

April 2, 2012

The Honorable Kimberly D. Bose
Secretary
Federal Energy Regulatory Commission
888 First Street, NE
Washington, DC 20426

**Re: California Independent System Operator Corporation
Docket No. ER12-760-001
Compliance Filing for Tariff Amendment Regarding Penalty
Cost Allocation Procedure**

Dear Secretary Bose:

As directed in the Commission's March 2, 2012 Order¹ in the above-referenced proceeding, the California Independent System Operator Corporation (ISO) submits this compliance filing to revise its tariff to include provisions relating to penalty cost allocation procedures.

I. Background

On January 4, 2012, the ISO filed a proposed tariff amendment to include penalty allocation procedures in its tariff addressing the procedures the ISO would follow when seeking Commission approval, on a case-by-case basis, for the allocation of the cost of any monetary penalties that may be imposed upon the ISO by the Commission, the North American Electric Reliability Corporation (NERC), the Western Electric Coordination Council (WECC), or any other regulatory body for either reliability-related violations or other violations. This filing sought to implement guidance on penalty allocation procedures that had been provided by the Commission in several orders, including its Order Providing Guidance on Recovery of Reliability Penalty Costs by Regional Transmission Organizations and Independent System Operators ("Guidance Order")² and

¹ *California Independent System Operator Corporation*, Order Accepting in Part and Rejecting in Part Tariff Revisions and Directing Compliance Filing, 138 FERC ¶ 61,156 (2012) ("March 2, 2012 Order").

² *Reliability Standard Compliance and Enforcement in Regions with Regional Transmission Organizations or Independent System Operators*, 122 FERC ¶ 61,247 (2008).

subsequent orders addressing penalty allocation amendments made by other ISOs/RTOs.

In the March 2, 2012 Order, the Commission accepted in part and rejected in part the ISO's proposed tariff amendment and directed the ISO to make a compliance filing within 30 days implementing the Commission's order.³ The Commission accepted without further modification the subsection of the ISO's tariff amendment (subsection 14.7.2) addressing direct allocation of the cost of penalties involving reliability standards violations.⁴ The Commission, however, did not accept subsections 14.7.1 or 14.7.3.1 as filed because those subsections included provisions related to indirect allocation of non-reliability-related monetary penalties imposed by either the Commission or other regulatory bodies. The Commission held that those provisions were beyond the scope of the Guidance Order and thus should not be adopted.⁵ Accordingly, the Commission directed the ISO to revise those subsections to exclude non-reliability-related penalties from its allocation procedure and to revise the tariff headings to reflect that exclusion.⁶

II. Summary of Revisions

Consistent with the March 2, 2012 Order, the ISO's compliance filing makes four revisions to the proposed tariff language previously submitted in the January 4, 2012 filing. The first two revisions are to the headings for section 14.7 and subsection 14.7.3. In both headings, the ISO adds the words "Reliability-Related" in order to make clear that the tariff amendment does not address allocation of non-reliability-related monetary penalties. In order to keep the two headings within the applicable 60-character limit for tariff headings, the ISO has also made further non-substantive edits to each heading to make it more succinct. The other two revisions are to subsections 14.7.1 and 14.7.3.1. In both subsections, the ISO removes the language that made reference to allocation of non-reliability-related monetary penalties. The ISO has also added the words "reliability-related" immediately before the word "penalties" in subsection 14.7.3.1. These revisions make clear, as directed by the March 2, 2012 Order, that the procedures for penalty allocation set forth in this amendment exclude non-reliability-related monetary penalties imposed by the Commission or another regulatory body.

³ March 2, 2012 Order, PP 1, 15-17, and ordering paragraphs (A), (B). The Commission held that the tariff amendment would be effective March 5, 2012, subject to the compliance filing directed therein. *Id.* at P 1.

⁴ March 2, 2012 Order, P 16.

⁵ *Id.* at PP 15, 17.

⁶ *Id.* at P 17.

III. Materials Provided in this Compliance Filing

In addition to this transmittal letter, this compliance filing includes the following attachments:

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|--------------|---|
| Attachment A | Clean ISO tariff sheets reflecting the revisions described in Section II of this transmittal letter |
| Attachment B | Proposed tariff revisions in black-line format |

IV. Conclusion

The ISO requests that the Commission accept this filing as complying with the directives set forth in the March 2, 2012 Order. Please contact the undersigned with any questions regarding this matter.

Respectfully submitted,

By: /s/ Burton Gross

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CERTIFICATE OF SERVICE

I hereby certify that I have served the foregoing document upon the parties listed on the official service lists in the above-referenced proceedings, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, California this 2nd day of April, 2012.

Anna Pascuzzo

Anna Pascuzzo

California Independent System Operator Corporation

Fifth Replacement FERC Electric Tariff

Attachment A - Clean Tariff

Penalty Payment Allocation Compliance Filing

April 2, 2012

14.7 Allocation of Reliability-Related Penalty Costs

14.7.1 Overview of Process

Under the NERC Functional Model and the NERC Rules of Procedure, Registered Entities for a specific function, including the CAISO, may be assessed monetary penalties by FERC, NERC, and/or WECC for violations of one (1) or more NERC Reliability Standards applicable to that function. This Section 14.7 sets forth the procedure through which the CAISO may seek, with FERC approval, to directly allocate, in whole or in part, the cost of any such penalties assessed upon the CAISO to an entity or entities whose conduct or omission(s) NERC, WECC and/or FERC has determined contributed, in whole or in part, to the violation that gave rise to the penalty. This Section 14.7 also sets forth procedures through which the CAISO may seek, with FERC approval, to recover, in whole or in part, from Market Participants the cost associated with a monetary penalty for a NERC Reliability Standards violation(s) that is not subject to direct allocation. Penalties that are assessed upon the CAISO and become final on or after the effective date of this Section 14.7 shall be subject to the procedures set forth herein regardless of the date of the underlying violation(s) for which the penalty is assessed.

14.7.2 Direct Allocation Of Reliability Standards Penalties

14.7.2.1 Conditions For Direct Allocation

If FERC, NERC, and/or WECC assess(es) one (1) or more monetary penalties against the CAISO as the Registered Entity for the violation of one or more NERC Reliability Standards, and the conduct or omission(s) of a particular Market Participant or Market Participants contributed, in whole or in part, to the violation(s) at issue, then the CAISO may seek to directly allocate, in whole or in part, such penalty costs to the Market Participant(s) whose conduct or omission(s) contributed to the violation(s), provided that each of the following conditions are met:

- (1) The Market Participant(s) subject to potential direct allocation receive notice of, and an opportunity to fully participate in, the underlying CMEP proceeding before NERC and/or WECC, or the FERC proceeding in the case of an enforcement proceeding directly instituted by FERC without a prior NERC or WECC proceeding;

- (2) The CMEP proceeding, or enforcement proceeding directly instituted by FERC, results in a finding that the conduct or omission(s) of the Market Participant(s) subject to potential direct allocation contributed, either in whole or in part, to the Reliability Standards violation(s) at issue; and
- (3) Any findings by NERC and/or WECC regarding whether the conduct or omission(s) of the Market Participant(s) contributed, either in whole or in part, to the Reliability Standards violation(s) at issue are filed with FERC.

14.7.2.2 Notice To Affected Market Participant

The CAISO will notify the Market Participant(s) it believes contributed to the Reliability Standards violation(s) during the CMEP proceeding or, if applicable, during the enforcement proceeding directly instituted by FERC. This notification shall be in writing and shall: (i) inform the Market Participant(s) that the CAISO intends to invoke the direct allocation provisions of this Section; (ii) detail the underlying factual basis for the CAISO's position; and (iii) inform the Market Participant(s) that it may seek to participate in the CMEP proceeding or, if applicable, the enforcement proceeding directly instituted by FERC.

14.7.2.3 Failure To Participate

A failure by the notified Market Participant(s) to participate in the CMEP proceeding or, if applicable, in the enforcement proceeding directly instituted by FERC, will not prevent the CAISO from directly allocating the cost associated with a monetary penalty to the Market Participant(s) provided all other conditions in Section 14.7.2 are satisfied.

14.7.2.4 Proposed Allocation And FERC Review Process

Where NERC and/or WECC, or FERC as may be applicable in an enforcement proceeding directly instituted by FERC, determines that the conduct or omission(s) of the Market Participant(s) identified by the CAISO contributed, in whole or in part, to the NERC Reliability Standard(s) violation(s) at issue, the CAISO shall inform the involved Market Participant(s) in writing and shall initially propose an allocation of the penalty cost on a basis proportional to the parties' relative fault, consistent with the applicable regulator's analysis. Regardless of whether the involved Market Participant(s) agree or disagree over the

allocation, the reasonability of such an allocation shall be determined by FERC through submission of the matter to FERC pursuant to Section 205 of the Federal Power Act.

14.7.2.5 Payment Of Allocated Amount

After FERC issues a final order regarding the CAISO's ability to directly allocate the penalty cost, the CAISO shall include any FERC-approved allocated amounts in the invoice for the appropriate Market Participant(s) for the next billing period, or as soon as practicable. The amount to be paid by the Market Participant(s) shall include the allocated portion of the penalty, as established by FERC, together with interest calculated at the FERC authorized refund rate for the period of time, if any, between the CAISO's payment of the penalty and the Market Participant(s) payment of its allocated portion of the penalty.

14.7.3 Indirect Allocation of Reliability-Related Penalty Costs

14.7.3.1 Procedure For Allocation

Where the conduct or omission(s) of a particular Market Participant or Market Participants has not been identified by NERC, WECC, or FERC as a contributing cause for a monetary penalty assessed against the CAISO for a NERC Reliability Standards violation, the CAISO may make a filing with FERC under Section 205 of the Federal Power Act seeking approval to recover the cost of such reliability-related penalties from all Market Participants. The CAISO's Section 205 filing may include a proposed methodology for allocating the penalty across the various types of Market Participants.

14.7.3.2 Case-By-Case FERC Review

Any allocation of penalties pursuant to Section 14.7.3 must be determined by FERC on a case-by-case basis. Absent FERC approval, the CAISO will not allocate a penalty under Section 14.7.3 to Market Participants.

14.7.3.3 Payment of Allocated Amount

After FERC issues a final order regarding allocation of the monetary penalty, the CAISO shall include any FERC-approved allocated amounts in the invoices for the appropriate Market Participants for the next billing period, or as soon as practicable.

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Appendix A Master Definitions Supplement

* * *

- Compliance Monitoring and Enforcement Program

The program used by NERC and the Regional Entities to monitor, assess and enforce compliance with the NERC Reliability Standards. As part of this program, NERC and the Regional Entities may, among other functions, conduct investigations, determine fault and assess monetary penalties.

* * *

- NERC Functional Model

The model used by NERC to define and establish the set of functions that must be performed to ensure the reliability of the bulk power system.

* * *

- NERC Reliability Standards

The standards that have been developed by NERC and/or a Regional Entity, and have been approved by FERC, to ensure the reliability of the bulk power system. The NERC Reliability Standards set forth the specific requirements that responsible entities must perform with respect to the functions defined in NERC's Functional Model.

* * *

- NERC Rules of Procedure

A set of rules and procedures developed by NERC and approved by FERC that establish processes that NERC, NERC members, and Regional Entities must follow. The NERC Rules of Procedure include the process through which a responsible entity that is to perform a set of functions to ensure reliability of the bulk power system must register with NERC as a Registered Entity.

* * *

- Regional Entity

An entity to whom NERC has delegated certain of its electric reliability organization functions for a particular geographic region. WECC is the applicable Regional Entity for the region encompassing the CAISO.

* * *

- Registered Entity

An entity registered with NERC under the NERC Functional Model and the NERC Rules of Procedure as responsible for compliance with a designated set of requirements established by the NERC Reliability Standards.

California Independent System Operator Corporation

Fifth Replacement FERC Electric Tariff

Attachment B - Marked Tariff

Penalty Payment Allocation Compliance Filing

April 2, 2012

14.7 Allocation of ~~Costs Associated with Reliability-Related~~ Penalties Costs

14.7.1 Overview of Process

Under the NERC Functional Model and the NERC Rules of Procedure, Registered Entities for a specific function, including the CAISO, may be assessed monetary penalties by FERC, NERC, and/or WECC for violations of one (1) or more NERC Reliability Standards applicable to that function. This Section 14.7 sets forth the procedure through which the CAISO may seek, with FERC approval, to directly allocate, in whole or in part, the cost of any such penalties assessed upon the CAISO to an entity or entities whose conduct or omission(s) NERC, WECC and/or FERC has determined contributed, in whole or in part, to the violation that gave rise to the penalty. This Section 14.7 also sets forth procedures through which the CAISO may seek, with FERC approval, to recover, in whole or in part, from Market Participants the cost associated with a monetary penalty for a NERC Reliability Standards violation(s) that is not subject to direct allocation, ~~or the cost associated with other monetary penalties that may be imposed by FERC or another regulatory authority.~~ Penalties that are assessed upon the CAISO and become final on or after the effective date of this Section 14.7 shall be subject to the procedures set forth herein regardless of the date of the underlying violation(s) for which the penalty is assessed.

14.7.2 Direct Allocation Of Reliability Standards Penalties

14.7.2.1 Conditions For Direct Allocation

If FERC, NERC, and/or WECC assess(es) one (1) or more monetary penalties against the CAISO as the Registered Entity for the violation of one or more NERC Reliability Standards, and the conduct or omission(s) of a particular Market Participant or Market Participants contributed, in whole or in part, to the violation(s) at issue, then the CAISO may seek to directly allocate, in whole or in part, such penalty costs to the Market Participant(s) whose conduct or omission(s) contributed to the violation(s), provided that each of the following conditions are met:

- (1) The Market Participant(s) subject to potential direct allocation receive notice of, and an opportunity to fully participate in, the underlying CMEP proceeding before NERC and/or WECC, or the FERC proceeding in the case of an enforcement proceeding directly instituted by FERC without a prior NERC or WECC proceeding;

- (2) The CMEP proceeding, or enforcement proceeding directly instituted by FERC, results in a finding that the conduct or omission(s) of the Market Participant(s) subject to potential direct allocation contributed, either in whole or in part, to the Reliability Standards violation(s) at issue; and
- (3) Any findings by NERC and/or WECC regarding whether the conduct or omission(s) of the Market Participant(s) contributed, either in whole or in part, to the Reliability Standards violation(s) at issue are filed with FERC.

14.7.2.2 Notice To Affected Market Participant

The CAISO will notify the Market Participant(s) it believes contributed to the Reliability Standards violation(s) during the CMEP proceeding or, if applicable, during the enforcement proceeding directly instituted by FERC. This notification shall be in writing and shall: (i) inform the Market Participant(s) that the CAISO intends to invoke the direct allocation provisions of this Section; (ii) detail the underlying factual basis for the CAISO's position; and (iii) inform the Market Participant(s) that it may seek to participate in the CMEP proceeding or, if applicable, the enforcement proceeding directly instituted by FERC.

14.7.2.3 Failure To Participate

A failure by the notified Market Participant(s) to participate in the CMEP proceeding or, if applicable, in the enforcement proceeding directly instituted by FERC, will not prevent the CAISO from directly allocating the cost associated with a monetary penalty to the Market Participant(s) provided all other conditions in Section 14.7.2 are satisfied.

14.7.2.4 Proposed Allocation And FERC Review Process

Where NERC and/or WECC, or FERC as may be applicable in an enforcement proceeding directly instituted by FERC, determines that the conduct or omission(s) of the Market Participant(s) identified by the CAISO contributed, in whole or in part, to the NERC Reliability Standard(s) violation(s) at issue, the CAISO shall inform the involved Market Participant(s) in writing and shall initially propose an allocation of the penalty cost on a basis proportional to the parties' relative fault, consistent with the applicable regulator's analysis. Regardless of whether the involved Market Participant(s) agree or disagree over the

allocation, the reasonability of such an allocation shall be determined by FERC through submission of the matter to FERC pursuant to Section 205 of the Federal Power Act.

14.7.2.5 Payment Of Allocated Amount

After FERC issues a final order regarding the CAISO's ability to directly allocate the penalty cost, the CAISO shall include any FERC-approved allocated amounts in the invoice for the appropriate Market Participant(s) for the next billing period, or as soon as practicable. The amount to be paid by the Market Participant(s) shall include the allocated portion of the penalty, as established by FERC, together with interest calculated at the FERC authorized refund rate for the period of time, if any, between the CAISO's payment of the penalty and the Market Participant(s) payment of its allocated portion of the penalty.

14.7.3 Indirect Allocation of Reliability-Related Penalty Costs Not Subject to Direct Allocation

14.7.3.1 Procedure For Allocation

Where the conduct or omission(s) of a particular Market Participant or Market Participants has not been identified by NERC, WECC, or FERC as a contributing cause for a monetary penalty assessed against the CAISO for a NERC Reliability Standards violation, ~~or where the CAISO is assessed a monetary penalty by FERC or another regulatory body for the CAISO's own actions or inaction in violation the CAISO Tariff, FERC rules, or rules or regulations established by other regulatory bodies,~~ the CAISO may make a filing with FERC under Section 205 of the Federal Power Act seeking approval to recover the cost of such reliability-related penalties from all Market Participants. The CAISO's Section 205 filing may include a proposed methodology for allocating the penalty across the various types of Market Participants.

14.7.3.2 Case-By-Case FERC Review

Any allocation of penalties pursuant to Section 14.7.3 must be determined by FERC on a case-by-case basis. Absent FERC approval, the CAISO will not allocate a penalty under Section 14.7.3 to Market Participants.

14.7.3.3 Payment of Allocated Amount

After FERC issues a final order regarding allocation of the monetary penalty, the CAISO shall include any FERC-approved allocated amounts in the invoices for the appropriate Market Participants for the next billing period, or as soon as practicable.

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