

agreement. Because of the 6-month notice requirement, the effective date of the termination is not immediate. In the interim, as an MSS, Western and Reclamation would need to conform their business practices to the extent not precluded by Federal law.

If the ISO is certified by the Commission as an RTO, any changes that the ISO would need to make as a result of its new role would presumably be incorporated in its tariff. Western could choose to either undertake the necessary changes in its business processes or choose to terminate the MSS agreement. As with the PTO Alternative, because of a specific notice requirement (several existing MSS agreements have a 6-month termination notice requirement) the effective date of the termination is not immediate. In the interim, as an MSS, Western and Reclamation would need to conform their business practices to the extent not precluded by Federal law.

Since Reclamation is not required to sign a PGA under the MSS agreement, to the extent that Reclamation chooses not to be party to Western's MSS agreement, potential concerns may arise from liability that Western could incur from the lack of a contractual relationship between the ISO and Reclamation. For example, as the control area operator, the ISO could direct that certain generators undertake specific actions. To the extent that such actions are inconsistent with the project authorization for the CVP, or other Federal law or regulation, Western would need to negotiate exceptions to take care of Federal legal and jurisdictional issues. The specific terms and conditions relating to the ISO's operational jurisdiction over Federally-owned generation and transmission facilities would need to be carefully evaluated to assure that, as the result of implementing this alternative, the authorized project purposes of the CVP would not be impaired.

Because the MSS Alternative specifically requires Western to define its physical boundaries, it provides future flexibility to move its system intact to another control area or an RTO. While Western is under an MSS arrangement, any operating changes necessitated by NERC and WECC would presumably be translated into ISO Tariff revisions or operational protocol changes.

Since Western would have its boundaries formed under the MSS Alternative, Western believes that this alternative provides for short-term and long-term flexibility, restricted only by the termination provisions of the MSS agreement. However, the MSS

Alternative could create business uncertainty and unforeseen impacts for off-system Western customers should Western decide it would need to terminate its MSS agreement. Since the MSS participant continues to retain its ability to provide a notice to terminate the MSS agreement at its discretion, Western concludes that this option meets the flexibility criteria.

Evaluation of the Certainty Criteria Under the MSS Alternative

The MSS Alternative provides participants the ability to avoid some ISO charges because the ISO will base its charges on net flows into the MSS, not gross flows as under the PTO option. The ISO indicated charges for power deliveries to off-system customers would be based on "cost causation" principles that would recover the cost for providing the product or service. Western interpreted this statement to mean that individual customers would be charged for power deliveries based on their use of the ISO grid. Some commentors have raised questions related to the meaning of "cost causation." For instance, the TPUD commented:

During the July 30 hearing, the Cal ISO's use of the term "cost causation" was illustrative of their mind set. This term should not be confused with "cost based" as it seemed the Cal ISO wanted to imply. Cost based charges are based on the cost to provide a service. "Cost causation" is an attempt to appropriately divvy up whatever charges a particular provider can get away with under whatever the "Market" rules are at the time.

The TID commented on the cost basis for rates under a Federal control area and said:

Under an alternative CAISO approach, the cost of transmission from generation to load will be set by a market that cannot be forecast with any certainty. Although there may be ways to partially hedge the uncertainty, there are costs associated with the hedges and hedges are not perfect.

The ISO is in the midst of implementing new operating guidance for its MD02 initiative. The proposed new initiative would implement the concept of locational marginal pricing as a means to deal with congestion of transmission pathways. If MD02 is implemented in its current format during periods of congestion, the ISO would re-dispatch all generation based on economic factors. Under this alternative, affected CVP Preference Power customers and the Project Use loads could end up paying a different price than the actual cost-of-service rates associated with Federal hydropower resources. These rates may

not be consistent with Reclamation law and policy and Western may need to consider mitigation strategies. Unlike the PTO Alternative, where all CVP Preference Power customers are potentially impacted, under this alternative, those Preference Power customers and Project Use loads, which are contained within Western's interconnected generation and transmission system (known as the bubble), may be able to mitigate some of these impacts.

Under the MSS Alternative, Western and its customers would avoid certain ISO charges. Although Western views the MSS Alternative as providing some relief from ISO charges, to the extent that some of these charges continue to be market-based and subject to changes from tariff amendments, the MSS Alternative continues to present business risk and uncertainty. Notwithstanding a contractual agreement, Western would need to conform its business practices every time the ISO Tariff is revised. Although the MSS Alternative provides some relief from costs, to the extent that the charges are subject to potential ISO Tariff revisions and the differential MD02 impacts between the direct and non-direct connected Preference Power and Project Use loads, Western determined that this alternative almost meets the certainty criteria.

Evaluation of the Durability Criteria Under the MSS Alternative

In general, operating business protocols and practices are established and defined by the agreements which create the relationship. These agreements establish obligations and responsibilities of the parties and allocate the burdens and benefits of each business relationship. In a contractual relationship, these practices and procedures are established for the duration of the agreement and normally allow the parties to modify parts of the agreement over time to properly account for any significant changes in the benefits and burdens that may be experienced by either party.

Under the MSS option, although the relationship between Western and the ISO will be based upon an agreement entered into between the parties, because the ISO's business operating protocols and procedures are tariff based, and not contract-based, the terms, conditions, rates, and other pertinent aspects of interacting with the ISO can be changed through new ISO Tariff amendments. Notwithstanding a contractual agreement, Western would need to conform its business practices every time the ISO Tariff is revised. In