101 FERC ¶ 61, 151
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
and Nora Mead Brownell.

Pacific Gas and Electric Company	Docket Nos.	ER97-2358-004
		ER97-2358-003
		ER98-2351-002
		ER98-2351-003
Southern California Edison Company	Docket Nos.	ER97-2355-004
		ER98-2322-001
		ER97-2355-006
		ER98-2322-002
San Diego Gas & Electric Company	Docket Nos.	ER97-2364-004
		ER97-4235-003
		ER98-497-003
		ER98-2371-001
		ER97-2364-005
		ER97-4235-004
		ER98-497-004
		ER98-2371-002

OPINION NO. 458-A

ORDER DENYING REHEARING, GRANTING CLARIFICATION
AND APPROVING PARTIAL SETTLEMENT

(Issued November 1, 2002)

20021105-3012 Received by FERC OSEC 11/01/2002 in Docket#: ER97-2358-004

1. In Opinion No. 458,[1] the Commission affirmed an Initial Decision[2] which addressed issues arising from the non-rate terms and conditions of Transmission Owner (TO) Tariffs and Wholesale Distribution Tariffs (WDTs) filed by Pacific Gas and Electric Company (PG&E), Southern California Edison Company (Edison) and San Diego Gas and Electric Company (San Diego),[3] as a result of the restructuring of California's electric industry. As relevant here, the Commission affirmed with discussion the presiding judge's decision that certain cost differentials between the Companies' existing transmission contracts (Existing Contracts or ETCs) and the California Independent System Operator Corporation (California ISO) Tariff cannot be collected from the Companies' TO Tariff customers. Timely requests for rehearing were filed by PG&E, Edison, San Diego, the Sacramento Municipal Utility District (SMUD), the M-S-R Public Power Agency and the Cities of Redding and Santa Clara, California (collectively, the Cities), the Modesto Irrigation District (Modesto), and the Transmission Agency of Northern California (TANC). As discussed below, the Commission denies rehearing, though we grant clarification requested by certain parties on a few issues. This order benefits the public by assuring that the TO Tariff non-rate terms and conditions are just and reasonable, and that the TO Tariff customers are not subject to inappropriate costs.

Background

2. This case involves the treatment of two categories of costs imposed on the Companies by the California ISO Tariff: transmission loss and ancillary service costs and, with respect to PG&E only, certain neutrality and unaccounted for energy (UFE) costs. While these costs arise in connection with service under the Existing Contracts, the Companies do not seek to recover them from their Existing Contract customers. Rather, they would prefer to recover these costs from customers who take service under the TO Tariffs, by means of the Transmission Revenue Balancing Account Adjustment (TRBAA)[4] mechanism contained in those tariffs.

3. The Initial Decision summed up the issues in these terms:

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[1]Pacific Gas and Electric Company, et al., 100 FERC ¶ 61,156 (2002).

[2]Pacific Gas and Electric Company, et al., 88 FERC ¶ 63,007 (1999).

[3]We generally refer to these three parties as the Companies.

[4]Occasionally referred to as the TRBA, when the mechanism itself is meant.

> The Companies have Existing Contracts (which they acknowledge must be honored) that fail, according to the Companies, to permit collection of certain costs now charged to the Companies by the ISO. The Companies' attempted response to collecting these costs is to charge them to all customers but those with Existing Contracts. All other customers, then, would be responsible for costs incurred on their own behalf as well as those incurred on behalf of the Existing Contract customers.[5]

4. The judge rejected the Companies' approach to recovering the transmission loss and ancillary service cost differentials, holding that the Commission policy of honoring existing contracts did not "mean that cross-subsidization is an approved method for doing so."[6] In the judge's view, "[c]ost-causation principles dictate that the Existing Contract customers, and not all TO Tariff customers, should pay for the charges incurred as a result of the ISO's billing requirements which affect service provided under those Existing Contracts."[7] The judge also expressed concern that the inclusion of the Existing Contracts' transmission loss and ancillary service requirements costs in the TRBAA of the TO Tariffs would result in the double-charging of any TO Tariff customer which performs its own scheduling coordination services.

5. The Initial Decision interpreted the ISO Tariff as "explicitly provid[ing]" for Existing Contracts to be reformed, by means of Federal Power Act (FPA) sections 205 or 206.[8] If not, the judge found, the Companies themselves must shoulder this cost burden. In his view, to the extent that the terms of the Existing Contracts prohibit rate changes, the Companies accepted the risk of potential cost increases at the time of the negotiation

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[5] 88 FERC at 65,051.

[6] Id. (footnote omitted).

[7] Id. at 65,052.

[8] Id., citing California ISO Tariff, Section 2.4.4.4.4.5.

of those contracts. By the same token, the TO Tariff customers, who were not parties to the negotiations, should not be exposed to that risk.[9]

6. The Initial Decision resolved the issue of whether the UFE costs could be included within PG&E's TO Tariff in the same manner. The judge expressed concern that PG&E's approach would compel entities serving as their own Scheduling Coordinators to nonetheless pay ISO-imposed UFE costs, and noted that PG&E had conceded this potential for double charging. The judge also found that the same cost-shifting/cost-subsidization concerns that exist with respect to transmission losses and ancillary services "precludes PG&E from including the ISO-imposed Neutrality/Unaccounted for Energy Charges in PG&E's TO Tariff TRBAA."[10]

7. In Opinion No. 458, the Commission affirmed the Initial Decision on these issues. In our view, "[t]he fundamental question in this proceeding is whether the Companies' proposed TO and WDT tariffs are just and reasonable."[11] We went on to reject the Companies' contention that the plain meaning of the California ISO Tariff provisions required the recovery of the costs at issue through the TO Tariffs' TRBAA. In this regard, we determined that Section 2.4.3.1 of the ISO Tariff "is essentially precatory," providing only that the parties to the Existing Contracts will work with the California ISO to ensure that such contracts are exercised in a manner which, "to the extent possible, imposes no additional financial burden on either the Participating TO or the contract rights holder (beyond that in the Existing Contract)."[12] The Commission also rejected the Companies' reliance on the California ISO Tariff's definition of Transmission Revenue Credit as irrelevant. In our view, this definition merely provided

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[9]The Initial Decision went on to hold that the TRBAA was an inappropriate tracking mechanism. Opinion No. 458 did not reach this issue, as we concluded that the costs should not be recovered from the TO Tariff customers in any event. For the same reason, we deny Edison's contention (Edison Request at 22) that we should revisit this issue.

[10]88 FERC at 65,054.

[11]100 FERC ¶ 61,156 at P 27.

[12]Id. at P 28, quoting Section 2.4.3.1.

that the ISO will assess these costs to the Companies, but says nothing about what the Companies can do to recover these costs.[13]

8. The Commission further concluded that the judge had reasonably relied on Section 2.4.4.4.4.5 of the California ISO Tariff. We agreed with the judge's reading of that provision to mean that, if the California ISO's rules and protocols governing transmission losses or ancillary service requirements are not the same as those in the Existing Contracts, the California ISO will provide the information so that the parties to those contracts may resolve the matter "by contract modification or otherwise."[14]

9. Opinion No. 458 also affirmed the judge's analysis that cost causation principles favored the Companies shouldering the resulting cost burden, unless and until they could modify the Existing Contracts. As the Commission explained:

> The fact is that the costs are associated with service provided under the existing contracts, not the TO Tariffs, and should not be shifted to the TO Tariff customers. The remedy, as the judge observed, is for the Companies to reform their existing contracts by means of FPA sections 205 and 206. The Companies' contention that these remedies are inadequate is devoid of merit; these are the remedies the statute provides.[[15]]

10. The Commission went on to reject PG&E's argument concerning recovery of the UFE charges on the same basis. Additionally, we dismissed SMUD's concern that customers who self-provide ancillary services would face double charges: "It appears self-evident that for any party in this circumstance, the Companies will incur no related costs that need to be recovered."[16]

Discussion

Interpreting the ISO Tariff

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[13] Id. at P 28.

[14] Id. at P 29.

[15] Id. at P 30.

[16] Id. at P 31.

11. The parties seeking rehearing argue that Opinion No. 458 misinterpreted the relevant terms of the California ISO Tariff.[17] Thus, San Diego asserts that reading Section 7.1 of the tariff, governing transmission pricing, in conjunction with the tariff's definition of Transmission Revenue Credit (Item G, Master Definitions Supplement), unambiguously means that

> any difference between losses as calculated in an existing contract and losses as calculated under the ISO Tariff would be reflected as a Transmission Revenue Credit and thus, through the mechanism of the TRBA, operate as an adjustment to the Transmission Revenue Requirement underlying the Access Charge for each Transmission Owner.[[18]]

As Edison puts it, if the ISO Tariff "did not intend" that the "cost recovery methodology" would be based on the interaction of Section 7.1 and the definition of Transmission Revenue Credit, the latter would be "superfluous."[19]

12. The Companies likewise take issue with the Commission's reading of Section 2.4.4.4.4.5. Edison accuses the Commission of ignoring the portion of that section which provides that the TOs and the parties to the Existing Contracts may settle their differences "through the relevant TO Tariff."[20] PG&E, on the other hand, acknowledges

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[17]San Diego Request at 6-9; Edison Request at 7-9; PG&E Request at 7-9; SMUD Request 3-5. As SMUD's request for rehearing generally tracks that of the Companies, we address it individually only where it brings up distinct points. It should also be mentioned that the requests for rehearing of the Cities, Modesto and TANC require no additional comment on our part, as they merely incorporate SMUD's arguments by reference.

[18]San Diego Request at 7. See also Edison Request at 11; PG&E Request at 8-9.

[19]Edison Request at 10.

[20]Edison Request at 10, quoting Section 2.4.4.4.4.5 (emphasis Edison's).

that the section additionally provides for contract modification as a remedy, but dismisses that clause as "truly precatory," as opposed to cost recovery through the TO Tariff.[21]

13. Interestingly, the Companies make scant mention of Section 2.4.3.1 of the ISO Tariff in their requests for rehearing. PG&E takes the most categorical position, claiming that "the intent of this provision" is clearly that Existing Contracts should be honored without being subject to any "additional financial burden" unless such burden "is impossible to avoid."[22] San Diego merely observes that its interpretation of Section 7.1 as requiring cost differentials with existing contracts to be recovered by the TRBA is "consistent" with Section 2.4.3.1's provision that, "to the extent possible," no additional financial burden be imposed on the TOs and Existing Contract customers.[23]

14. The Companies also argue that the Commission agreed with the interpretation of the California ISO Tariff they favor when we originally accepted the tariff for filing.[24] Thus, according to San Diego, in the order:

> the Commission declared that the tariff remedy is for the ISO to work with the Transmission Owner to fix the problem through the Transmission Owner's rates – i.e., through the TRBAA – the very remedy [Opinion No. 458] rejects.[[25]]

15. The Commission denies rehearing on this issue. We reject the Companies' view that Section 7.1 and the definition of Transmission Revenue Credit in the California ISO Tariff must be interpreted to place the burden of the Existing Contract-related cost differentials on TO Tariff customers. As we held in Opinion No. 458, the ISO Tariff provisions determine the manner in which the California ISO will collect the costs from

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[21]PG&E Request at 9. San Diego takes a similar view. San Diego Request at 9.

[22]PG&E Request at 9 n.14 (emphasis PG&E's).

[23]San Diego Request at 7, quoting Section 2.4.3.1. Edison and SMUD do not appear to address Section 2.4.3.1 at all.

[24]See San Diego Request at 8-9 and PG&E Request at 6-7, citing Pacific Gas & Electric, et al., 81 FERC ¶ 61,122 at 61,463-64 & n.145 (1997) (hereafter October 1997 Order).

[25]San Diego Request at 9, citing October 1997 Order, 81 FERC at 61,464 n.145.

the Companies. Reading these provisions as determinative of how the Companies should, in turn, recover these costs is not a reasonable interpretation, as it would render superfluous Section 2.4.3.1 (dealing with the manner in which Existing Contracts for transmission service should be treated) and Section 2.4.4.4.4.5 (dealing with transmission losses and ancillary services under Existing Contracts).

16. We also reject the Companies' arguments on rehearing concerning Section 2.4.3.1 and Section 2.4.4.4.4.5. Concerning PG&E's newly-minted argument that these provisions, read together, require the Companies to recover the costs at issue through the TRBA, it is instructive to review PG&E's earlier thoughts on the matter:

> The Companies are not denying that ISO Tariff Section 2.4.4.4.4.5 allows the Companies to bilaterally settle differences with their Existing Contract holders . . . through settlement or by making section 205 or 206 filings. This approach, however, is not as consistent with the Commission's policy of honoring Existing Contracts or ISO Tariff Section 2.4.3.1 because it requires Existing Contract holders to bear the costs, which they have not caused. Section 2.4.4.4.4.5 provides the Companies several options for addressing a problem created by the ISO and the Companies chose the option that better reflected Commission policy and cost causation.[[26]]

In other words, PG&E has previously conceded that the relevant provisions of the ISO Tariff allowed the Companies to recover the cost differential either by means of the Existing Contracts or the TO Tariffs – exactly as the Presiding Judge concluded.

17. Nor did the Commission speak to the issue in this case in the October 1997 Order. In the language primarily relied on by the Companies in this context, we stated:

> Parties to Existing Contracts will also continue to pay for transmission losses and ancillary services under their Existing Contracts. To the extent there are any differences in the requirements associated with Existing Contracts and those under the ISO's rules and protocols, the ISO will establish a

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[26]PG&E Reply Brief at 8 (citations omitted) (March 26, 1999) .

> mechanism acceptable to the Transmission Owner to roll any shortfall or surplus into the ISO rates applicable to that Transmission Owner.[27]

Thus, the Commission was addressing the manner in which the ISO collects its revenues under the ISO Tariff, i.e., how the costs in question would be rolled "into the ISO rates." This language does not, and was not intended to, explain the next step in the process – how the TOs would recover the costs from their customers.[28]

18. We once again therefore affirm as reasonable the Initial Decision's interpretation of the two relevant provisions of the California ISO Tariff. First, Section 2.4.4.4.5 contemplates that the Companies may seek to recover the contested costs though the Existing Contracts, by filing to reform the contracts, either under section 205 or section 206, as appropriate. Second, this approach is consistent with Section 2.4.3.1, which provides only that exercise of Existing Contract rights under the ISO regime will impose no additional financial burden on the Participating TO or contract rights holder "to the extent possible."[29]

Cost Shifting and Detrimental Reliance

19. The Companies argue that the Commission's decision is flawed on equitable grounds. First, they object to our approval of the judge's view that assessing these costs to the TO Tariff customers would result in unwarranted cost-shifting or cross-subsidization. San Diego maintains that the added costs for transmission losses and ancillary services did not arise from any changes in the cost of serving Existing Contract customers: service to those customers "has not been substantially changed by virtue of

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[27]October 1997 Order, 81 FERC at 61,464 n.145.

[28]Similarly, Edison's reliance (Edison Request at 5 & n.10) on language in California Independent System Operator Corporation, 100 FERC ¶ 61,209 at P 9 n.10 (2002), is misplaced. The Commission there merely described as background the definition of the TRBA. We did not address the cost recovery issue.

[29]Our interpretation of the relevant provisions of the California ISO Tariff disposes of Edison's claim (Edison Request at 7-10) that Opinion No. 458 violates the filed rate doctrine.

industry restructuring."[30] Rather, San Diego states, restructuring was "adopted for the benefit of California retail customers, as part of the effort to promote competitive markets."[31] Similarly, PG&E argues that the costs of making service under the California ISO available to the market should be "shared broadly among those customers who are the direct beneficiaries of the ISO Tariff structure and industry restructuring generally," namely, TO Tariff customers.[32]

20. Second, the Companies make an argument that the result in this case undermines their legitimate expectation that, on entering into the Existing Contracts that they would recover their costs. As Edison asserts:

> while the Companies accepted the risk that their costs would increase when they entered into fixed-rate ETCs, they did not accept the risk that the Commission would increase their costs by approving an ISO Tariff that required them to pay more than their own costs for the services they had contracted to render.[[33]]

Edison complains that some of the contracts in question were of the fixed-variety, under which the parties had waived their Section 205 and 206 rights. As a result, Edison contends, Opinion No. 458 runs afoul of the basic ratemaking doctrine that regulated utilities are guaranteed a reasonable return on investment.[34]

21. The Companies make a related claim that they "justifiably relied in 1997" on their interpretation of the ISO Tariff, permitting them to recover the costs through the TRBAA, so that it would be "fundamentally unfair" to impose such a burden on their

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[30]San Diego Request at 5.

[31]Id.

[32]PG&E Request at 11-12.

[33]Edison Request at 16 (emphasis in original).

[34]In this context, Edison relies on such seminal cases as FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944) (Hope) and Bluefield Water Works v. Public Service Commission, 262 U.S. 679 (1923).

shareholders.[35] For example, Edison maintains that it was "lulled . . . into believing" that the Commission agreed with the Companies' interpretation by the October 1997 Order accepting the ISO Tariff.[36] Edison further claims that it "may well have taken actions that would mitigate its losses" had it known that the Commission "would not reverse" the judge.[37] Finally, Edison and PG&E contend that they relied on the Commission's acceptance in September 2001 of a TO Tariff filed by City of Vernon, which includes the same definitions of TRBA and Transmission Revenue Requirement as do their own TO Tariffs.[38] According to Edison and PG&E, the Commission there has approved the same passthrough of Existing Contract-related costs to TO Tariff customers that Opinion No. 458 forbids.

22. San Diego also argues that, since Existing Contract revenues are used to reduce the TO Tariff revenue requirement, any additional costs associated with the cost differentials at issue should likewise be reflected in the TO Tariff revenue requirement.

23. The Commission denies rehearing on these issues. Concerning the application of cost causation principles, we cannot agree that the benefits of energy industry restructuring have accrued merely to TO Tariff customers. On the contrary, we have observed that enhanced reliability and market development resulting from industry restructuring are benefits that are distributed across the spectrum of industry participants.[39] Thus, we decline to identify the TO Tariff customers as benefitting from restructuring so singularly as to require costs incurred in connection with the Existing Contracts, to which they are not parties, to be passed on to them. In sum, it was hardly

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[35]PG&E Request at 12-13; San Diego Request at 12-15. On this reasoning, the Companies request that, at the least, the Commission's interpretation be applied prospectively only.

[36]Edison Request at 17, citing October 1997 Order, 81 FERC at 61,464 n.145.

[37]Id. at 19.

[38]Id. at 17-18; PG&E Request at 10 n.18, citing City of Vernon, 96 FERC ¶ 61,312 (2001) (Vernon).

[39]See, e.g., Remedying Undue Discrimination through Open Access Transmission Service and Standard Market Design, Notice of Proposed Rulemaking, FERC Stats. & Regs. ¶ 32,563 at P 35 (2002); California Power Exchange, 85 FERC ¶ 61,263 at 62,068 (1998).

unreasonable for the judge to find that such an assignment of costs would amount to inappropriate cross-subsidization. The Companies' contention that they may not be able to recover these costs from some of the Existing Contract customers does not change this result. It is well-established that while regulated companies must have a reasonable opportunity to recover their costs, they enjoy no guarantee that they will necessarily do so.[40]

24. The Commission also rejects San Diego's claim that the Existing Contact revenue credit incorporated into the TO Tariff revenue requirement constitutes a benefit to TO Tariff customers that should be balanced by assigning the associated cost differentials to the TO Tariff customers. As San Diego acknowledges,[41] TO Tariff rates are designed to recover all of the transmission owner's fixed costs. Thus, far from being some sort of unwarranted benefit, the Existing Contract revenue credit merely reflects the proper prevention of double recovery in TO Tariff rates.

25. Finally, the notion that the Companies justifiably relied to their detriment on any action by the Commission is totally without merit. First, as explained above, it was simply not reasonable for the Companies to assume the October 1997 Order resolved the issue here in their favor. Second, we cannot take seriously Edison's assumption that the Initial Decision would be reversed.[42] Finally, no party in the Vernon proceeding raised this issue.[43] In any event, we find that Vernon does not support Edison's and PG&E's position. The City of Vernon's circumstances are distinguishable from those of Edison

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[40]E.g., Hope, 320 U.S. at 603; Jersey Central Power & Light v. FERC, 810 F.2d 1168, 1180-81 & n.3 (D.C. Cir. 1987).

[41]San Diego Request at 5-6.

[42]In this regard, it is interesting to note that PG&E, on the heels of the Initial Decision, filed a tariff to recover the costs it might incur from the California ISO as Scheduling Coordinator for existing transmission customers. See Pacific Gas & Electric Co., 90 FERC ¶ 61,010 (1999). This would tend to undermine the claim of the other Companies that no alternate recourse was available.

[43]See, e.g., Midwest Generation, LLC, 95 FERC ¶ 62,231 at 61,799 n.17 (2001).

and PG&E, in that it has no Existing Contracts of the type that can lead to the unrecovered cost differentials at issue here.[44]

Requests for Clarification

26. Edison and PG&E request clarification concerning an uncontested Offer of Partial Settlement (Partial Settlement) that resolved a number of issues in this proceeding. While the judge certified the Partial Settlement to the Commission on the same date that he issued the Initial Decision, Opinion No. 458 did not address the Partial Settlement. Accordingly, Edison and PG&E request clarification that the Partial Settlement should be approved.

27. The Commission grants the requested clarification. The proposed uncontested Partial Settlement, as conditioned below, is in the public interest. Accordingly, we clarify that the Partial Settlement, as conditioned below, is approved.

28. While Trial Staff supported the Partial Settlement, it requested certain language corrections to the tariff sheets attached thereto. In their reply comments, the Companies agreed to all but two of the requested corrections. We find that the Companies' explanation of their objections to the two corrections is persuasive. Accordingly, our approval of the Partial Settlement is conditioned upon the Companies including the agreed-upon corrections in their compliance filing.[45]

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[44]While Edison makes reference to City of Vernon's Existing Contract with PG&E (Edison Request at 7, n.13), this contract merely provides for an exchange of firm transmission services between the parties over transmission entitlements they each own, without charge by either party. Thus, this Existing Contract does not contain traditional rates for transmission service which could differ from those charged by the California ISO. More importantly, it expressly assigns all potential costs associated with the transmission entitlements being exchanged between the two parties. There is thus no potential for cost differentials of the type at issue in this proceeding to be passed through City of Vernon's TO Tariff.

[45]Edison also requests clarification that the language contained in the Partial Settlement with respect to distribution facility ownership is approved, rather than preliminary language which was inadvertently quoted by the Initial Decision. The Commission grants this clarification; the language in the Partial Settlement is approved.

29. SMUD and Modesto seek clarification with respect to self-provided ancillary services. As Modesto explains:

> Scheduling Coordinators should not be charged by the ISO for ancillary services which are, in turn, attributed to wholesale customers of those Scheduling Coordinators which are self-providing those ancillary services.[[46]]

Otherwise, Modesto states, the likely unreasonable result will be that such Scheduling Coordinators will seek to pass through costs for ancillary services to self-providing customers.

30. The Commission agrees. The ISO and the Companies must ensure that customers which self-provide ancillary services will not also be charged for them.

31. San Diego requests clarification that if the Commission declines to grant rehearing, it nonetheless does not intend to preclude enforcement of Section 2.4.3.1(vi) of the ISO Tariff, which requires the ISO to accommodate Existing Contracts to the extent possible where doing so "does not require the ISO to interpret or underwrite the economics of the Existing Contract."[47] San Diego is concerned that it be able to continue to reimburse losses in kind, rather than through a charge or credit to the TRBAA.

32. We grant the requested clarification. Such flexibility should be maintained.

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[46]Modesto Request at 5.

[47]San Diego Request at 10 n.16, quoting Section 2.4.3.1 (vi).

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The Commission orders:

(A) The requests for rehearing are hereby denied.

(B) The requests for clarification by Edison and PG&E, and SMUD and Modesto, and San Diego are hereby granted, as discussed in the body of this order.

(C) The Partial Settlement, as conditioned, is hereby approved, as discussed in the body of this order. A compliance filing, with the agreed-upon corrections, should be filed within 30 days of the date of the issuance of this order.

By the Commission.

(S E A L)

Linwood A. Watson, Jr.,
Deputy Secretary.