[32]

49. Turning to the behind the meter gross load exception established by the July 2003 Order, Opinion No. 478 went on to state:

> We believe that the issue of whether the behind the meter exception that we have applied to the Control Area Services portion of the Grid Management Charge, by means of which the ISO collects its administrative costs, is appropriate in the context of the TAC, a transmission charge designed to collect the embedded transmission costs of the ISO-controlled grid, requires further analysis. In view of the ongoing hearing on the issue in the GMC

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[28] We will not require the Participating TO to follow the new split methodology when it makes its annual Transmission Revenue Balancing Account adjustment which updates the TRR. This is a ministerial filing that leaves the base TRR unchanged from its previously filed level.

[29] July 2003 Order, 104 FERC ¶ 61,062 at P 55.

[30] *Cal. Indep. Sys. Operator Corp.*, 103 FERC ¶ 61,114 (2003).

[31] *Cal. Indep. Sys. Operator Corp.*, 106 FERC ¶ 61,032 (2004).

[32] *Cal. Indep. Sys. Operator Corp.*, 109 FERC ¶ 61,162 (2004). On April 15, 2005, an Initial Decision was issued in response to the remand. *Cal. Indep. Sys. Operator Corp.*, 111 FERC ¶ 63,008 (2005).

> case, the Commission has decided to defer decision on the gross load exception issue here pending our review of the record compiled in that proceeding.[33]

Request for Rehearing

50. Silicon Valley Power requests clarification, or, in the alternative, rehearing on this issue. Silicon Valley Power does not disagree with defering the decision on the gross load exception in this proceeding pending the Commission's determination concerning the gross load exception issue in the Grid Management Charge proceeding. However, Silicon Valley Power seeks clarification that, in deferring the decision here, "the Commission did not intend to pre-judge the outcome of the gross load exception in the TAC proceeding" based on the eventual outcome of the Grid Management Charge case.[34]

51. Silicon Valley Power goes on to set out what it believes are a number of distinctions between the Grid Management Charge and the TAC which would preclude "automatically" applying the result in the former case to this one.[35] Thus, Silicon Valley Power "urges the Commission" to "allow for public comment and evidentiary submittals, if appropriate," prior to applying a gross load exception established for the Grid Management Charge to the TAC.[36]

52. Alternatively, Silicon Valley Power requests rehearing if the Commission did intend to have the outcome of the Grid Management Charge proceeding apply to the TAC without further opportunity for public comment.

Commission Determination

53. The Commission grants Silicon Valley Power's request for clarification. We do not intend to "automatically" apply whatever result we reach in the Grid Management Charge proceeding to the TAC without further evaluation, and, if appropriate, an opportunity for comment by the parties. Silicon Valley Power's alternate request for rehearing is, therefore, dismissed as moot.

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[33] Opinion No. 478, 109 FERC ¶ 61,301 at P 103.

[34] Silicon Valley Power Request for Clarification or Rehearing at 6.

[35] *Id.* at 7.

[36] *Id.*

Justness and Reasonableness of the TAC

Opinion No. 478

54. In Opinion No. 478, the Commission summarily affirmed the Initial Decision's determination of what factors should be considered in evaluating whether the ISO's TAC was just, reasonable, and not unduly discriminatory.[37] We further summarily affirmed the judge's related rejection of the time-of-use rate design proposed by DWR and SWC/Metropolitan, as well as certain accompanying evidentiary determinations. Because DWR and SWC/Metropolitan dispute on rehearing our resolution of these issues, we set out the Initial Decision's conclusions with respect to these matters.

55. In determining whether the ISO's TAC proposal was just and reasonable, the Initial Decision first examined the factors that should be employed to evaluate the proposal. The judge began by explaining that her decision on this issue would "be guided by Commission policy and precedent," including the Commission's Transmission Pricing Policy Statement, general cost causation principles, and the May 2000 Order, which set this matter for hearing.[38] In the May 2000 Order, the judge observed, the Commission had endorsed the "ISO's objectives of creating an equitable balance of costs and benefits among the various affected classes of stakeholders and the treatment of all Participating TOs on the same basis," the goal of a uniform grid-wide high voltage rate, and incentives for new Participating TOs.[39]

56. While these factors supplied the analytical framework for her decision, the judge explained, the FPA provided statutory framework for her evaluation of the justness and reasonableness of the TAC. While a utility proposing a rate increase has the burden of proof under section 205(e) of the FPA, she explained, once "a utility's method of cost estimation [is found] to be reasonable," the parties challenging the method bear the burden of coming forward with contrary evidence.[40] "For the rate design proposal to be

[37] Opinion No. 478, 109 FERC ¶ 61,301 at P 11.

[38] Initial Decision, 106 FERC ¶ 63,026 at P 53. *See Inquiry Concerning the Commission's Pricing Policy for Transmission Service Provided by Public Utilities Under the Federal Power Act, Policy Statement*, 59 Fed. Reg. 55,031 (Nov. 3, 1994), FERC Stats. & Regs. ¶ 31,005 (1994), *order on reconsideration*, 71 FERC ¶ 61,195 (1995).

[39] *Id.* P 54 (quoting May 2000 Order, 91 FERC at 61,722).

[40] *Id.* P 56 (citing *Pub. Serv. Co. of Ind., Inc.*, 56 FPC 3003, 3017-18 (1976), *reh'g granted in part*, 57 FPC 1173 (1977) (footnote omitted).

acceptable," the judge explained, "it need be neither perfect nor even the most 'desirable'; it need only be reasonable."[41]

57. Applying these standards to the ISO's TAC rate proposal, the Initial Decision concluded that because the Commission had in fact approved the proposed rate design,

> the ISO's proposed TAC must be found to be unjust, unreasonable, or unduly discriminatory before alternative proposals are ripe for consideration. Further, if a party wishes to challenge a feature of the TAC that is unchanged from the previous rate that the Commission has approved as just and reasonable, then that party bears the burden of coming forward with evidence sufficient to establish that the feature in question is unjust or unreasonable.[[42]]

58. Because the flat MWh-based TAC was unchanged by the ISO's Amendments 27 and 49 to its tariff, the judge concluded that it had already been found just and reasonable by the Commission in its 1997 Order approving the original TAC.[43] The judge therefore rejected SWC/Metropolitan's argument that the flat MWh-based TAC did not conform to the Commission's Transmission Pricing Policy Statement, as the Commission had already held that the ISO's flat MWh-based rate design conformed to the policy.[44] The judge went on to reject DWR's claim that the ISO bore the burden of proof that its proposal was just and reasonable without employing time-of-use rates.

59. The Initial Decision reiterated these findings in its Summary and Conclusion sections.[45]

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[41] *Id.* P 57 (citing *New England Power Co.*, 52 FERC ¶ 61,090, at 61,336 (1990), *reh'g denied*, 54 FERC ¶ 61,055 (1992), *aff'd sub nom. Town of Norwood v. FERC*, 962 F.2d 20 (D.C. Cir. 1992); *City of Bethany v. FERC*, 727 F.2d 1131, 1136 (D.C. Cir. 1984), *cert. denied*, 469 U.S. 917 (1984); *OXY USA, Inc. v. FERC*, 64 F.3d 679, 692 (D.C. Cir. 1995)).

[42] *Id.* P 58 (citing *Pub. Serv. Comm'n of N.Y. v. FERC*, 642 F.2d 1335, 1345 (D.C. Cir. 1980)).

[43] *Pacific Gas & Elec. Co.*, 80 FERC ¶ 61,128 (1997) (*Guidance Order*).

[44] Initial Decision, 106 FERC ¶ 63,206 at P 58 (citing *Guidance Order*, 80 FERC ¶ 61,128).

[45] *Id.* P 380-82.

Requests for Rehearing

60. On rehearing, DWR argues that the Commission's summary affirmance of the Initial Decision on this issue is arbitrary because it ignores that the May 2000 Order "specifically set for hearing the question of time sensitive rates," as well as what DWR sees as the ISO's commitment "to establish a new rate methodology based on principles which include off-peak transmission rates."[46] In this regard, DWR believes that the Commission erroneously relieved the ISO of the burden of proof with respect to its proposed TAC: "This is the first filing by the ISO to establish ISO-wide rates, and therefore is *the* filing in which the ISO must justify its rates, including addressing the issue of time-sensitive rates."[47]

61. With respect to the judge's holding that the Commission had previously approved the ISO's flat pricing methodology, DWR argues that the Commission's prior approval of the ISO's rate design in the *Guidance Order* was not precedential with respect to time-of-use rates, as the rate design was "only interim and subject to change."[48]

62. DWR next argues that the Commission's rejection of time-sensitive rates violates cost causation principles. In this context, DWR maintains that the result here cannot be reconciled with the judicial mandate of *Union Electric Co. v. FERC (Union Electric)*,[49] which held that "a FERC approved rate methodology is not reasonable if it fails to differentiate cost-causation and thus pricing between on-peak and off-peak transmission users."[50] As DWR goes on to assert:

> It is well established that the need for transmission investment, which is the primary cost component in transmission rates, is driven by peak system usage, and that, accordingly, off-peak users should bear only those costs immediately attributable to off-peak usage.[[51]]

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[46] DWR Request for Rehearing at 5-6 (citing May 2000 Order, 91 FERC at 61,729; Former ISO Tariff § 7.1.6).

[47] *Id.* at 9 (emphasis in original).

[48] *Id.* at 7.

[49] 890 F.2d 1193, 1198 (D.C. Cir. 1989).

[50] DWR Request for Rehearing at 8 (footnote omitted).

[51] *Id.* at 10.

Furthermore, DWR alleges, "Commission decisions apply the rule that 'customers using . . . transmission off-peak hours do not constrict the system during the critical load and should pay less.'"[52]

63. DWR goes on to argue that the Commission's failure to adopt time-sensitive rates is not supported by substantial evidence. DWR maintains that it put forth "[i]ndisputable evidence in the hearing support[ing] the well-recognized concept of time-differentiated rates in the context of the ISO's system."[53] DWR attacks the ISO's position that its congestion charges provide a reasonable substitute for time-sensitive rates, because that charge "is not designed to, and cannot, address the fundamental problem itself, i.e., establishing price signals that result directly in lowered long-term demand on the electric grid."[54] Furthermore, DWR contends, congestion pricing "does nothing to properly distribute or allocate network costs under the principles of cost causation."[55]

64. The evidence in the record, DWR believes, supports either the modified *Appalachian* rate design method,[56] or, alternatively, the traditional 12-coincident peak (12-CP) methodology.[57]

65. SWC/Metropolitan makes similar arguments in its request for rehearing of this issue. SWC/Metropolitan asserts that the Initial Decision "failed to articulate a reasoned basis for rejecting the evidence and argument against" the ISO's proposed flat MWh-based rate design.[58]

66. Like DWR, SWC/Metropolitan objects to the Initial Decision relying on the *Guidance Order* to establish the justness and reasonableness of the ISO's proposal. Indeed, SWC/Metropolitan's position is that the judge and the Commission failed to recognize that time-sensitive rates were properly at issue in this proceeding. In this regard, SWC/Metropolitan observes that because the ISO proposed "a quantum change in the overall rate design of its TAC in this proceeding, from a utility-specific to a uniform,

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[52] *Id.* at 12 (quoting *Am. Elec. Power Serv. Corp.*, Opinion No. 440, 88 FERC ¶ 61,141, at 61,453-54 (1999)).

[53] *Id.* In this regard, DWR primarily relies on Ex. SWP-65 and Ex. SWP-67.

[54] *Id.* at 14.

[55] *Id.* (citing Ex. SWC-1; Ex. SWC-24).

[56] *Id.* at 17 (citing *Appalachian Power Co.*, 39 FERC ¶ 61,296 (1987)).

[57] *Id.* at 18 (citing Ex. SWC-1 at 60-71).

[58] SWC/Metropolitan Request for Rehearing at 15.

ISO-wide rate," the *Guidance Order* could not preclude consideration of time-sensitive rates here.[59]

67. Additionally, SWC/Metropolitan contends that the Commission has recognized that the ISO's intra-zonal congestion management system, one of the components of congestion management the Commission relied upon in the *Guidance Order* approving the original, interim TAC as just and reasonable, is seriously flawed.[60] In support of its view that the time-sensitive rates should have been fully considered in this case, SWC/Metropolitan also relies on the ISO's consideration of demand-based rates in the development of its TAC proposal,[61] as well specific language in the May 2000 Order to this effect.[62]

68. SWC/Metropolitan next outlines in some detail the basis for its argument that the ISO's proposed rate design is unjust and unreasonable, the argument that it contends was ignored by the presiding judge. On this issue, SWC/Metropolitan emphasizes evidence it presented that the ISO's proposal was inconsistent with the Commission's established transmission pricing principles, particularly that transmission pricing should provide more efficient price signals, and not simply reallocate sunk costs.[63] SWC/Metropolitan further relies on judicial precedent that it believes mandate Commission adherence to the principle "that a utility's revenue requirement be allocated among its customers in a manner appropriately reflecting the cost to provide service to that class of customers."[64]

69. SWC/Metropolitan attacks the "scant" evidence introduced by the ISO to support its proposed volumetric TAC as erroneously relying on "intended market structure."[65] SWC/Metropolitan further explains:

> Since the Commission allocates costs based on cost-causation, the ISO's position that its intended market structure justified its proposed volumetric allocation methodology is not supported by Commission precedent or practice. The evidence SWC/[Metropolitan] and [DWR] amassed in this

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[59] *Id.* at 21-22.

[60] *Id.* at 21 (citing *Cal. Indep. Sys. Operator Corp.*, 90 FERC ¶ 61,006, at 61,013-14 (2000); Ex. SWC-1 at 35).

[61] *Id.* at 24-27.

[62] *Id.* at 28-31 (citing May 2000 Order, 91 FERC at 61,722, 61,729).

[63] *Id.* at 31-36 (citing Ex. SWC-4 at 9-10; Ex. SWC-21 at 4).

[64] *Id.* at 38 (citing *Union Electric*, 890 F.2d at 1198; *Ala. Elec. Coop. v. FERC*, 684 F.2d 20, 27-28 (D.C. Cir. 1982)).

[65] *Id.* at 39-40.

> proceeding conclusively demonstrates new transmission costs are incurred to serve growth in peak load. To adhere to principles of cost-causation, the allocation methodology must account for the load that causes new transmission to be built.[[66]]

SWC/Metropolitan goes on to describe its evidence that new transmission costs are generally incurred to serve peak load, regardless of off-peak congestion, and that "on peak load is the primary driver of investment in new transmission."[67] On the other hand, SWC/Metropolitan maintains congestion charges provide short-term, rather than more significant long-term, prices signals.

70. SWC/Metropolitan also argues that general principles of cost causation militate against a flat MWh-based rate, as the ISO uses system peak for transmission planning, and reliability and expansion of the ISO grid are driven by peak demand.[68] In spite of this, SWC/Metropolitan contends, under the TAC, "off-peak users pay the same MWh rate as on-peak users," a result which "has been firmly rejected by reviewing courts."[69]

71. SWC/Metropolitan asserts that a 12CP demand-based rate would be just and reasonable under the circumstances.

Commission Determination

72. The Commission denies the requests for rehearing filed by DWR and SWC/Metropolitan. At the outset, we reject the notion put forth by these parties that they were in any manner deprived of the opportunity to litigate their time-of-use rate proposals. DWR in particular introduced a significant amount of evidence in support of its time-of-use rate proposal. Indeed, neither DWR nor SWP/Metropolitan alleges that the presiding judge excluded any evidence introduced by them on this issue. Rather, the gravamen of their complaint is that the judge failed to consider the evidence they presented.

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[66] *Id.* at 40.

[67] *Id.* at 41 (citing Ex. SWC-1 at 26-27).

[68] *Id.* at 43-45. SWC/Metropolitan's evidentiary support for these contentions is primarily Ex. SWC-1 and Ex. SWC-24.

[69] *Id.* at 46-47 (citing *La. Pub. Serv. Comm'n v. FERC*, 184 F.3d 892 (D.C. Cir. 1999) (*Louisiana Public Service*); *Elec. Consumers Res. Council v. FERC*, 747 F.2d 1511 (D.C. Cir. 1984) (*ELCON*)).

73. In our view, the Initial Decision specifically indicates that the judge carefully considered the evidence and arguments on this issue propounded by both parties.[70] However, she rejected their claim on the merits, finding that the evidence they propounded was not sufficient to meet their burden to demonstrate that the ISO's flat dollar per MWh rate was not just and reasonable. Thus, the judge acted consistently with the May 2000 Order's requirement that time-of-use rates be considered in this proceeding.

74. On the burden of proof issue, we hold that the Initial Decision correctly applied the applicable legal principles. The ISO originally proposed a volumetric megawatt-hour-based charge, combined with a congestion charge, in 1997. In the *Guidance Order*, the Commission found that this rate design was just and reasonable and in compliance with our transmission pricing principles.[71] The new TAC proposal filed by the ISO as Amendments 27 and 34 to the ISO Tariff did not change this aspect of the TAC rate design. Rather, the new aspects of the proposed TAC at issue here were rolling the costs of the facilities of the various Participating TOs into one rate, and the High Voltage/Low Voltage split. And contrary to the contention of DWR, this rate design approved by the *Guidance Order* was the ISO's filed rate, encompassing the full legal effect of such a rate, regardless of whether the parties considered it "interim" or "subject to change" at a later date.

75. It is firmly established that the burden of proof lies with the party proposing a change from a rate design that is already part of a filed rate.[72] Thus, the judge appropriately determined that the DWR and SWC/Metropolitan had the burden of proof to show that the ISO's volumetric rate with a congestion charge was not just and reasonable.

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[70] *See* Initial Decision, 106 FERC ¶ 63,026 at P 292-316. Similarly, the ISO considered the use of time sensitive rates in developing the TAC, which was the extent of its obligation on this issue.

[71] *Guidance Order*, 80 FERC at 61,429. *See also Pacific Gas & Elec. Co.*, 81 FERC ¶ 61,122, at 61,459 (1997) (reiterating that the ISO's methodology sends appropriate price signals with respect to existing and future generation, transmission expansion and consumption).

[72] *See, e.g., Algonquin Gas Transmission Co. v. FERC*, 948 F.2d 1305 (D.C. Cir. 1991); *Sea Robin Pipeline Co. v. FERC*, 795 F.2d 182, 187 (D.C. Cir. 1986); *Williams Natural Gas Co.*, 77 FERC ¶ 61,277, at 62,209 & n.250 (1996). While these cases happen to arise under the Natural Gas Act, the analogous terms of the FPA are interpreted identically. *E.g., Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

76. We agree, however, that the Initial Decision's analysis in support of her approval of the ISO's TAC proposal was conclusory. The Commission will address *de novo*, therefore, DWR's and SWC/Metropolitan's contentions that the TAC proposal was not just and reasonable.

77. In order to address the parties' arguments, we first reiterate our rationale in the *Guidance Order* supporting our original finding that the ISO's volumetric rate design with congestion charges was just and reasonable. There, we stated that the ISO's proposal's features were "necessary to achieve two important objectives"; namely, that it "efficiently rations constrained transmission capacity" while providing for the recovery of each Participating TO's revenue requirement.[73] We went on to describe the proposal in these terms:

> All customers using the ISO Grid will be charged only a single stand-alone transmission utility access charge, and, if applicable, a congestion usage charge. The pricing being proposed . . . is intended to reduce the price of transmission over multiple utility systems in unconstrained situations and to rely on congestion charges to provide a uniform price signal to all users of a given transmission interface.[74]

78. The *Guidance Order* expressly measured the ISO's proposal against the Commission's Transmission Pricing Policy Statement, concluding that the proposal was fully consistent with the principles expressed therein. Of particular significance here is the Commission's discussion of the economic significance of the congestion charge:

> We agree that the congestion usage charge sends the proper price signals regarding the opportunity costs of using congested transmission paths. The usage charge will encourage efficient usage of the transmission system and facilitate the development of a competitive electricity market. By efficiently pricing the use of constrained transmission capacity, the ISO's proposed usage charge will also send the proper price signals for the location and dispatch of existing and new generating resources. To the extent generation located on the high cost (import) side of a constraint is priced higher as a result of congestion usage charges, generation that would otherwise be more expensive but for the usage charges will be dispatched first. Therefore, new load will have an incentive to locate on the low cost (export) side of the constraint, and new generation will have an incentive to locate on the high cost (import) side of the constraint. Moreover, the ISO's

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[73] *Guidance Order*, 80 FERC at 61,429.

[74] *Id.* at 61,430.

> proposed congestion usage charge is also likely to encourage efficient expansion of the transmission system. For example, to the extent that, over time, congestion usage charges are higher than the cost to expand constrained transmission capacity, transmission customers will have an incentive to expand the transmission system.[[75]]

79. Against this background, the Commission addresses the contentions raised by DWR and SWC/Metropolitan. Essentially, DWR argues that time-sensitive pricing is required because peak demand drives transmission expansion. However, as ISO witness Mr. Pfeiffenberger explained in some detail, peak end-use load (the measure of on-peak/off-peak pricing) on the ISO's system does not necessarily produce the most transmission use and the most congestion. Rather, lines are actually sometimes more congested during off-peak hours.[76] Moreover, the ISO presented evidence that it considers off-peak as well as peak conditions in transmission planning, and that congestion which causes transmission expansion occurs both in off-peak as well as peak periods.[77]

80. With respect to price signals, there is evidence in the record that the TAC is designed to recover those portions of the TRRs not paid for by congestion charges and FTR auction revenues, not to provide price signals in and of itself.[78] Rather, it is the ISO's congestion pricing mechanism that primarily provides price signals. Contrary to the assertions of DWR and SWC/Metropolitan, there is also evidence that congestion pricing does fulfill this function, as we recognized in the *Guidance Order*.[79]

81. We also find that the evidence introduced by the parties supporting time-of-use rates fails to establish that this rate design would be just and reasonable for the ISO's TAC. As the testimony of SWC/Metropolitan's witness Mr. Russell relates, DWR, which operates a large water transportation and storage system in California, has designed its pumping system to operate so that the great majority of its generation and transmission use occurs during the off-peak hours.[80] He also explains that SWC/Metropolitan is DWR's largest customer, paying between 60 and 80 percent of

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[75] *Id.* at 61,429.

[76] Ex. ISO-36 at 7-11; Ex. ISO-37; Ex. ISO-43-46; Tr. 909-11, 1000-02.

[77] Ex. ISO-36 at 6-11.

[78] *Id.* at 14.

[79] *Id.*; Ex. SCE-29 at 23. As SWC/Metropolitan indicates, changes are being made to improve the ISO's congestion pricing in another proceeding before the Commission. This does not affect our premise here.

[80] Ex. SWC-1 at 5.

DWR's energy and transmission costs.[81] Thus, it is hardly surprising that these parties advocate a rate design pursuant to which their financial liability would be extremely limited. Nor is it surprising that because none of the numerous intervenors in this proceeding have a similar system, that none of them supported DWR's and SWC/Metropolitan's time-of-use rate proposals.

82. There was also evidence presented that DWR's and SWC/Metropolitan's proposals would have an even more severe impact on other ISO customers than that inherent in the scheme of the rate design. In what appears to be unrebutted testimony, PG&E's witness Mr. Kozlowski explained that if the ISO adopted time-sensitive rates, it would require a significant change in how its transmission rates are currently developed and allocated. Thus, these proposals

> would require a large number of market participants to incur significant expense in modifying their scheduling and settlement systems. Moreover, new metering would be required for millions of end-users served by the ISO Controlled Grid to implement the [DWR] and [SWC/Metropolitan] proposals.[[82]]

83. That DWR and SWC/Metropolitan would be the sole beneficiaries of their rate design proposals and that their proposals would add significant additional costs to most other market participants pose considerable stumbling blocks to these proposals being approved by the Commission as just and reasonable for the ISO TAC.

84. In sum, the Commission finds that, based on our review of the evidence in the record and applicable precedent, the ISO's TAC rate design is just and reasonable, and not unduly discriminatory, and that the opposing parties have not met their burden of showing otherwise.

85. We further reject the contention that this result is inconsistent with relevant precedent concerning cost causation. While the parties believe that the court's decision in *Union Electric* found that a rate methodology is not reasonable if it fails to differentiate cost-causation and thus pricing between on-peak and off-peak users, this claim does not survive scrutiny of the actual holding of the case. In *Union Electric*, which involved generation rather than transmission rates, the Commission "had sought to impose a higher portion of fixed costs on off-peak users by adopting a new billing form for the demand charge."[83] This resulted, the court explained, in a charge "solely on users

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[81] *Id.* at 4.

[82] PG&E Brief Opposing Exceptions at 7 (citing Ex. PGE-5 at 8-9) (footnotes omitted).

[83] *Union Electric*, 890 F.2d at 1199.

whose off-peak consumption is high relative to their peak use," a deviation from prior Commission practice upon which the complaining generation customers had relied.[84] *Union Electric*, then, can hardly be read to demand time-sensitive transmission rates in all circumstances.

86. The other judicial precedent on which the parties rely is no more persuasive. In *Louisiana Public Service*, the court reviewed the dismissal of a complaint by the Commission. Accepting for purposes of the decision that all of the complainant's factual allegations were true, the court held that it was arbitrary for the Commission to permit assessment of capacity charges for interruptible service when there was no evidence that such service caused the addition of new capacity. The court's conclusion was based on the economic theory, recognized by the Commission, that capacity costs "are assessed to the peak-period users because it is peak demand that determines how much a utility will invest in capacity."[85]

87. In the present case, however, as we describe below, there was specific evidence that peak use did not determine investment in capacity. Indeed, in *ELCON*, also relied on by SWC/Metropolitan, the court specifically admonished that "mere economic theory may not take the place of record evidence and reasoned decision-making."[86]

88. In short, precedent does not require that off-peak users may never pay the same MWh rate as on-peak users under any circumstances. In view of the record evidence discussed above, the Commission finds that the ISO's TAC rate design is not inconsistent with general principles of cost causation.

Partial Initial Decision and Motion to Reopen the Record

Opinion No. 478

89. In Opinion No. 478, the Commission affirmed a Partial Initial Decision issued by the presiding judge, which held that the ISO's Tariff was not required to contain a clear description of the ISO's standards and criteria to determine whether facilities would be accepted for ISO operational control, and thus be included in the TAC rates.

[84] *Id.*

[85] 184 F.3d at 895 (quoting *Union Elec. Co. v. FERC*, 890 F.2d 1193, 1198 (D.C. Cir. 1989)).

[86] 747 F.2d at 1517.

90. The Partial Initial Decision had relied on Opinion No. 466, the result of which was subsequently changed on rehearing.[87] Specifically, while Opinion No. 466 held that any facilities turned over to the ISO's operational control should be included in the ISO's TAC rates, Opinion No. 466-A concluded that the decision of whether the facilities should be turned over to the ISO's operational control would, rather, be based on whether the facilities would be used for transmission. Based on this modification, DWR filed with the Commission a motion to reopen the record on this issue.

91. The Commission affirmed the Partial Initial Decision on two grounds: First, we observed that the issue here was whether the ISO's proposed amendments to its tariff concerning the TAC were just and reasonable. "However," we explained, "the ISO's policy with respect to which facilities it should operate is primarily addressed in its Transmission Control Agreement, which is not at issue here."[88] Second, we concluded, the question of which facilities should be included in the Participating TO's TRRs (and thus be an element of the TAC) "should be and is being decided in their individual TRR proceedings."[89]

92. Opinion No. 478 went on to reject DWR's motion. Since the judge correctly found that the issue raised by DWR was not relevant to this proceeding, the Commission reasoned, it made no difference that she reached this result by relying on a Commission order that we subsequently overturned.

Request for Rehearing

93. DWR requests rehearing on both of these determinations. DWR emphasizes, as it did in its brief on exceptions, that "the *sole* precedent upon which the Partial [Initial Decision] rested was Opinion No. 466."[90] As the Commission itself acknowledged, DWR observes, Opinion No. 466 erroneously failed to distinguish ISO operational control from ratemaking treatment.

94. DWR goes on to argue that the Commission ignored evidence presented by DWR with "concrete recommendations" on how the ISO Tariff "can be refined" to address

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[87] *Pacific Gas & Elec. Co.*, Opinion No. 466, 104 FERC ¶ 61,226 (2003), *reh'g granted*, Opinion No. 466-A, 106 FERC ¶ 61,144, *reh'g denied*, Opinion No. 466-B, 108 FERC ¶ 61,297 (2004), *appeal pending sub nom. Cal. Dep't of Water Res. v. FERC*, No. 04-76131 (9th Cir. Nov. 22, 2004).

[88] Opinion No. 478, 109 FERC ¶ 61,301 at P 87.

[89] *Id.* P 88.

[90] DWR Request for Rehearing at 34 (emphasis in original; footnote omitted).

which facilities should be placed under its operational control, as well as endorsed the judge's error in failing to permit more evidence to be presented on the matter.[91]

95. With respect to its motion to reopen the record, DWR maintains that the Commission failed to apply the proper standards governing reopening of the administrative record, which permit such reopening when there is a change in governing law, as there was here. In this regard, DWR believes that evidence introduced in the ongoing proceedings of *City of Vernon, California*, Docket No. EL00-105 (*Vernon*), and *City of Anaheim, California, et al.*, Docket No. EL03-15, *et al.* (*Anaheim)*, reveals "the ISO's level of control, or lack thereof, over facilities transferred to it."[92] Deciding the issue in the instant proceeding, DWR contends, would prevent the parties from having "to litigate [and] relitigate[] in order to expose the ISO's inability to fully implement" the facilities it is accepting.[93]

96. Finally, DWR argues that the Commission's refusal to reopen the record is inconsistent with an order issued by the presiding judge in *Anaheim*, allowing the reopening of the record concerning the ISO's proposed revisions to its operating procedures.

Commission Determination

97. The Commission denies DWR's request for rehearing on these issues. First, as we stated in Opinion No. 478, and DWR appears to acknowledge, the issue of which facilities are under the ISO's operational control and which should be included in the TAC rates is being addressed in the individual TRR proceedings, such as *Vernon* and *Anaheim*.

98. Second, as Opinion No. 478 also made plain, the question of whether operational control issues should or must be addressed in the ISO Tariff is not at issue in this proceeding. That the presiding judge relied on Opinion No. 466 in reaching this conclusion is simply irrelevant to this outcome. If DWR believes that it essential for the ISO to include such criteria in its tariff, DWR may file a complaint raising the issue.

99. Finally, the Commission is not bound by and need not distinguish the motion granted by the presiding judge in *Anaheim*. We will review that motion if and when it is excepted to in the course of that proceeding.

Supplemental Testimony Concerning Disbursement Methodology

[91] *Id.* at 37.

[92] *Id.* at 41.

[93] *Id.* at 42.

Opinion No. 478

100. Opinion No. 478 summarily affirmed the presiding judge's ruling that certain supplemental testimony offered by Vernon was untimely and should be excluded from the record. Vernon requests rehearing of the Commission's summarily affirming this ruling.

101. On July 25, 2003, Vernon filed with the presiding judge a motion for leave to file supplemental testimony concerning changes in the in the ISO's disbursement methodology included in the ISO's proposed Amendment 34 to its tariff. Vernon's testimony addressed a proposed revision to the ISO Tariff which would change the basis for apportionment of TAC revenue allocation from a pro rata allocation based on each Participating TO's TRR to an allocation based on actual gross load. In its motion, Vernon asserted that it was not cognizant of the alleged improper effect of the disbursement methodology change until an ISO witness testified in a deposition on May 22, 2003, that other Participating TOs had been over collecting their TRRs.

102. Several parties to the proceeding objected to this testimony because it was beyond the June 4, 2003 deadline set for the judge in December 2002 for filing answering testimony in this proceeding. At a prehearing conference held on August 20, 2003, the presiding judge addressed these objections.

103. The judge determined that Vernon's testimony was directed at changing the tariff language with respect to the disbursement, rather than merely addressing its impact.[94] However, she explained that "the only possible scintilla of surprise" for Vernon arising from the deposition was that other Participating TOs "may be over-recovering" their TRRs.[95] As she went on to explain:

> [T]hat surprise goes to disparate impact and an imbalance of benefits flowing from the implementation of the tariff language. That is not the same magnitude or scope that would permit one to challenge the tariff language itself.
>
> Certainly, if Vernon had a serious issue with the tariff language, that could have raised well before the July 25th, 2003, motion to file supplemental testimony.[96]

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[94] Tr. 194.

[95] *Id.* at 209.

[96] *Id.*

Thus, the judge concluded that while she would allow Vernon's testimony to be filed, to the extent that it went to changing the tariff language – a new issue – it would be subject to a motion to strike.

104. On October 23, 2003, during the course of the hearing, the presiding judge granted the motion to strike on the ground that raising the new issue addressed in the testimony would lead to a "disruption in the development of the current record."[97]

Request for Rehearing

105. On rehearing, Vernon argues that its motion was proper under Rule 507(c)(2) of the Commission's Rules of Practice and Procedure, which provides for supplemental testimony being submitted on a showing that it is "necessary for a full disclosure of the facts or is warranted by any other showing of good cause."[98] According to Vernon, the testimony "established that Vernon submitted its supplemental testimony as soon as it was able, and had good cause for submitting the testimony when it did."[99] In this regard, Vernon explains that its testimony showed that Amendment 34 was negotiated without Vernon's participation. Thus, Vernon concludes, while it had been aware that it was under-collecting its TRR, "it was not aware of and could not be aware" that the other Participating TOs had been over-collecting their TRRs.[100]

106. Vernon goes on to argue that on rehearing, regardless of our decision on the judge's evidentiary ruling,

> the Commission should rule that the ISO's Amendment No. 34 HVAC revenue disbursement methodology is improper and should be replaced with a method that is based upon transmission investment and that is independent of utility load.[101]

Commission Determination

107. The Commission denies Vernon's request for rehearing on this issue. Under Rule 507(c)(2), late filed testimony may be admitted by the presiding judge if she determines that introduction of the testimony

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[97] *Id.* at 722.

[98] Vernon Request for Rehearing at 36 (quoting 18 C.F.R. § 385.507 (2004)).

[99] *Id.* at 37.

[100] *Id.*

[101] *Id.*

> (i) Is necessary for a full disclosure of the facts or is warranted by any other showing of good cause; and
> (ii) Would not be unduly prejudicial to any participant.[[102]]

108. The judge specifically found that Vernon's new issue would disrupt the ongoing proceeding. Thus, she clearly believed that permitting Vernon's testimony on this issue would be "unduly prejudicial" to other participants in the proceeding. Vernon's request for rehearing barely addresses the "undue prejudice" prong of Rule 507 beyond asserting that the ISO, PG&E, and SoCal Edison do not have "clean hands" on this issue because of their allegedly delaying their explanation of the surprise deposition testimony. Even assuming this to be the case, the other active parties would likewise have been subject to undue prejudice if a new issue had been introduced this late in the proceeding. Thus, the presiding judge was well within her considerable discretion in denying Vernon's motion.

109. Furthermore, the Commission is unwilling to second guess the presiding judge's finding that Vernon was not unduly surprised with respect to the underlying disbursement issue, regardless of what it learned in the deposition. Like the judge, we do not understand Vernon's contention that only the revelation with respect to the other Participating TOs' TRR collection alerted it to the need to revise the entire disbursement methodology.

110. Finally, the Commission rejects Vernon's contention that, regardless of our treatment of the evidentiary ruling, we should address the merits of its disbursement methodology claim. Under the circumstances, there is obviously no record on which we could base a decision on the issue in this proceeding. If Vernon continues to believe that the disbursement methodology is unjust and unreasonable, it may file a complaint raising this issue.

The Commission orders*:*

(A) SoCal Edison's request for clarification concerning the prospective application of the High and Low Voltage split methodology is hereby granted, as discussed in the body of this order.

(B) Silicon Valley Power's request for clarification with respect to the behind the meter exception for allocation is hereby granted, as discussed in the body of this order.

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[102] 18 C.F.R. § 385.507(c) (2004).

(C) The requests for rehearing of Opinion No. 478 are hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.