119 FERC ¶ 61,266
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Independent Energy Producers Association	Docket Nos. EL05-146-001
	EL05-146-002
v.	EL05-146-003
	EL05-146-005
California Independent System Operator Corporation	
California Independent System Operator Corporation	ER07-326-001
	ER07-326-002

(Not Consolidated)

ORDER ON REHEARING AND COMPLIANCE

(Issued June 11, 2007)

1. These proceedings arise out of an August 26, 2005 complaint (Complaint) filed by the Independent Energy Producers Association (IEP) against the California Independent System Operator Corporation (CAISO) with respect to the then-existing must-offer obligation under the CAISO Tariff in Docket No. EL05-146. On July 20, 2006,[1] as clarified on September 27, 2006,[2] the Commission issued an Order on Complaint and Offer of Settlement accepting, in part and on an interim basis, an Offer of Settlement between certain of the parties which proposed the institution of a Reliability Capacity Services Tariff (RCST), and establishing a paper hearing. This order addresses requests for clarification and/or rehearing of the July 20, 2006 and September 27, 2006 Orders. This order also addresses requests for rehearing of the February 13, 2007 Order on the

[1] *Independent Energy Producers Association v. California Independent System Operator Corp.*, 116 FERC ¶ 61,069 (2006) (July 20, 2006 Order).

[2] *Independent Energy Producers Association v. California Independent System Operator Corp.*, 116 FERC ¶ 61,297 (2006) (September 27, 2006 Order).

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CAISO's proposal to implement 2007 tariff amendments to the Offer of Settlement.[3] For the reasons discussed below, we deny the requests for clarification and/or rehearing. We also accept the March 15, 2007 compliance filings submitted by the CAISO in these proceedings and reject as moot the October 20, 2006 compliance filing.

I. Background

A. Procedural History

2. In an order issued on April 26, 2001,[4] the Commission established a prospective mitigation and monitoring plan for the California wholesale electric markets. One of the fundamental elements of the plan was the implementation of a must-offer obligation, pursuant to which most generators serving California markets were required to offer all of their capacity in real time during all hours if it is available and not already scheduled to run through bilateral agreements. The CAISO implemented the must-offer obligation beginning July 20, 2001.

3. In an order issued on June 17, 2004,[5] the Commission recognized the California Public Utilities Commission's (CPUC) plan to phase in resource adequacy requirements and suggested that if the CAISO determines that the resource adequacy requirements are sufficient to meet its operational needs, the resource adequacy requirements and obligations could serve to replace the existing must-offer obligation.[6] Additionally, on July 8, 2004,[7] the Commission advised that if IEP believed the current must-offer

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[3] *California Independent System Operator Corp.*, 118 FERC ¶ 61,097 (2007) (February 13, 2007 Order on 2007 RCST).

[4] *San Diego & Electric Co.*, 95 FERC ¶ 61,115, at 61,355-57 (April 26, 2001 Order), *order on reh'g*, 95 FERC ¶ 61,418, *order on reh'g*, 97 FERC ¶ 61,275 (2001), *order on reh'g*, 99 FERC ¶ 61,160 (2002), *pet. granted in part and denied in part sub nom. Public Utils. Comm'n of the State of Cal. v. FERC*, 462 F.3d 1027 (9th Cir. 2006).

[5] *California Independent System Operator Corp.*, 107 FERC ¶ 61,274 (June 17, 2004 Order), *order on reh'g*, 108 FERC ¶ 61,254 (2004).

[6] *See* June 17, 2004 Order, 107 FERC ¶ 61,274 at P 26-28.

[7] *California Independent System Operator Corp.*, 108 FERC ¶ 61,022 (July 8, 2004 Order), *order on reh'g*, 109 FERC ¶ 61,097 (2004).

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obligation to be unjust and unreasonable, it may seek to initiate a section 206 proceeding to challenge the justness and reasonableness of the current method and seek an alternative proposal.[8]

4. On August 26, 2005, IEP filed the Complaint against the CAISO under section 206 of the Federal Power Act (FPA).[9] The Complaint alleged that the existing must-offer obligation under the CAISO Tariff is flawed and no longer just and reasonable. The Complaint also requested that the Commission direct the CAISO to replace the existing must-offer obligation and related minimum load cost compensation tariff provisions with an interim set of tariff provisions to remain in effect until the CAISO's market redesign goes into effect.[10]

5. On November 14, 2005, IEP requested that the Commission defer action on the Complaint pending settlement discussion with the parties.[11] On November 18, 2005, Commission Staff convened a technical conference to discuss the issues raised in the Complaint.

6. On March 31, 2006 certain parties (the Settling Parties[12]) filed the Offer of Settlement, which proposed the institution of an RCST. The RCST, which was initially proposed by IEP in the Complaint, modifies the existing Commission-imposed must-offer obligation under the CAISO Tariff, as well as other market design elements. The RCST provides a backstop capacity procurement mechanism to the CAISO that includes provisions establishing: (1) must-offer capacity payment rates; (2) RCST rates due to designation resulting from a Significant Event; (3) RCST rates due to designation resulting from deficiency in Resource Adequacy showings; and (4) payments to

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[8] July 8, 2004 Order, 108 FERC ¶ 61,022 at P 111.

[9] 16 U.S.C. § 824e (2000).

[10] The CAISO's market redesign is currently planned to go into effect on January 31, 2008.

[11] IEP and the CAISO filed joint motions to continue deferral of action on the Complaint on December 9, 2005, and on December 19, 2005.

[12] The Settling Parties are: IEP; the CAISO; the CPUC; Pacific Gas and Electric Company (PG&E); San Diego Gas & Electric Company; and Southern California Edison Company (SCE).

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frequently mitigated units. In addition, the RCST establishes cost allocation methodologies and governs the rules by which the CAISO can procure RCST capacity. The Settling Parties stated that the Offer of Settlement resolves the Complaint.

7. In a July 20, 2006 Order on Complaint and Offer of Settlement,[13] the Commission found that, under the then-current market design, the must-offer obligation does not adequately compensate generators for the reliability services they provide and that the compensation to generators under the must-offer obligation is no longer just and reasonable. However, the Commission was unable to find that the rates and cost allocation mechanism under the Offer of Settlement are just and reasonable. Accordingly, the July 20, 2006 Order set forth three data requests and established paper hearing procedures to review evidence on whether the rates and cost allocation under the Offer of Settlement or some other rates and cost allocation are just and reasonable with respect to the must-offer obligation.

8. In addition, the July 20, 2006 Order permitted each seller of capacity, as defined under the terms of the Offer of Settlement, at its election, to collect the Offer of Settlement rates from the date of this order, so long as such seller agrees that all of these revenues will be subject to refund, even if they are collected after the statutory refund period ends.

9. On September 27, 2006, the Commission issued an Order on Clarification as to the July 20, 2006 Order.[14] The Commission clarified, among other things, that the July 20, 2006 Order implemented the Offer of Settlement rates on an interim basis, pursuant to Rule 602(h) of our regulations,[15] and subject to refund. Moreover, the Commission clarified that, upon approval of appropriate interim tariff sheets, the CAISO would be authorized to implement all of the terms of the Offer of Settlement relating to the sale of capacity and each potential seller of capacity would be authorized to collect the Offer of Settlement rates, if the seller so elected pursuant to the July 20, 2006 Order. The Commission also stated that the interim tariff sheets should include the cost allocation methodologies and all reporting and procedural requirements set forth in the Offer of Settlement. The Commission stated, however, that it was not authorizing the CAISO to implement the provisions in the Offer of Settlement relating to automatic mitigation procedures (AMP) and ancillary services on an interim basis.

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[13] July 20, 2006 Order, *supra* note 1.

[14] September 27, 2006 Order, *supra* note 2.

[15] 18 C.F.R. § 385.602(h) (2006) (Rule 602(h)).

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10. On February 13, 2007, the Commission approved, with modifications, the Offer of Settlement as a just and reasonable outcome for this proceeding.[16] Although the Commission found that the RCST provisions were just and reasonable, the Commission recommended modifying the Offer of Settlement with respect to two secondary provisions relating to AMP and ancillary services.

11. On December 15, 2006, the CAISO submitted, pursuant to FPA section 205, proposed tariff revisions to implement the 2007 cost allocation methodologies for the costs incurred while making 2007 Local and Significant Event RCST designations in Docket No. ER07-326-000. On February 13, 2007, the Commission accepted those amendments which related to the 2007 Local and Significant Event RCST designations, effective January 1, 2007, among other things.[17]

B. Requests for Clarification and/or Rehearing

12. Timely requests for clarification and/or rehearing of the July 20, 2006 Order were filed by the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (collectively, Six Cities) and the CPUC, PG&E and SCE (jointly).

13. Timely requests for rehearing of the September 27, 2006 Order were filed by Six Cities and the City of Santa Clara, California d/b/a Silicon Valley Power (SVP).

14. Timely requests for rehearing of the February 13, 2007 Order on 2007 RCST were filed by Six Cities and SVP.

15. Each of the requests for clarification and/or rehearing are discussed in greater detail in Section II.B, *infra*.

C. Compliance Filings and Responsive Pleadings

16. On October 20, 2006, the CAISO filed a compliance filing as directed by the July 20, 2006 and September 27, 2006 Orders. Timely comments on the compliance

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[16] *Independent Energy Producers Association v. California Independent System Operator Corp.*, 118 FERC ¶ 61,096 (2007) (February 13, 2007 Order on Paper Hearing). The Commission will address requests for rehearing of the February 13, 2007 Order on Paper Hearing (pending in Docket No. EL05-146-004) in a subsequent order.

[17] February 13, 2007 Order on 2007 RCST, *supra* note 3.

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filing were filed by the California Department of Water Resources State Water Project (SWP) and Williams Power Company, Inc. (Williams). On November 28, 2006, the CAISO filed an answer to the comments.

17. On March 15, 2007, the CAISO filed a compliance filing as directed by the February 13, 2007 Order on Paper Hearing. Also on March 15, 2007, the CAISO filed a compliance filing as directed by the February 13, 2007 Order on 2007 RCST. The three compliance filings and related comments are discussed in greater detail in Section II.C, *infra*.

II. Discussion

A. Notice of Filings, Responsive Pleadings, and Procedural Matters

18. Notice of the CAISO's October 20, 2006 compliance filing in Docket No. EL05-146-002 was published in the *Federal Register*, 71 Fed. Reg. 65,094 (2006), with interventions and protests due on or before November 13, 2006. As noted above, timely comments on the compliance filing were filed by SWP and Williams. On November 28, 2006, the CAISO filed an answer to the comments.

19. Notice of the CAISO's March 15, 2007 compliance filing in Docket No. EL05-146-005 was published in the *Federal Register*, 72 Fed. Reg. 14,269-70 (2007), with interventions and protests due on or before April 5, 2007. None was filed.

20. Notice of the CAISO's March 15, 2007 compliance filing in Docket No. ER07-326-002 was published in the *Federal Register*, 72 Fed. Reg. 13,784 (2007), with interventions and protests due on or before April 5, 2007. None was filed.

21. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2006), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the CAISO's November 28, 2006 answer because it has provided information that assisted us in our decision-making process.

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B. Requests for Clarification and/or Rehearing

1. Requests for Clarification and/or Rehearing of the July 20, 2006 and September 27, 2006 Orders

a. Binding Nature of the Offer of Settlement

i. Request for Clarification and/or Rehearing of the July 20, 2006 Order

22. The CPUC, PG&E and SCE request clarification, or in the alternative, rehearing as to whether the July 20, 2006 Order intends to implement the remainder of the RCST settlement terms not addressed in the July 20, 2006 Order. The CPUC, PG&E and SCE argue that the July 20, 2006 Order fails to expressly state which terms of the Offer of Settlement are binding on the Settling Parties. The parties argue that without the implementation of various terms of the Offer of Settlement, the CPUC, load serving entities (LSEs) and generators are not realizing the benefits of the bargain to which they agreed, and for which the LSEs and ratepayers are now paying. The CPUC, PG&E and SCE maintain that the Offer of Settlement only binds the parties if it was implemented in full.[18] The parties argue that the Commission "cannot force parties to accept a materially modified settlement agreement, particularly when the parties have provided that the settlement may terminate if the parties do not agree to such modification."[19] The CPUC,

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[18] CPUC, PG&E and SCE Request for Rehearing of July 20, 2006 at 6 (*citing* Offer of Settlement at 14.1.2). Section 14.1.2 of the Offer of Settlement states:

> If the Commission, in approving this Settlement or by taking any other regulatory action, or if any other regulatory action modifies the Settlement in a manner that materially changes the benefits and burdens negotiated herein, the Settling Parties shall meet and confer as to whether all Settling Parties can agree to the modified Settlement. If all of the Settling Parties do not agree, in writing, to the modified Settlement, then the Settlement and the CAISO Tariff provisions implementing the terms of the Settlement shall terminate, except that the provisions concerning compensation, cost allocation, and settlement will remain in effect until such time as RCST resources have been fully compensated for their services rendered under the RCST prior to the termination of the RCST, and the CAISO has finally allocated and recovered the costs associated with such RCST compensation.

[19] CPUC, PG&E and SCE Request for Rehearing of July 20, 2006 Order at 6.

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PG&E and SCE argue that if the Commission clarifies that the Offer of Settlement is to be implemented with all of its material terms intact, they do not contest the July 20, 2006 Order.

ii. Commission Determination

23. The September 27, 2006 Order clarified which terms of the Offer of Settlement are binding on the Settling Parties.[20] As clarified in the September 27, 2006 Order, and as ultimately approved in the February 13, 2007 Order on Paper Hearing, the Commission did not materially modify the Offer of Settlement. Pursuant to our authority under Rule 602(h), the Commission accepted those provisions that it found to be related to the sale of capacity.[21]

24. In the July 20, 2006 Order, the Commission found it unduly discriminatory that units under the must-offer obligation would be required to operate for reliability purposes in a manner similar to units contracted for capacity under the resource adequacy program and not receive a similar capacity payment.[22] As further explained by the Commission in the February 13, 2007 Order on Paper Hearing, the "primary issue underlying the Complaint was that the Commission-imposed must-offer obligation provided unjust and unreasonable compensation for needed capacity and reliability services."[23] Accordingly, the Commission accepted all provisions of the Offer of Settlement relating to the sale of capacity as filed, including the rules for procuring capacity, the price paid for capacity, and the methodologies for allocating the costs incurred from purchasing capacity. The Commission modified only two provisions that it determined to be beyond the scope of the proceeding.[24] The action taken by the Commission was not a material modification,

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[20] September 27, 2006 Order, 116 FERC ¶ 61,297 at P 14-16.

[21] *See infra* section II.B.1.c.

[22] July 20, 2006 Order, 116 FERC ¶ 61,069 at P 36.

[23] February 13, 2007 Order on Paper Hearing, 118 FERC ¶ 61,096 at P 197.

[24] The Commission determined that the Offer of Settlement tariff provisions relating to mitigation measures and ancillary service dispatch decision were beyond the scope of IEP's Complaint. *See* February 13, 2007 Order on Paper Hearing, 118 FERC ¶ 61,096 at P 187, 197.

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and instead, was appropriate given the issues raised in the Complaint and proposed resolution of the Complaint. Accordingly, we find that the CPUC, PG&E and SCE concerns are moot.

25. Regardless of whether the concerns have been rendered moot, the Commission finds that section 14.1.2 of the Offer of Settlement is not triggered for non-material changes and, as discussed above, we find the modification to be non-material. However, the Commission will not require any party to accept a settlement agreement that such party deems to be materially modified. If the CPUC, PG&E and SCE believe the July 20, 2006 and September 27, 2006 Orders, or even the subsequent February 13, 2007 Order on Paper Hearing, has materially modified the Offer of Settlement to such an extent that the parties no longer believe it provides any benefit, then they may terminate the Offer of Settlement, pursuant to the provisions stated therein.[25]

b. Finding that the Must-Offer Obligation Has Become Unjust and Unreasonable

i. Requests for Rehearing of the July 20, 2006 Order

26. The CPUC, PG&E and SCE argue that the Commission erred in finding that the must-offer obligation has become unjust and unreasonable. The parties argue that because this controversy arose under section 205, the Commission does not have the authority to reject, *post hoc*, a previously accepted tariff provision.[26] The parties argue that because the must-offer obligation was previously deemed to be just and reasonable, the July 20, 2006 Order should have been supported by a demonstration that the must-offer obligation is no longer just and reasonable and a determination that the alternative

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[25] We note, however, that section 14.1.2 of the Offer of Settlement provides that, "the terms of the Settlement shall terminate, *except that the provisions concerning compensation, cost allocation, and settlement will remain in effect until such time as RCST resources have been fully compensated for their services rendered under the RCST prior to the termination of the RCST, and the CAISO has finally allocated and recovered the costs associated with such RCST compensation.*" Offer of Settlement Agreement at § 14.1.2, *supra* note 18 (emphasis added). The Commission believes that the interim imposition of the Offer of Settlement provisions is consistent with this provision.

[26] CPUC, PG&E and SCE Request for Rehearing of July 20, 2006 Order at 9 (*citing ChevronTexaco Exploration & Prod. Co. v. FERC*, 387 F.3d 892 (D.C. Cir. 2004) (*ChevronTexaco*)).

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rate is just and reasonable, pursuant to FPA section 206. The parties maintain that the Commission erred in failing to hold a hearing on whether any alternative rate to the Offer of Settlement was just and reasonable.[27]

ii. Commission Determination

27. Under section 206,[28] the Commission reviews the justness and reasonableness of rates. This is a two pronged review.[29] Under the first prong, the Commission ascertains the justness and reasonableness of an existing rate. If it finds that rate to be unjust or unreasonable then, under the second prong, it must determine what would be just and reasonable. The mere fact that a tariff provision implementing a particular rate was at one time found to be just and reasonable does not preclude the Commission from later reviewing the tariff provision to determine whether it continues to be just and reasonable.

28. The July 20, 2006 Order found, under the first prong of the Commission's section 206 analysis, that the existing tariff provisions were unjust and unreasonable because generators operating under the must-offer obligation were required to make their capacity available to the CAISO without explicitly being provided a mechanism to ensure sufficient fixed costs recovery to keep generation needed for reliability purposes available to the CAISO.[30] The Commission also found that "given the current

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[27] *Id.* at 4.

[28] The Complaint underlying these proceedings was filed pursuant to FPA section 206. It was not filed pursuant to section 205. September 27, 2006 Order, 116 FERC ¶ 61,297 at P 10.

[29] This "bifurcated approach" has been upheld by the courts. *See, e.g.*, *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 583-85 (1942) (permitting the Commission to separate different phases of a ratemaking procedure under section 5 of the Natural Gas Act (NGA)); *ChevronTexaco*, 387 F.3d at 895 (stating that in a NGA section 5 proceeding, "the Commission bears the burden of adducing substantial evidence to prove (1) the pipeline's existing rate is unjust and unreasonable and (2) the rate determined by the Commission is just and reasonable"); *"Complex" Consolidated Edison Co. of New York, Inc. v. FERC*, 165 F.3d 992, 1001 (D.C. Cir. 1999) ("Under [NGA] section 5, the Commission must first establish that the proposed or existing rate is unjust and unreasonable. It is only after this antecedent showing has been made that the Commission properly can illustrate that its alternative rate proposal is both just and reasonable."). NGA section 5 is analogous to FPA section 206.

[30] July 20, 2006 Order, 116 FERC ¶ 61,069 at P 36.

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compensation structure . . . generators under the must-offer obligation may not have sufficient opportunity to recover their fixed costs in the energy market."[31] The Commission instituted additional proceedings, a paper hearing, under the second prong of the Commission's section 206 analysis, to determine the justness and reasonableness of the Offer of Settlement, a proposed resolution of the issues.[32] The Commission also allowed the Offer of Settlement to operate on an interim basis, pending the outcome of the paper hearing procedures.[33] Ultimately, the February 13, 2007 Order on Paper Hearing established a just and reasonable alternative to the original tariff provisions.

29. With respect to the hearing procedures established in this proceeding, the Commission is required to provide a trial-type hearing only if the material facts in dispute cannot be resolved on the basis of the written submissions in the record. The courts have deferred to the Commission with respect to process.[34] In this regard, the Commission is not obligated to hold hearings before an administrative law judge to determine what alternatives may provide a reasonable outcome. Here, the Commission instituted paper hearing procedures to determine whether the Offer of Settlement was just and reasonable. These actions satisfy our statutory responsibility.

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[31] *Id.* P 37.

[32] *Id.* P 41.

[33] *See infra* section II.B.1.c.

[34] The use of a paper hearing rather than a trial-type evidentiary hearing has been addressed in previous cases. *See, e.g.*, *Public Service Co. of Indiana*, 49 FERC ¶ 61,346 (1989), *order on reh'g*, 50 FERC ¶ 61,186, *opinion issued*, Opinion No. 349, 51 FERC ¶ 61,367, *order on reh'g*, Opinion No. 349-A, 52 FERC ¶ 61,260, *clarified*, 53 FERC ¶ 61,131 (1990), *appeal dismissed*, *Northern Indiana Public Service Co. v. FERC*, 954 F.2d 736 (D.C. Cir. 1992). As the Commission noted in Opinion No. 349, 51 FERC ¶ 61,367, at 62,218-19 and n.67, while the FPA and case law require that the Commission provide the parties with a meaningful opportunity for a hearing, the Commission is required to reach decisions on the basis of an oral, trial-type evidentiary record only if the material facts in dispute cannot be resolved on the basis of the written record, *i.e.*, where written submissions do not provide an adequate basis for resolving disputes about material facts. The courts have upheld the Commission's discretion in this regard. *See Central Maine Power Co. v. FERC*, 252 F.3d 34, 46-47 (1st Cir. 2001); *Lomak Petroleum, Inc. v. FERC*, 206 F.3d 1193, 1199 (D.C. Cir. 2000) (*citing Conoco Inc. v. FERC*, 90 F.3d 536, 543 n.15 (D.C. Cir. 1996) (quoting *Environmental Action v. FERC*, 996 F.2d 401, 413 (D.C. Cir. 1993)).

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c. Implementation of the Offer of Settlement Rates on an Interim Basis

i. Requests for Rehearing of the July 20, 2006 Order

30. Six Cities argues that the Commission erred in permitting the immediate implementation of the capacity charge proposed in the Offer of Settlement upon issuance of the July 20, 2006 Order. Six Cities maintains that the FPA and controlling precedent requires that a rate increase proposed under FPA section 206 may only become effective after Commission acceptance of the compliance filing that follows the Commission's final order in the proceeding.[35] Six Cities also notes that the CAISO's August 1, 2006 request for clarification and rehearing of the July 20, 2006 Order demonstrates the confusion resulting from the Commission's interim implementation of the requested rate increase. Six Cities maintains that "[t]his sea of perplexity caused by the Commission's premature implementation of a rate tied to an as yet unapproved Offer of Settlement is precisely what the *Electrical District* court was attempting to avoid by mandating that the rate become effective only after acceptance of a compliance filing."[36] Six Cities asks that the Commission reconsider its July 20, 2006 Order by "reinstat[ing] the CAISO's filed rate until after the hearing process has concluded, the Commission has issued a final order approving revised rates for compensation of must-offer generators, the CAISO has made a compliance filing in response to such order, and the Commission has accepted the compliance filing."[37]

ii. Requests for Rehearing of the September 27, 2006 Order

31. In their request for rehearing of the September 27, 2006 Order, Six Cities reiterate the argument that the Commission erred by prematurely authorizing sellers of capacity in the CAISO market to collect Offer of Settlement Rates on an interim basis. Six Cities argues that the Commission's reliance on its own regulation, Rule 602(h), to supersede

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[35] Six Cities Request for Rehearing of the July 20, 2006 Order at 6-7 (*citing, inter alia*, *Electrical Dist. No. 1 v. FERC*, 774 F.2d 490 (D.C. Cir. 1985) (*Electrical District*); *Public Service Co. of New Mexico v. FERC*, 832 F.2d 1201 (10th Cir. 1987) (*Public Service Co. of New Mexico*); *Kansas Gas & Electric Co.*, 34 FERC ¶ 61,288, at 61,517 (1986)).

[36] *Id.* at 9.

[37] *Id.*

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the clear requirements of the FPA is misplaced and erroneous. Six Cities also argues that reliance on *Arctic Slope Regional Corp. v. FERC*, 832 F.2d 158 (D.C. Cir. 1987) (*Arctic Slope*), which interprets the regulation, is misplaced because that case is distinguishable. Six Cities maintains that *Arctic Slope* "dealt with Commission discretion over its procedures for protecting the rights of non-settling parties" and, moreover, does not override the fundamental terms of section 206.[38]

32. Six Cities further argue that even if the Commission has the authority to permit an interim rate increase, subject to refund, in response to a FPA section 206 complaint, such an interim increase cannot be made effective until the CAISO has filed and the Commission has accepted tariff provisions reflecting the interim increase.

33. Finally, Six Cities maintains that the September 27, 2006 Order creates ambiguity as to when the Commission intends to allow the interim compliance filing to be submitted by the CAISO to become effective. Six Cities maintain that "[i]t is not clear . . . whether the Commission intends to authorize the sellers of capacity to collect rates retroactively from the July 20[, 2006] Order . . . , or whether the sellers are only authorized to collect the new rates starting on the date the Commission approves CAISO's tariff sheets implementing the specified terms of the Offer of Settlement on an interim basis."[39] Six Cities argue that, to the extent the September 27, 2006 Order suggests that an interim increase in payment to must-offer generators may become effective prior to the Commission's acceptance of the CAISO's compliance filing directed by the September 27, 2006 Order, that determination would contradict the precedent previously cited.

34. Similarly, SVP argues that the Commission erred in implementing the Offer of Settlement Rates before those rates had been determined to be just and reasonable and before they were accepted through an approved compliance filing. SVP argues that the Commission erred in its reliance on Rule 602(h)(1)(ii)(B). SVP argues that while the Commission's regulations may allow the Commission to "take appropriate action" if it finds the record does not allow contested issues to be resolved or severed, the action taken here is contrary to the FPA. SVP also argues that the Commission erred in its reliance on *Arctic Slope*, arguing that in this proceeding, unlike *Arctic Slope*, the

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[38] Six Cities Request for Rehearing of September 27, 2006 Order at 11-12.

[39] *Id.* at 13.

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Commission is attempting "to foreclose the resolution of contested issues prior to a paper hearing"[40] and the Commission has not yet made any determination as to the justness or reasonableness of the settlement rates.

35. SVP argues that the September 27, 2006 Order does not adequately respond to the CAISO's August 1, 2006 request for rehearing regarding the "legal infirmity" of the Commission's section 206 analysis.[41] SVP argues that the September 27, 2006 Order implements rates that have not been found to be just and reasonable, authorizes rates that have not been implemented by acceptance of a compliance filing, and implements a settlement that has not yet been approved in violation of section 206 and relevant precedent.[42]

iii. Commission Determination

36. The Commission denies requests for rehearing about the claimed "legal infirmity" of the Commission's section 206 analysis in the July 20, 2006 and September 27, 2006 Orders. This analysis does not "override" the fundamental terms of section 206. The Commission has the authority to set an interim rate order.[43] We do not believe that the "necessary predictability" cited by *Electrical District* is threatened by our decisions in those orders. The purpose of the rule against retroactivity, and the closely related filed rate doctrine, is to ensure predictability. The courts have found that as long as the affected parties have notice, these concerns are satisfied.[44] Under these factual

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[40] SVP Request for Rehearing of the September 27, 2006 Order at 5.

[41] *Id.* at 6.

[42] *Id.* at 7-8 (*citing, inter alia, Enron Power Enterprise Corp.*, 52 FERC ¶ 61,193, at 61,709 (1990); *Electric District*, 774 F.2d at 492-93; *Public Service Co. of New Mexico*, 832 F.2d at 1223-25; *Tarpon Transmission Co.*, 58 FERC ¶ 61,354, at 62,171 (1992); *Trunkline Gas Co.*, 58 FERC ¶ 61,240, at 61,784 (1992).

[43] *See FPC v. Tennessee Gas Transmission Co.*, 371 U.S. 145, 150-52 (1962); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. at 584.

[44] *See NStar Elec. and Gas Corp. v. FERC*, 481 F.3d 794, 801 (D.C. Cir. 2007) (stating "the filed rate doctrine and bar on retroactive ratemaking are satisfied, in keeping with their functions, 'when parties have notice that a rate is tentative and may later be adjusted with retroactive effect, or where they have agreed to make a rate effective retroactively'") (*citing Consolidated Edison Co. of N.Y. v. FERC*, 347 F.3d 964, 969 (D.C. Cir. 2003) (*Con Edison*)); *Exxon Co., U.S.A. v. FERC*, 182 F.3d 30, 49 (D.C. Cir.

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circumstances, parties had sufficient notice of the interim rates. For example, the settlement process itself provided notice of the interim rates to all affected parties. Although not all affected parties were settling parties, non-settling parties were provided notice of and had the opportunity to comment on the settlement principles that resulted in the Offer of Settlement.[45]

37. Moreover, the initiative to provide reliability resources with a compensatory capacity payment was not raised for the first time in the Complaint. The CPUC, Local Regulatory Authorities, the CAISO, and various market participants have participated in a multi-year effort to establish resource adequacy programs that help to address California's reliability needs. We find that the implementation of interim capacity rates under the Offer of Settlement is consistent with these initiatives and our responsibility to ensure just and reasonable rates, terms and conditions of service. Furthermore, as discussed in the February 13, 2007 Order on Paper Hearing, "the RCST payment structure better reflects the costs to these units for providing reliability services and reduces the likelihood that units needed for reliability purposes will be mothballed or shut down and unavailable when needed."[46] Hence, the Commission's decision to implement interim rates was in part based on the need to address potential short-term reliability needs. Accordingly, application of the Offer of Settlement rates on an interim basis until

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1999) (*Exxon*) (finding that "FERC does have a measure of discretion in determining when and if a rate should apply retroactively" although "such discretion is not without its limits"); *OXY USA, Inc. v. FERC*, 64 F.3d 679, 699 (D.C. Cir. 1995) (stating "[t]he goals of equity and predictability are not undermined when the Commission warns all parties involved that a change in rates is only tentative and might be disallowed"); *Public Utils. Comm'n of the State of Cal. v. FERC*, 988 F.2d 154, 163 (D.C. Cir. 1993) (stating "[i]t is not that notice relieves the Commission of the bar on retroactive ratemaking, but that it 'changes what would be purely retroactive ratemaking into a functionally prospective process by placing the relevant audience on notice at the outset that the rates being promulgated are provisional only and subject to later revision'") (internal citations omitted); *Natural Gas Clearinghouse v. FERC*, 965 F.2d 1066, 1075 (D.C. Cir. 1992) (stating the rule does not apply in situations where there is "adequate notice that resolution of some specific issue may cause a later adjustment to the rate being collected at the time of service").

[45] *See* CAISO May 1, 2006 Reply Comments, Docket No. EL05-146-000, at 9-12.

[46] February 13, 2007 Order on Paper Hearing, 118 FERC ¶ 61,096 at P 49.

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the Commission had an opportunity to review parties' submissions in the February 13, 2007 Order on Paper Hearing was an initial step toward remedying the unjust and unreasonable compensation to generators under the must-offer obligation.

38. Moreover, as stated in the September 27, 2006 Order, under Rule 602(h) of our regulations, the Commission has broad authority and discretion to address contested settlements.[47] As in *Arctic Slope*, the Commission made a justness and reasonableness determination in this case – as stated above, the Commission found that it was just and reasonable for the CAISO to provide capacity payments to generators. What the Commission set for paper hearing, however, was the adjustments to the ultimate rate.

39. Further, we note that our approval of the Offer of Settlement rates on an interim basis, will have no adverse effect. Given that the July 20, 2006 Order established rates subject to refund and the February 13, 2007 Order on Paper Hearing has now implemented the rates, parties will be fully compensated for transactions during the interim period.

40. Regarding SVP's concerns about the effective date of the order, we will not revise the finding of the September 27, 2006 Order that each seller of capacity may collect Offer of Settlement rates beginning August 26, 2005, subject to refund.[48] "Courts have recognized only two circumstances in which a rate adjustment may take effect prior to a section 205 filing: when parties have notice that a rate is tentative and may be later adjusted with retroactive effect, or when they have agreed to make a rate effective retroactively."[49] As indicated above, we find that the parties had sufficient notice of the interim rates and, accordingly, the retroactive rate is appropriate.

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[47] September 27, 2006 Order, 116 FERC ¶ 61,297 at P 10. We do not believe that reliance on *Arctic Slope* was in error.

[48] July 20, 2006 Order, 116 FERC ¶ 61,069 at P 41.

[49] *Con Edison*, 347 F.3d at 969-70 ("Neither of these circumstances undermines the twin goals of predictability and equity.") (also *citing Exxon*, 182 F.3d at 49 (noting that "the rule against retroactive ratemaking . . . does not extend to cases in which [customers] are on adequate notice that resolution of some specific issue may cause a later adjustment to the rate being collected at the time of service") and *City of Holyoke Gas & Elec. Dep't v. FERC*, 954 F.2d 740, 744 (D.C. Cir. 1992) (finding FERC's decision to make the rate change effective prior to the filing date proper because the parties had contracted to make rate retroactive and a waiver was not against the public interest)).

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2. Requests for Clarification and/or Rehearing of the February 13, 2007 Order on 2007 RCST

a. Requests for Rehearing

41. Six Cities and SVP contend that the Commission erred by approving amendments to the CAISO Tariff that were not yet lawfully in effect, arguing that a rate increase proposed under FPA section 206 may become effective only after Commission acceptance of the compliance filing that follows the Commission's final order on the section 206 complaint. Six Cities states that even though the Commission issued the February 13, 2007 Order on Paper Hearing on the same date as it approved the CAISO's proposed amendments to the CAISO Tariff in the February 13, 2007 Order on Paper Hearing, the Commission has not yet issued any order approving the tariff sheets to implement the settlement approved in the February 13, 2007 Order on Paper Hearing. Six Cities further states that the Commission unlawfully authorized sellers to collect Offer of Settlement rates prior to any Commission decision regarding the merits of the February 13, 2007 Order on Paper Hearing's terms and cannot have an effective date earlier than the effective date of the tariff provisions that are being amended. SVP adds that approving tariff amendments for tariffs that have not yet been determined as just and reasonable is counter to the Commission's practice and violates the filed rate doctrine.

42. Therefore, according to Six Cities and SVP, the 2007 RCST provisions cannot become effective until after the Commission issues an order approving the CAISO's compliance filing directed in the February 13, 2007 Order on Paper Hearing, concluding that the Commission may not give the 2007 RCST provisions an effective date on January 1, 2007. The parties request that the Commission grant rehearing and order that the amendments become effective no earlier than the date of a Commission order approving the CAISO's filing of tariff pages implementing the Settlement resolved in the February 13, 2007 Order on Paper Hearing.

43. Six Cities and SVP also seek rehearing of the Commission's determination in the February 13, 2007 Order on 2007 RCST that resolution of the RCST issues in Docket No. EL05-146 "moot" the protestors' concern that the proposed 2007 cost allocation methodology is premature. SVP notes that the 2007 RCST provisions are not resolved through the February 13, 2007 Order on Paper Hearing and reiterate that "[a]ny amendments to the RCST tariff provisions must not become effective before the date that the Commission approves the CAISO's compliance filing of tariff pages that first implement the RCST tariff in Docket No. EL05-146."[50]

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[50] SVP Request for Rehearing of the February 13, 2007 Order on 2007 RCST at 7.

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b. Commission Determination

44. We disagree with Six Cities' and SVP's claims that the provisions approved in the February 13, 2007 Order on 2007 RCST may not have an effective date of January 1, 2007. With respect to the "second prong" of the Commission's section 206 investigation, *see supra* P 27, the Commission allowed the Offer of Settlement to be made effective, subject to the outcome of our review under the paper hearing procedures as to the justness and reasonableness of the settlement tariff provisions as a resolution of the Complaint. Consequently, we deny rehearing.

45. However, as stated above and as stated in the February 13, 2007 Order on 2007 RCST, the July 20, 2006 Order implemented the Offer of Settlement rates on an interim basis pursuant to Rule 602(h) of our regulations, but, importantly, the Offer of Settlement did not propose a method for allocating certain RCST costs in 2007.[51] Therefore, the February 13, 2007 Order on Paper Hearing and resulting compliance filing did not address the 2007 allocation of these costs.[52] The CAISO submitted its filing in Docket No. ER07-326-000 to propose tariff revisions to allow for the implementation of cost allocation methodologies for RCST in 2007. Despite Six Cities' and SVP's arguments that the 2007 RCST provisions cannot become effective until after the Commission issues an order approving the CAISO's compliance filing directed in the February 13, 2007 Order on Paper Hearing, the CAISO must have RCST provisions effective at the beginning of 2007 in order to continue implementation of the interim tariff sheets, which have a proposed effective date of January 1, 2007, or the Offer of Settlement, which has a proposed effective date of June 1, 2006, once approved by the Commission. Therefore, contrary to Six Cities' and SVP's claims, the 2007 RCST provisions will not have an effective date earlier than the effective date of the tariff provisions that are being amended. If no 2007 RCST cost allocation provisions had been approved, implementation would cease at the beginning of 2007.

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[51] September 27, 2006 Order, 116 FERC ¶ 61,297 at P 22.

[52] *Id.*

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C. Compliance Filings

1. Compliance Filings in Docket No. EL05-146

a. October 20, 2006 Compliance Filing (Interim Tariff Sheets)

i. Compliance Filing

46. On October 20, 2006, the CAISO submitted tariff sheets to comply with the September 27, 2006 Order (Interim Tariff Sheets). The CAISO states that the tariff sheets reflect the provisions of the Offer of Settlement that the Commission has approved for implementation on an interim basis. The CAISO further states that the tariff sheets do not include the provisions regarding AMP or those concerning ancillary services. The CAISO explains that the tariff sheets are based on the *pro forma* tariff sheets filed with the Offer of Settlement, with modifications to reflect the following:

> (1) the fact that … there will not be any 2006 forward local RCST designations; (2) other language changes resulting from the removal of the 2006 local RCST tariff provisions; (3) compliance with the directives in the July 20 and September 27 Orders; (4) elimination of the AMP and RMR Condition 2 provisions; and (5) certain clean-up changes.[53]

The CAISO also explains that, consistent with the Commission's findings in the September 27, 2006 Order, it has not included in the compliance filing any of the provisions from the Offer of Settlement pertaining to the 2006 local RCST designations and that the elimination of these provisions has required some wording changes to other sections of the *pro forma* tariff language.

47. Moreover, the CAISO states that the proposed tariff sheets bear effective dates of July 20, 2006, in compliance with the directive in the July 20, 2006 Order that each seller of capacity, at its election, may collect the Offer of Settlement rates from the date of the July 20, 2006 Order (so long as the seller agrees that all of these revenues will be subject to refund).

ii. Protests

48. Williams states that proposed tariff section 43.5.1 provides that any "undesignated" capacity from a unit that also provides RCST capacity must offer

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[53] CAISO October 20, 2006 Compliance Filing, Docket No. EL05-146-002, at 3.

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ancillary services. Williams notes that section 4.3 of the Offer of Settlement only provides that RCST capacity must offer ancillary services to the extent capable.[54] Williams argues that the CAISO's compliance filing is beyond the scope of the Offer of Settlement because it attempts to implement additional offering obligations. Moreover, Williams states that if the CAISO does not intend to partially designate units as RCST, the offering obligation is superfluous because there would be no undesignated capacity on an RCST unit. Accordingly, Williams asserts that the Commission should direct the CAISO to revise proposed tariff section 43.5.1 so that it is consistent with the Offer of Settlement.

49. In its protest, SWP states that it preserves its protests and all objections previously proposed in this proceeding.

50. SWP asserts that no previous tariff filing compliant with FPA section 205 has been made with respect to the tariff language the CAISO now proposes to make effective as of July 20, 2006. SWP points out that the tariff language in question had been appended not for filing, but rather for illustrative purposes, to the Offer of Settlement "that was widely opposed and was not found to be just and reasonable."[55] SWP submits that the tariff language requires close scrutiny, noting that it contains errors. Specifically, SWP argues that the reference to tariff section 43.9 in the definition of "Must-Offer Capacity Payment" and in proposed tariff section 40.14 is in error because no section 43.9 exists in the proposal or in the currently posted the CAISO Tariff. SWP also argues that a new, unexplained and undefined acronym "SCRA" appears in the proposed tariff section 43.8.

51. Additionally, SWP argues that "the extreme complexity of the proposed Must-Offer Capacity Payment—and the extreme opacity of the tariff language purporting to describe it" is of great concern.[56] SWP submits that the Commission should order the CAISO to clarify and correct the tariff provisions submitted in CAISO's compliance filing.

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[54] Williams November 13, 2006 Protest, Docket No. EL05-146-002, at 3 (*citing* Offer of Settlement at § 4.3 ("Once designated, RCST capacity must offer Ancillary Services to the extent capable")).

[55] SWP November 13, 2006 Protest, Docket No. EL05-146-002, at 2.

[56] *Id.* at 3.

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52. Finally, SWP asserts that if the Commission grants a July 20, 2006 effective date, it should enforce all tariff provisions from that date. Specifically, SWP asks that the Commission direct the CAISO to comply with each of the reporting requirements set forth in proposed sections 40.15 and 43.6 from July 20, 2006 forward.

iii. Answer

53. In its November 28, 2006 answer to protests, the CAISO asks that the Commission accept the compliance filing but with the minor modifications it proposes in response to protests and comments. First, the CAISO states that it does not object to Williams' modification to proposed section 43.5.1 to make clear that "once RCST capacity has been designated, that RCST capacity must offer Ancillary Services to the extent capable."[57]

54. Second, the CAISO agrees with SWP that references to "section 43.9" of the tariff are in error. The CAISO states that the Commission should direct the compliance filing be amended to correct the reference to section 40.14.

55. Third, the CAISO explains that the undefined term "SCRA" cited by SWP is actually "SC-RA Entity," which is defined in section 2.2.2(a) of the Offer of Settlement. The CAISO states that the Commission should direct the compliance filing be modified to add the definition of "SC-RA Entity" to Appendix A of the tariff.

56. Fourth, as to SWP's concern about the effective date of reporting requirements, the CAISO states that it proposed an effective date of July 20, 2006 for all provisions of the compliance filing and agrees that the Commission should make the reporting requirements (and the rest of the provisions) effective as of July 20, 2006.

57. Finally, the CAISO argues that SWP's concerns about the Must-Offer Capacity Payment provisions are without merit, arguing that its Must-Offer Capacity Payment Tariff provisions are not difficult to understand or comply with.

b. March 15, 2007 Compliance Filing (Paper Hearing Tariff Sheets)

i. Compliance Filing

58. On March 15, 2007, the CAISO submitted tariff sheets to comply with the February 13, 2007 Order on Paper Hearing (Paper Hearing Tariff Sheets). The CAISO

[57] CAISO November 28, 2006 Answer, Docket No. EL05-146-002, at 2.

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states that the proposed tariff revisions are consistent with the Interim Tariff Sheets filed on October 20, 2006 except for certain exceptions laid out below.

59. First, sections 34.1.2.1.1 and 40.14 have been revised to remove language regarding notice and refund because the charges would no longer be effective on an interim basis.

60. Second, section 43.5.1 was revised to "more accurately reflect the language in the Offer of Settlement regarding the obligation of Eligible Capacity designated as RCST to offer Ancillary Services."[58] The CAISO states that this change is consistent with that requested by Williams in its protest of the October 20, 2006 Compliance Filing and agreed to by the CAISO in its answer to that protest.

61. Third, the proposed tariff sheets were revised to reflect a June 1, 2006 effective date, as required by the February 13, 2007 Order on Paper Hearing.

62. Fourth, the proposed tariff sheets include the changes requested by SWP in its protest of the October 20, 2006 Compliance Filing and agreed to by the CAISO in its answer to that protest. The proposed tariff sheet corrects the erroneous references to "section 43.9" in the October 20 Compliance Filing and replaces them with references to "section 40.14." The proposed tariff sheets also replace the undefined term "SCRA" with "SC-RA Entity" and incorporate the definition of "SC-RA Entity" from section 2.2.2(a) of the Offer of Settlement into Appendix A of the tariff.

63. Finally, the CAISO states that proposed clean Tariff Sheet Nos. 515 and 515A, as part of the October 20, 2006 Compliance Filing, failed to account for revisions to its Low Voltage Transmission Revenue Requirements accepted by the Commission in Docket No. ER06-1395-000. The proposed tariff sheets correct that language.

c. Commission Determination

64. We accept the Paper Hearing Tariff Sheets as filed to be effective on June 1, 2006, and we reject the Interim Tariff Sheets as moot. The Paper Hearing Tariff Sheets modify the Interim Tariff Sheets in two regards. First, the Paper Hearing Tariff Sheets include tariff language modifications as requested by protestors. Second, the Paper Hearing Tariff Sheets establish an earlier effective date for all relevant tariff provisions included in the Interim Tariff Sheets. We accept the Paper Hearing Tariff Sheets as compliant with the February 13, 2007 Order on Paper Hearing and consistent with prior orders in

[58] CAISO March 15, 2007 Compliance Filing, Docket No. EL05-146-001, at 3.

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this proceeding. We reject the Interim Tariff Sheets as moot since those proposed sheets have been superseded by the Paper Hearing Tariff Sheets filed in compliance with the February 13, 2007 Order on Paper Hearing.

65. Finally, with respect to SWP's concern in response to the Interim Tariff Sheets regarding the clarity of the proposed Must-Offer Capacity Payment Provisions, we disagree. We find the proposed tariff language to be consistent with the proposed provision under the Offer of Settlement and therefore, will not require additional revisions.

2. Compliance Filing in Docket No. ER07-326 (2007 RCST Tariff Sheets)

a. March 15, 2007 Compliance Filing

66. On March 15, 2007, the CAISO submitted tariff sheets to comply with the February 13, 2007 Order on 2007 RCST (2007 RCST Tariff Sheets). As required by that order, the CAISO has modified section 43.2.1 to clarify that if the information regarding Local Resource Adequacy Requirements has already provided to the CAISO, it need not be provided again. Section 43.2.1 was also revised to correct a inadvertent reference to a "Local Reliability Authority" rather than a "Local Regulatory Authority."

b. Commission Determination

67. The CAISO's proposed tariff modifications are consistent with the Commission directives in the February 13, 2007 Order on 2007 RCST and, accordingly, we accept the 2007 RCST Tariff Sheets effective on January 1, 2007.

The Commission orders:

(A) The requests for clarification and/or rehearing of the issues discussed above are hereby rejected, as discussed in the body of this order.

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(B) The CAISO's Interim Tariff Sheets are hereby rejected as moot and the CAISO's Paper Hearing Tariff Sheets and 2007 RCST Tariff Sheets accepted for filing, effective June 1, 2006 and January 1, 2007, respectively, as discussed in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.