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DEC 2003 RECEIVED

Mr. Tom Carter
Operations Manager
Western Area Power Administration
Sierra Nevada Region
Parkshore Drive
Folsom, California 95630-4710

Subject: SVP Comments on Western's Federal Register Notice dated December 2nd, 2003 at page 67417.

Tom:

The City of Santa Clara, doing business as Silicon Valley Power (SVP), respectfully submits comments in response to the filing, by Western Area Power Administration, Sierra Nevada Region (Western) in the Federal Register Notice dated December 2nd, 2003 (Vol. 68, No. 231) wherein Western gives notice of its proposed decision to implement a contract-based sub-control area within either the CAISO or SMUD control area. SVP appreciates the opportunity to comment in this Federal Register Notice process.

SVP provides reliable, economical retail electricity service to 46,000 customers in the heart of Silicon Valley, including such leading companies as Intel's World Headquarters, Advanced Micro Devices, National Semiconductor, and many more. Through its membership in the Transmission Agency of Northern California (TANC), SVP is a part owner of the 500-kV California-Oregon Transmission Project (COTP). As a Preference Power customer in Western's Sierra Nevada Division, SVP also has an interest in the 500-kV PACI transmission lines. Western's power deliveries are an important part of SVP's power portfolio.

SVP is pleased that Western has issued its Proposed Decision in its effort to select an alternative for its post-2004 operations. We strongly support Western's continued control of its generation and transmission system, which we believe is essential to meeting the legislative requirements of the Central Valley Project (CVP). The CVP is a crucially important resource for Western's Project Use, First Preference and Preference customers:

1500 Warburton Ave.
Santa Clara, CA 95050
Ph: (408) 261-5292
Fax: (408) 249-0217

As Western considers its contractual relationships with different Control Areas, SVP suggests the following minimum requirements:

1. Contracts must be durable and not subject to unilateral modifications.

2. Western's retention of its physical firm transmission rights is essential in order to meet its obligations to its water and power customers. Western must retain its ability to use, manage and sell excess transmission consistent with OASIS principles. Western should not turn over control of its transmission in return for financial rights to transmission that require (CRRs) to manage congestion risks.

3. Western must retain rights to physically self provide ancillary services and to meet its water and power customers' ancillary service obligations in accordance with WECC standards and consistent with its post-2004 Marketing Plan. Western's scheduling of ancillary services must not be subject to counter-flow congestion charges that result from obligation type CRRs.[1]

4. Western should establish a contractual relationship with a Control Area that:

   a. Has sufficient operating reserves and would not subject its customers to expensive real-time procurement strategies.

   b. Utilizes accurate and timely settlement practices to minimize credit risk.

   c. Follows the standard scheduling timelines and protocols consistent throughout the WECC region and does not create the sort of seams issue evidenced between CAISO and the rest of the Western Region.

   d. Utilizes proper emergency management procedures that do not enable a party to shift the burden of load shedding or financial consequences due to resource inadequacy to other parties that are adequately resourced. Procedures for emergency resource sharing must be established with all parties.

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[1] The ISO's proposal for mitigating congestion price uncertainty only offers greater uncertainty. To hedge spinning reserve needs Western would need to obtain an obligation CRR hedge to financially cover the delivery risk. However, since energy is not actually flowing Western would still be subject to counter flow congestion charges. Managing the CAISO's proposed obligation CRRs will be a difficult and risky task. In fact obligation CRRs introduce a new risk to their owners., If there is congestion in the opposite direction of the obligation CRR rights and if the owner is using less than the contracted amount, the owner would be obligated to pay for congestion on the unused amount! Western should not accept the risks associated with such an obligation upon a capacity-constrained hydro system and its loads. SVP points out that this risk could be virtually eliminated if option-type CRRs were allocated to load instead of the proposed burdensome obligation-type CRRs. SVP has voiced its preference for an ISO allocation of option CRRs followed by an auction of obligation CRRs, but the ISO has apparently decided otherwise. Another concern in the ISO's present MD02 proposal is that phantom congestion can be created by the ISO's own actions, which requires generation to be hedged with risky obligation CRRs even when there is no real congestion and even if the generation is within the owner's service territory.

e. Has an advisory process that is transparent, balanced, inclusive and representative of all entities involved.

f. Has reasonable administrative overhead costs managed through an advisory committee in accordance with the Control Area budget process.

g. Is WECC-certified.

5. Western must ensure that its costs for operating as a sub-control area are reasonable, stable and allocated consistently with cost-causation principles and in accordance with Reclamation Law, which prohibits imposing discriminatory rates on non-direct connected Project Use, First Preference and Preference customers.

6. Any alternative must allow for the COTP, PACI and all other Western assets to be operated and fully utilized in a reliable and cost effective manner.

7. Western must maintain rate stability and ensure that its contracts are not devalued by the CAISO's constantly morphing tariff.

SVP agrees with Western's *initial* cost/benefit analysis that concluded that the formation of a Control Area was the most durable and cost-effective alternative. Western's current Proposed Decision reiterates that the formation of a Control Area is the only alternative that will meet all of the evaluation criteria. Preference customer support for Western is evidenced through contributions of $19 million dollars in fiscal years 2002 through 2004. This support has assisted Western in its development of a the Control Area alternative consistent with the preparation of the post-2004 Marketing Plan. SVP strongly encourages Western to form its own Control Area in order to continue to meet the requirements of the CVP system. SVP supports Western's pursuit of a contract based sub-control area as a first step towards establishing an independent Control Area. SVP cannot overemphasize how important it is for Western to distance itself from CAISO control.

SVP appreciates Western's candor in rebutting the CAISO's specious argument that another control area would reduce reliability in the Western Region. The Western Electricity Coordinating Council (WECC) and the North American Electric Reliability Council (NERC) are the responsible entities for maintaining reliability in Western Region electric systems and any proposed control area must pass their review.

In fact the CAISO has had to deal with reliability issues of it own. As an example, the CAISO violated reliability standards in the aftermath of the incident at Vincent Substation on March 21st 2003, that resulted in the loss of three 500/220 kV transformers, five 500kV transmission lines and eight 220 kV transmission lines. Interestingly, the only loss of load was California Department of Water Resource's (CDWR) pumping load. The CAISO, in a memo dated October 28th, 2003, acknowledged that the manner in which they dispatched generation during the open loop configuration resulted in unscheduled power flows over the eastern portion of the WECC grid, thereby imposing unanticipated burdens on several other control areas. It is a violation of WECC guidelines to burden other control areas unnecessarily. The CAISO's response to this situation was, "To foresee [that] this ramping issue would cause USF when the WECC loop was open at Vincent is asking for control areas to establish procedures for events that are not considered credible."

Further evidence of the CAISO's hubris is its refusal to establish an independent board as ordered by FERC.

Western's proposed alternatives do not *create* complexity as the CAISO states. On the contrary, it is the CAISO's presence and actions that complicate the electric system in California and the Western Region. We commend Western's efforts to achieve a post-2004 operating environment that does not reduce reliability in the WECC region nor negatively impact the CVP's operations with regard to the criteria of flexibility, certainty, durability, operating transparency, and cost-effectiveness.

SVP is confident that regardless of which alternative Western chooses the WECC and NERC review processes will ensure a safe and reliable transition.

In its filing, Western clearly identifies how it perceives each alternative will impact its post-2004 operations with regard to the above criteria.

Federal Control Area Alternative

SVP cannot overstate the importance of Western's continuing its efforts to form its own Control Area. The Federal Control Area clearly meets all of the above criteria and would guarantee Western's control over its own resources and allow them to be managed consistent with Federal law. As a first step toward these objectives, SVP cautiously supports Western's decision to pursue a contract-based sub-control area within either the ISO or SMUD control area. However, SVP does have specific concerns with respect to certain of the alternatives being considered by Western.

PTO Alternative

Flexibility:

SVP disagrees with Western's evaluation that the PTO alternative meets the flexibility criterion. This alternative would bind Western to the ISO for a minimum of two years, on account of the mandatory two-year termination notice. Forcing Western to remain under the ISO's control for two years after seeking termination could result in substantial litigation expense if the termination was not amicable. A shorter termination notice would reduce these risks and enable Western to join a FERC approved RTO in the future. SVP wishes to emphasize the distinction between the six-month disengagement period under an MSS agreement and the two-year disengagement under the PTO alternative underscoring the undesirability of the PTO alternative.

Certainty:

The CAISO tariff offers no cost certainty. The CAISO produces a tariff amendment every five-weeks on average. The CAISO also is not accountable for its expenditures. SVP and Western have decades of experience in scheduling generation to load over physical transmission. The CAISO seeks to convert traditional firm transmission rights to CRRs, also known as virtual (or financial) transmission rights. These rights essentially provide no guarantee of energy delivery but purport to keep the holder financially whole if there is insufficient transmission capacity. CRRs introduce uncertainty as to whether the energy will actually flow and also brings rate uncertainty due to the complex risks associated with the CAISO's proposed use of obligation-type CRRs.

Durability:

In SVP's view, any relationship with the CAISO fails to meet the durability criterion. Any relationship governed by the CAISO tariff exposes Western to unilateral modifications to its contract. The CAISO's scheduling timelines and protocols are also not consistent with industry standards in the WECC region, which creates serious seams issues.

Operating Transparency:

The CAISO has repeatedly shown its unwillingness to share important information with stakeholders. As an example, SVP and other entities have repeatedly requested access to the CAISO Locational Market Price (LMP) modeling software in order to assess the impact that the CAISO's proposed LMP market will have on our systems. Yet the CAISO has thus far refused to grant this access. Because of its technical status as a private corporation, the CAISO is also not subject to the Brown Act nor to the Public Records Act. Any relationship with the CAISO will always have unknown future impacts as they redesign their marketplace in a shroud of secrecy.

Cost Effectiveness:

The CAISO's costs are very high while it provides no demonstrable benefits, let alone benefits that are commensurate with its costs. SVP urges Western to insist that the CAISO keep any cost shifts to a minimum and that all charges by the CAISO for its services be based on cost causation principles.

SVP concurs with Western's conclusion that the PTO alternative is not viable for post-2004 operations. SVP believes that the PTO alternative fails with respect to all of the criteria mentioned above.

Metered Subsystem Alternative

SVP is currently in a Metered Subsystem (MSS) agreement with the CAISO. While SVP considers the MSS a modest success after 16 months of operations, its durability, certainty and cost-effectiveness remain in doubt on account of the MSS agreement's subjection to the unilateral modification under the CAISO tariff.

Contract-Based Sub-Control Area Alternative

Western's proposed decision to implement a contract-based (e.g. non-CAISO tariff based) sub-control area within either the CAISO or SMUD control area offers some potential to protect Western's customers from the CAISO's continuously rising costs, endless tariff amendments and further risks inherent in having a PTO or MSS relationship with the CAISO. Most importantly, this alternative would allow Western to continue its effort to form its own Control Area.

This alternative would allow Western to maintain control over its resources and enable it to invest in long term resource and transmission planning as well as enabling it to serve its water and power customers consistent with Federal Law. SVP places great importance on maintaining a stable operating environment while the industry undergoes broad changes. Therefore, SVP appreciates and supports Western's efforts as it strives to uphold control over its resources and maintain a voice in its future.

In particular, SVP supports Western's proposal to establish a contract based sub-control area within the SMUD control area, as this may well provide a workable alternative to the CAISO. SVP is confident that having alternatives increases the likelihood of Western being able to negotiate and achieve its five stated evaluation criteria mentioned above. SVP is concerned that the CAISO lacks a history of negotiating the sort of contract-based agreements of which Western seeks. A successful contract-based sub-control area must not be subject to the CAISO tariff.

SMUD has successfully and reliably formed a reliable, WECC-certified control area along side the CAISO. It is clear, through our longstanding relationship with SMUD, that it has an appreciation of the foundational concerns listed in Western's five-stated criteria. It is our experience that SMUD understands operating on a *true* cost basis, whereas the CAISO does not. SMUD appears to understand cost causation principles, as opposed to spreading all costs regardless of the justness and reasonableness of the expense. In summary, CAISO participation is outrageously expensive without commensurate benefits. It is most important that Western insulate itself as much as possible from the unstable CAISO world.

SVP further urges Western to consider the litigation costs associated with doing business with the CAISO. If Western finds itself in a relationship with the CAISO, it will most likely be in the unenviable position that many CAISO ratepayers find themselves today: funding their own massive litigation expenses as well as those of the CAISO through the CAISO's rates and charges. The burden and expense of defending oneself from a constant onslaught of tariff amendments must be avoided and a non-tariff based contractual agreement is necessary to achieve this end. Establishing a sub-control area within the SMUD control area offers the best way to avoid the burden of excessive tariff-related litigation.

No Action Alternative

This alternative will not meet any of the five-stated criteria mentioned above. It is most important for Western to implement one of the other alternatives prior to December 31, 2004 in order to avoid this unacceptable outcome.

Time is Critical

Western should enforce a strict timeline while soliciting SMUD and the CAISO for a contract-based sub-control area relationship. SVP suggests the following timeline to accomplish this end:

1. Define the specific criteria needed to meet all statutory obligations and preference customer needs by January 2, 2004.

2. Commence negotiations simultaneously with SMUD and the CAISO.

3. Assess the status of negotiations by January 25, 2004 to determine which entity is most likely able to meet Western's needs regarding a cost-based sub-control area.

4. Complete negotiations and be prepared to sign a sub-control area Letter of Commitment by February 29, 2004.

5. File with WECC for a Federal Control Area by February 1, 2004.

6. Execute a comprehensive sub-control area agreement by April 1, 2004.

7. Implement sub-control area and run parallel with Western's existing system by August 1, 2004.

SVP strongly recommends that Western continue its pursuit of a federal Control Area formation to ensure an alternative in the event that sub-control area negotiations with either party are unsuccessful.

Sincerely,

JHPope

James H. Pope
Director of Electric Utility