

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

California Independent System
Operator Corporation

Docket Nos. EL04-133-001
ER04-1198-000
ER04-1198-001

ORDER ADDRESSING REHEARING AND CLARIFICATION REQUESTS,
AND PROCEDURAL MOTION

(Issued May 16, 2006)

1. In this order, we address requests for rehearing and clarification of a November 5, 2004 Order.¹ In that order, we addressed issues pertaining to the transfer of the Western Area Power Administration's (Western) rights and interests in the Path 15 Upgrade to the California Independent System Operator Corporation's (CAISO) operational control.
2. In this order, we grant Western's request for rehearing and clarification, and deny Southern California Edison Company's (SCE) request for rehearing and clarification. Specifically, we accept Western's level of compensation, as proposed. We also deny a motion to establish hearing procedures in this proceeding.

Background

3. In the November 5 Order, we addressed two interrelated filings submitted concurrently by the CAISO. In Docket No. EL04-133-000, we granted in part and denied in part the CAISO's complaint seeking to modify its Transmission Control Agreement (TCA) with the Participating Transmission Owners (TOs), to provide for the transfer of Western's rights and interests in the Path 15 Upgrade to the CAISO's operational control, thereby Western became a partial Participating TO. Accordingly, in that order, we accepted the CAISO-proposed revisions to the TCA, subject to certain modifications, and directed a compliance filing.²

¹ *California Independent System Operator Corporation*, 109 FERC ¶ 61,153 (2004) (November 5 Order).

² The CAISO's compliance filing was accepted for filing in a Director Letter Order, Docket Nos. EL04-133-002 and ER04-1198-002, April 13, 2005.

4. In Docket No. ER04-1198-000, we addressed the CAISO-proposed Amendment No. 63 to its tariff, which was intended to conform the CAISO's tariff to the proposed TCA and detailed how Western would be compensated for its contribution to the Path 15 Upgrade project. Specifically, we accepted for filing certain tariff revisions in the CAISO-proposed Amendment No. 63, and conditionally accepted for filing remaining revised tariff sheets, subject to further Commission action. To aid parties to resolve the issues among themselves, we directed the Director of the Commission's Dispute Resolution Service (DRS) to convene a meeting of the parties to arrange a process that would foster negotiation and agreement with regard to the level of compensation for Western's involvement in the Path 15 Upgrade project. On April 15, 2005, the Director of the DRS reported that parties were unable to reach a resolution and future mediation sessions were suspended.³

5. Commercial operation of the Path 15 Upgrade commenced on December 22, 2004.⁴

6. Western and SCE have requested clarification and rehearing of the November 5 Order.

7. On November 4, 2005, SCE, San Diego Gas & Electric Company, the California Public Utilities Commission, and Pacific Gas and Electric Company (Joint Parties) submitted a joint motion requesting the Commission to establish an evidentiary hearing in this proceeding to examine the issue of the appropriate level of Western's cost recovery. Western filed an answer to the motion, and Joint Parties responded to Western's answer.

Discussion

8. In the original filing, to accommodate the transfer by Western to the CAISO of operational control of Western's 10 percent interest in the Path 15 Upgrade, the CAISO proposed to permit Western to transfer only that portion of its transmission facilities to the CAISO's operational control and thereby become a partial Participating TO. The CAISO also proposed to treat Western as a Project Sponsor⁵ in accordance with section 3.2.7 of its tariff for the purpose of cost recovery. Under section 3.2.7.3 of the CAISO's

³ See Dispute Resolution Service's Status Report, Docket No. ER04-1198-000, April 15, 2005.

⁴ Notice of Commercial Operation of Path 15, Docket No. ER03-1217-000, December 22, 2004.

⁵ A Project Sponsor is defined as a market participant that proposes the construction of a transmission addition or upgrade in accordance with section 3.2 of the CAISO's tariff. See Appendix D to the TCA.

Tariff,⁶ Western would be allowed to keep all related Congestion revenues and Firm Transmission Rights (FTRs) auction proceeds it derives from FTRs in the Path 15 Upgrade, and would not be permitted to recover costs pursuant to a Transmission Revenue Requirement (TRR). Protesters, however, argued that Western's cost recovery should be capped.

9. In the November 5 Order, we permitted Western to become a partial Participating TO. Specifically, we found that under specific circumstance of this case, a waiver of the requirement to turn over operational control to the CAISO of all transmission facilities was appropriate. We reasoned that Western was a federal power marketing administration which financed the construction of the vitally important project, the energization of which was to relieve severe congestion on Path 15 connecting Southern California with the northern part of the state.

10. In their rehearing requests parties raise issues pertaining to the cost recovery and Western's status as a partial Participating TO, and other miscellaneous issues addressed below.

A. Partial Participating TO

11. On rehearing, SCE challenges the Commission's decision to allow Western to become a partial Participating TO instead of requiring it to turn over to the CAISO's operational control all of its transmission facilities. SCE argues that the Commission afforded Western preferential treatment without proper justification. SCE further contends that Western's 10 percent share in the Path 15 Upgrade would only minimally reduce congestion. In support, SCE quotes the statement from the CAISO's filing in Docket No. EL04-133-000 providing that the cost of congestion that Western's share of the Path 15 Upgrade would ameliorate is not significant in dollar terms.

Commission Determination

12. We disagree that the November 5 Order treated Western in a preferential manner without proper justification. In allowing a partial transfer of Western's interests in the Path 15 Upgrade, we followed the previously-established rule that "a waiver from the general requirement can be granted 'in a very narrow circumstance, that is, if the request involves exempting a federal agency from this requirement and that agency is involved in a high value project both with overriding regional significance and that provides

⁶ See *California Independent System Operator Corp.*, 102 FERC ¶ 61,278 (2003). (*Amendment No. 48 Order*); and *California Independent System Operator Corp.*, 104 FERC ¶ 61,128, *reh'g denied*, 104 FERC ¶ 61,127 (2003) (acting on a compliance filing directed in the *Amendment No. 48 Order*).

substantial benefits to customers.”⁷ We reiterate in this order that the instant situation fits the above described criteria for the waiver. Western is a federal power marketing administration that sponsored the construction of the vitally important project. Path 15 has been identified by the U.S. Department of Energy as a major western transmission bottleneck. According to the U.S. Department of Energy, constraints on Path 15 resulted in congestion costs to California energy customers estimated at \$222 million over just the 16 months prior to December 2000.⁸ Path 15 transmission lines were often constrained because of the need for significant north-to-south transmission to accommodate the movement of hydro power from the Pacific Northwest to Southern California and also to permit the movement of energy from generators in Southern California to Northern California.⁹ The energization of the Path 15 Upgrade will relieve severe congestion on Path 15 connecting Southern California with the northern part of the state. While, as appropriately noted by SCE, the cost of congestion that Western’s share of the Path 15 Upgrade would ameliorate is not significant in dollar terms, the energization of the entire Path 15 Upgrade would not have been possible if Western had refused to turn operational control of its share to the CAISO.

B. Cost Recovery

13. On the cost recovery issue, the Commission held that “Western [was] entitled to recover the amount of its project investment (approximately \$1.3 million) plus interest on the investment amount, which [would] compensate Western for the time value of money.”¹⁰ However, we also found that “the record before us [did] not provide sufficient evidence to determine whether Western’s compensation, as proposed by the CAISO, [was] just and reasonable.”¹¹ For this reason, we encouraged parties to resolve the issue of Western’s compensation level through the Commission’s DRS. On April 15, 2005, the Director of the Commission’s DRS informed the Commission that despite “much effort, ... the parties have been unable to reach a resolution and no future mediation sessions are scheduled at this time.”¹²

⁷ See November 5 Order at P 28, citing *California Independent System Operator Corp.*, 103 FERC ¶ 61,260 at P 13 (2003).

⁸ U.S. Department of Energy's *National Transmission Grid Study*, at 15, 17, and 22 (May 2002)

⁹ *Western Area Power Administration*, 99 FERC ¶ 61,306 at 62,280 (2002) (June 12 Order).

¹⁰ See November 5 Order at P 28.

¹¹ *Id.*

¹² See *supra* n. 3.

14. On rehearing, Western requests that the Commission clarify whether it rejects or accepts the CAISO's proposed tariff revisions in the event that the parties fail to resolve the issue of Western's compensation through the DRS. In Western's opinion, the Commission may not alter the cost recovery mechanism proposed by the CAISO because it would interfere with Western's decision on the use of federal property. Western further contends that because the cost recovery mechanism is a fundamental aspect of the CAISO's proposal and without its approval the entire filing would have to be reexamined. Western also explains that the amount of its compensation is based on the amount of contribution and the amount of capacity it must retain to insure a federal interest. According to Western, it utilized many of its federal powers to facilitate the construction of the Path 15 Upgrade at a lower cost and within a shorter period of time.

15. According to Western, if it did not turn over its entitlement in the Path 15 Upgrade, it would have the ability to use 10 percent of the transmission capacity on the Path 15 Upgrade without incurring congestion charges.¹³ Instead, Western argues, it decided to turn over the operational control of its entitlement in the Path 15 Upgrade and committed to work with the CAISO to return overcollections resulting from the collection of congestion revenues in excess of the incurred congestions charges.

16. SCE also requests clarification of the cost recovery issue. Specifically, it requests the Commission to clarify that the CAISO should not distribute any revenues in excess of Western's actual investment cost, plus interest, until the appropriate level of compensation for Western is determined. SCE is concerned that refund protection provided in the November 5 Order conditionally accepting the CAISO's proposal subject to refund is inadequate. SCE's position is based on the fact that, in its opinion, two different entities have a claim on a 9.5 percent portion of the FTR auction and Congestion revenues generated by the Path 15 Upgrade. SCE is also concerned that Western, as a federal entity, may just leave the CAISO and refuse to provide the refunds if ordered.

Commission Determination

17. Upon further consideration of the cost recovery issue, we find that Western is entitled to recover 10 percent of the Congestion and FTRs auction revenues associated with the Path 15 Upgrade. On June 12, 2002, the Commission accepted for filing a Letter Agreement among Western, Trans-Elect Inc. (Trans-Elect), and Pacific Gas and Electric Company (PG&E).¹⁴ Pursuant to the Letter Agreement, Trans-Elect, PG&E and Western each would receive an entitlement to the Congestion and FTRs auction revenues associated with the Path 15 Upgrade. Under the terms of the Letter Agreement, Trans-

¹³ Western explains that under Amendment No. 48, it would receive congestion revenues, which will offset congestion costs. *See Amendment No. 48 Order.*

¹⁴ *See* June 12 Order.

Elect was entitled to receive 72 percent, PG&E was entitled to receive 18 percent and Western was entitled to receive 10 percent of these revenues. The Letter Agreement provided that final allocation of sponsors' shares would be based on the ratio of the contribution made by a participant to the project either in terms of funding or actual work performed; however, in no event would Western's share be less than 10 percent. The Letter Agreement also provided that Western would contribute about \$1.33 million to the project.¹⁵

18. The Letter Agreement was explicit with regard to the extent of Western's participation in the Path 15 Upgrade project and the level of compensation due to Western.¹⁶ The level of Western's entitlement in the Congestion and FTRs auction revenues was definitively established at the initial stage of the Path 15 Upgrade project and was not changed after the completion of the project. Western's allocation of no less than 10 percent of Congestion and FTRs auction revenue rights, unlike PG&E and Trans-Elect, was based, in part, on Western's role in initiating the development of the project and the benefits that Western provided to the entire project.¹⁷ It was recognized by all parties that Western's participation would be instrumental in getting this needed infrastructure built in an expedited time frame.

19. In setting rates, the Commission can take into account non-cost factors, such as the importance of a project for increasing the supply of energy available to customers and pricing incentives for a facilitator of the project.¹⁸ There is no dispute that the Path 15 Upgrade is crucial for relieving congestion along Path 15 and making the energy supply from Northern California available to customers in Southern California and *vice versa*. The proposed level of compensation provided an incentive for Western to participate in the Path 15 Upgrade project and get it constructed. Without Western's involvement the expeditious construction of such critical infrastructure upgrade would not have been possible. Our finding to allow Western to retain revenues above its study costs must be

¹⁵ *Id.* at 62,278.

¹⁶ *See* Letter Agreement, Docket No. ER02-1672-000, Exhibits A and B (April 30, 2002).

¹⁷ The Letter Agreement provides that PG&E's initial allocation was based on the ratio of: the estimated costs for PG&E substation modifications to the entire project cost. Similarly, Trans-Elect's initial allocation was based on the ratio of: the estimated funds it would provide for the transmission line to the entire project. Western's initial allocation was based on the ratio of: all other estimated costs, including land; its role in initiating the public/private partnership development; ownership of the project; and the benefits that Western provides to the entire project.

¹⁸ *Public Utilities Commission of the State of California v. FERC*, 367 F.3d 925, 929 (D.C. Cir. 2004).

viewed as a different rate treatment; that is, a pricing incentive to getting needed infrastructure built expeditiously. Pursuant to court precedent, “using pricing incentives to increase supply of energy available to customers is a valid, non-cost consideration in setting rates.”¹⁹

20. For these reasons, we find it appropriate for Western to retain the revenues it will receive above its \$1.3 million study costs. Accordingly, we clarify that we accept for filing the Amendment No. 63 provision setting forth a 10 percent entitlement in Congestion and FTRs auction revenues for Western. Western’s request for clarification is hereby granted; SCE’s request for clarification is rendered moot. Accordingly, we also deny the Joint Parties’ motion to establish an evidentiary hearing in this proceeding.

C. Interconnection Provision

21. In the November 5 Order, we rejected without prejudice one of the proposed amendments to the TCA. Specifically, the proposed revision to the TCA provides that Western’s general requirements for interconnection are the requirements set forth in Western’s TO Tariff or in Western’s OATT, as applicable, and that “[e]xecution of [the TCA] shall not constitute agreement of any Party that Western is in compliance with FERC’s regulations governing interconnections.”²⁰ We found that:

[a]s a general matter generator interconnection to facilities under the control of the CAISO should be governed by the CAISO tariff. In this case, where we have three project participants, we believe that one tariff should govern. We are unaware by the record before us in this case of how using the CAISO tariff may compromise Western’s mandate under federal statutes and regulations. Accordingly, we reject without prejudice this provision.²¹

22. On rehearing, Western argues that the Commission should have accepted the proposed TCA amendment. In Western’s opinion, the Commission should have deferred to the discretion of Western because the proposed revision is within Western’s power to impose reasonable conditions on the use of federal property. Western further explains that because a request for interconnection to Western’s transmission system represents a request for use of federal property, the TCA amendment in question was proposed to reserve the right of Western to determine the terms and condition for the use of federal property. Western further states that the proposed TCA revisions establish standard terms and conditions which Western imposes on all interconnection requests.

¹⁹ *Id.*

²⁰ Proposed TCA section 10.5.

²¹ *See* November 5 Order at P 40.

23. Western also contends that allowing requests for interconnection to Western's transmission systems to be governed by Western-established procedures is consistent with the current practice. It explains that the CAISO only governs large generator interconnections and each Participating TO has its own interconnection procedures for other type of interconnections. As a result, Western states, on the Path 15 Upgrade, interconnection requests other than large generator requests, are made in accordance with PG&E's tariff. Thus, Western concludes, requests for interconnection into Western's transmission line should be subject to Western's interconnection requirements. Western adds that while such requests are highly unlikely, it believes that nevertheless it must have appropriate procedures in place.

Commission Determination

24. Upon further consideration of the interconnection issue, we agree with Western and grant its rehearing request. The rejection of the interconnection provision was without prejudice. Western has demonstrated that using the CAISO tariff for interconnection purposes is inconsistent with Western's authority under federal law to impose reasonable conditions on the use of federal property.

D. Consistency with Federal Law and Regulations

25. On rehearing, SCE challenges the Commission's determination in regard to section 26.14 of the TCA, which provides that Western will not incur any liability for failing to comply with a TCA provision if that provision is inconsistent with any federal statute, or regulation or order lawfully promulgated thereunder. According to SCE, the Commission's finding that the proposed provision was reasonable in that it excuses any party to the TCA, not only Western, from liability for failure to comply with the TCA if the TCA becomes inconsistent with any federal law, order, or regulation did not address SCE's concern that Western may itself issue a federal regulation or order that exempts itself from liability under the TCA. SCE further argues that since the other participating TOs are not capable of issuing federal regulations or orders, the Commission's position that all parties are treated identically makes no sense. In conclusion, SCE states that the Commission should ensure that no party, including Western, can avoid liability through its own actions.

Commission Determination

26. We disagree with SCE's contention. Proposed TCA section 26.14 excuses *any* party to the TCA, not only Western, from liability for failure to comply with the TCA in the event that the TCA is inconsistent with any federal law, order, or regulation. Specifically, section 26.14 states in pertinent part:

... No Party shall incur any liability by failing to comply with a provision of this Agreement that is inapplicable to it by reason of being inconsistent with any federal statute, or regulation, or order lawfully promulgated thereunder...

27. Our acceptance of section 26.14 in the November 5 Order was intended to “remove for Western regulatory risks associated with its status as a federal power marketing entity and thus...[to] allow the transfer of operational control over a portion of the vitally important Path 15 Upgrade to the CAISO.”²² Western’s participation in the Path 15 Upgrade project was crucial for the expeditious construction of the critically needed transmission infrastructure and our action in the November 5 Order recognized that fact. We also noted in the November 5 Order that in another analogous proceeding, the Commission exempted certain municipal government utilities from the requirement conditioning their withdrawal from the CAISO due to impending adverse tax action.²³ In that order, the Commission stated that its decision to eliminate the requirement at issue there removed the financial risk of participating in the CAISO for those entities.²⁴ Similarly, here the November 5 Order removed for Western regulatory risks uniquely associated with its status as a federal power marketing entity and thus allowed the transfer of operational control over a portion of the vitally important Path 15 Upgrade to the CAISO. While we acknowledge that Western, unlike other parties, may issue federal regulations or orders, that fact does not dictate a different result. Indeed, for us to rule otherwise would amount to a determination by this Commission that another federal agency cannot issue regulations and orders. That is beyond our authority.

28. Moreover, as the Commission explained in the November 5 Order, the CAISO’s tariff contains certain protective mechanisms that would minimize an effect on other parties to the TCA in the event that Western or any other party to the TCA is compelled by law to withdraw from the TCA.²⁵ Section 26.14 of the TCA requires the non-complying party to use its best efforts to comply with the TCA to the extent that applicable federal laws, and regulation and orders lawfully promulgated thereunder, permit it to do so. Furthermore, under section 26.14, the notice requirement will be waived for Western only if: (1) Western’s withdrawal from the CAISO is directed by the United States Congress; and (2) Western’s withdrawal is requested by another party to the TCA due to a Western-issued regulation. In all other situations, Western does not have the right to withdraw from the TCA without notice or after a significantly shortened

²² *Id.* at P 44.

²³ *See California Independent System Operator Corp.*, 103 FERC ¶ 61,113 (2003).

²⁴ *See Id.* at P 2 and 5.

²⁵ *See* November 5 Order at P 43-44.

notice period. The notice and other withdrawal requirements in section 3.3 of the TCA will apply to Western should it be compelled to leave the CAISO. For these reasons, we deny SCE's request for rehearing.

The Commission orders:

(A) Western's request for rehearing and clarification is granted, as discussed in the body of this order.

(B) SCE's request for rehearing and clarification is denied, as discussed in the body of this order.

(C) Joint Parties' motion to establish an evidentiary hearing is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.