

119 FERC ¶ 61,053
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

California Independent System Operator
Corporation

Docket Nos. ER06-700-002 and
ER06-700-003

ORDER ON REHEARING AND COMPLIANCE FILINGS

(Issued April 19, 2007)

1. In this order, we grant in part and deny in part the requests for rehearing of the May 12, 2006 Order in this proceeding,¹ in which the Commission conditionally accepted the California Independent System Operator Corporation's (CAISO) proposed revisions to the credit policy described in its tariff.² We will also accept two compliance filings that the CAISO made to respond to the requirements of the Initial Order.

Background and Requests for Rehearing

2. The initially-proposed revisions to the CAISO tariff allow the CAISO to determine entity-specific unsecured credit limits, replacing the previous system in which market participants had an unlimited line of unsecured credit if they maintained an approved credit rating. The revisions clarify to what entities the credit provisions apply. Further, they specify that the credit requirements apply to the acceptance of schedules and transactions in the CAISO markets, as well as the payment of charges. The CAISO stated that these changes will provide greater assurance that each market participant and firm transmission rights bidder can satisfy its financial obligations and not present undue credit risk to CAISO market creditors.

¹ California Independent System Operator Corporation, 115 FERC ¶ 61,170 (2006) (Initial Order).

² FERC Electric Tariff, Second Replacement Volume Nos. I and II.

3. In the Initial Order, the Commission accepted the proposed tariff revisions, ordered further revisions to the CAISO credit policy, and directed the CAISO to submit a compliance filing. Most notably, the Commission required the CAISO to include in its tariff the eight-step process that the CAISO proposes to use to calculate unsecured credit limits, and to file its Credit Policy and Procedures Guide (Credit Guide) as an attachment to its tariff. The Commission also urged the CAISO to work with stakeholders to develop an alternative measure for calculating the financial strength of non-profits' unsecured credit limits, which could be included in the Credit Guide.

4. The CAISO filed a request for rehearing of the Initial Order. The Cities of Redding and Santa Clara, California and the M-S-R Public Power Agency (Cities/M-S-R) also filed a request for rehearing, and later filed an amended request for rehearing. The Northern California Power Agency (NCPA) filed a motion for clarification or, in the alternative, for temporary stay and expedited action. Cities/M-S-R and the CAISO filed answers to NCPA.

The CAISO's Compliance Filings

5. The CAISO submitted a compliance filing on July 11, 2006, which includes two sets of proposed tariff revisions. The first set of revisions contains the changes required by the Initial Order, including filing the Credit Guide as an amendment to the CAISO tariff, incorporating the eight-step process for determining unsecured credit limits into the tariff, and other required changes. The second, alternative set of revisions does not include filing the Credit Guide as an attachment, but it contains a description of the eight-step process for determining unsecured credit limits in the tariff and makes other changes that the Commission required in the Initial Order. The CAISO states that two sets of changes are mutually exclusive.

6. On August 9, 2006, as corrected on August 10, 2006, the CAISO submitted a further compliance filing. It proposed tariff modifications including measures for calculating unsecured credit limits for local publicly-owned electric utilities, measures for calculating unsecured credit limits for unrated governmental entities that receive federal or state government appropriations, and two new, related definitions in Appendix A of the CAISO tariff.

Notice of Filing and Responsive Pleading

7. Notice of the CAISO's July 11 compliance filing was published in the *Federal Register*, 71 Fed. Reg. 41,794 (2006), with interventions and protests due on or before August 1, 2006. The Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (Six Cities) and NCPA filed comments. Transmission Agency of Northern California (TANC) and Cities/M-S-R protested the CAISO's compliance filing. The CAISO filed an answer.

8. Notice of the CAISO's August 9 supplemental compliance filing was published in the *Federal Register*, 71 Fed. Reg. 47,800 (2006), with interventions and protests due on or before August 31, 2006. The Western Area Power Administration (WAPA) filed a motion to intervene and comments. NCPA filed comments.

Discussion

A. Procedural Matters

9. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2006), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

10. NCPA's request for clarification amounts to a request for rehearing of the Initial Order. Answers to requests for rehearing are prohibited under Rule 713(d)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d)(1) (2006). As such, we will reject Cities/M-S-R's and the CAISO's answers to NCPA.

11. 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 answer because it has provided information that assisted us in our decision-making process.

B. Requests for Rehearing and Clarification (Docket No. ER06-700-002)

1. Inclusion of Credit Guide in the Tariff

12. In its initial filing, the CAISO proposed to continue to post the Credit Guide on its website, as it has done since 2003. In the Initial Order, however, the Commission found that the Credit Guide includes information that will significantly affect the rates, terms and conditions of transmission service under the CAISO tariff. Accordingly, the Commission directed the CAISO to file the Credit Guide as an attachment to its tariff and to explain what Credit Guide provisions, if any, it recommends removing from the tariff. The Commission further directed the CAISO to include section A-3 of the Credit Guide, which details the eight-step process by which unsecured credit limits are calculated, in the body of its tariff.

13. On rehearing, the CAISO argues that the requirements that it file the Credit Guide and include the eight-step process for calculating unsecured credit limits in its tariff impose an undue burden. The CAISO states that it designed the eight-step process with the expectation that the process would need to be revised and refined based on experience

and changing market conditions. It adds that some of the default probability measures supplied by Moody's KMV³ are updated monthly and it would be impractical for the CAISO to file these changes every month.

14. Finally, the CAISO asserts that it should be permitted to add further details to its tariff regarding its credit policies instead of filing the entire Credit Guide as part of the tariff. It asserts that the provisions are already completely transparent because they are posted on the CAISO's website.

15. We partially grant the CAISO's request for rehearing and specify that it need not file the entire Credit Guide as part of its tariff. Consistent with the Commission's *Policy Statement on Electric Creditworthiness*,⁴ we expect that the information contained in the Credit Guide will continue to be available to market participants on the CAISO's Open-Access Same-Time Information System (OASIS) and the CAISO's website, as appropriate.

16. We deny rehearing to the extent that removal of the Credit Guide from the tariff would remove: (1) the eight-step process used to calculate an entity's unsecured credit limit, as detailed in sections 12.1.1A through 12.1.1A.2 of the first set of revisions contained in the CAISO's July 11 compliance filing; and (2) the process that the CAISO will use to calculate an entity's estimated aggregate liability, as described in Part C of the Credit Guide. These calculations form the basis upon which unsecured credit limits are determined and, therefore, significantly affect the rates, terms and conditions of jurisdictional transactions on the CAISO-controlled grid regarding creditworthiness and collateral requirements.⁵ Consistent with the Commission's "rule of reason," they must be included in the tariff.⁶ As further discussed below, we will require the CAISO to make a compliance filing within 60 days of the date of this order that updates the tariff to reflect these determinations. As we advised the Midwest Independent Transmission System Operator, Inc., we remind the CAISO that changes to the creditworthiness

³ As detailed in the Initial Order, Moody's KMV provides a non-public default probability measure that the CAISO expects will, at least for public companies, be more responsive than traditional credit ratings to underlying credit quality ahead of a bankruptcy event. Initial Order at P 28, 33.

⁴ 109 FERC ¶ 61,186 at P 12 (2004) (*Policy Statement*).

⁵ See Midwest Independent Transmission System Operator, Inc., 108 FERC ¶ 61,163 at P 453 (2004); New York Independent System Operator, Inc., 98 FERC ¶ 61,282 at 62,217 (2002).

⁶ *E.g., id.* P 1633.

standards are changes to the tariff subject to Commission review; as such, they should be filed under section 205 of the Federal Power Act (FPA).⁷

17. While we require the CAISO to include the process for calculating an entity's unsecured credit limit and estimated aggregate liability in its tariff, we recognize that certain inputs to those calculations are updated frequently.⁸ Having such details in the tariff would be impractical and would present a burden to the CAISO and stakeholders in keeping the tariff up to date. Publicly-available information from third parties, such as the Moody's KMV default probability measure, may be referred to without being included in the tariff, but the tariff must specify where one can find the most current input information. Other specific provisions to be required in the tariff are discussed below with respect to the CAISO's compliance filings.

2. Disclosure of Unsecured Credit Limits

18. Cities/M-S-R seek rehearing of the Commission's finding that the CAISO does not have to make public the unsecured credit limits of its market participants. Cities/M-S-R state that market participants would be unable to determine whether such unsecured credit limits appear excessive, and would be unable to challenge the unsecured credit limits of other market participants under section 206 of the FPA,⁹ if the Commission does not require disclosure of unsecured credit limits for public scrutiny. Cities/M-S-R argue that, under the CAISO's mutualized default risk format, the establishment of an improperly high unsecured credit limit could result in financial exposure to all market participants.

19. The Commission recognizes the unique credit risks that participants in independent system operators (ISO) and regional transmission organizations (RTO) face, including mutualized default risk. As noted in the *Policy Statement*, shortened settlement periods and netting are cost-effective steps to reduce the exposure to risk among market participants.¹⁰ In addition, the Commission encouraged ISOs and RTOs to work with

⁷ 16 U.S.C. § 824d (2000).

⁸ The Moody's KMV default probability measure table is one example of such an input. According to the CAISO, this table is updated monthly and, if included in the tariff, would required the CAISO to make monthly filings in order to keep the tariff up to date.

⁹ 16 U.S.C. § 824e (2000).

¹⁰ Policy Statement at P 20.

their stakeholders to improve their credit practices,¹¹ which is what the CAISO has done here. The Commission acknowledged that “market participants must trust ISOs/RTOs to implement their credit policies in a manner created to limit, as much as possible, the risk of credit defaults.”¹² The CAISO’s credit policy revisions – which were crafted with significant stakeholder input – rein in previously unlimited extensions of credit to market participants, arguably leaving Cities/M-S-R more protected from default risk than before.

20. We deny Cities/M-S-R’s request for rehearing. As explained in the Initial Order, it would be inappropriate for the CAISO to publicly reveal sensitive information, such as a market participant’s unsecured credit limit, for scrutiny by other market participants. As contemplated in the *Policy Statement*, market participants should work together with the CAISO to determine cost-effective practices for reducing credit risk. However, this collaboration does not extend to the release of sensitive information that is not otherwise publicly available.

21. We note that a market participant may take advantage of the dispute resolution procedures described in section 13 of the CAISO’s tariff if it becomes concerned that the CAISO has calculated its unsecured credit limit incorrectly. We further note that, to the extent that a market participant believes that its potential liability is unjust, unreasonable, unduly discriminatory or preferential as a result of CAISO’s credit policy, it may bring a complaint to the Commission under FPA section 206.

3. Determining Unsecured Credit Limits for Non-Profit Entities

22. In its original protest, NCPA argued that the CAISO’s revised method of calculating unsecured credit limits was not well-suited to the measurement of the financial strength of a non-profit entity such as itself. The CAISO, in its answer, expressed its willingness to work with NCPA to develop an alternative method of establishing creditworthiness.

23. In the Initial Order, the Commission encouraged the CAISO to work with its stakeholders to develop an alternative measure to calculate the unsecured credit limits of non-profit entities. The Commission ordered the CAISO to report to the Commission, on an informational basis, the progress made within 60 days of the Initial Order. NCPA now seeks clarification that the Commission intended that NCPA would not to be subject to the revised credit policies while an alternative measure of creditworthiness was being developed.

¹¹ *Id.* P 32.

¹² *Id.* P 18.

24. The CAISO's August 9 compliance filing, which we will address below, contains the alternative measure for calculating creditworthiness of non-profit entities. Moreover, the CAISO requests that this filing be accepted effective May 14, 2006 – the same effective date that the Commission set for the tariff revisions approved in the Initial Order – so that there will be no period of time in which the creditworthiness requirements for non-profit entities are unclear. We therefore deny NCPA's request for clarification.

B. Compliance Filings (Docket No. ER06-700-003)

1. July 11 Compliance Filing

a. The CAISO's Compliance Filing

25. In its July 11 compliance filing, the CAISO filed two sets of proposed revisions to its tariff. The first set of proposed revisions contains the changes required by the Initial Order, including filing the Credit Guide as an amendment to its tariff, incorporating the eight-step process for determining unsecured credit limits into the tariff, and making other required changes. The alternative set of proposed revisions does not include filing the Credit Guide as an attachment to the tariff, but rather contains a description of the eight-step process for determining unsecured credit limits. The CAISO states that two sets of changes are mutually exclusive.

26. The CAISO states that the Commission should accept the alternative set of revisions, rather than the first set of revisions. The CAISO believes that the alternative set of changes satisfies the Commission's "rule of reason" because it includes in the tariff the portions of the Credit Guide that will significantly affect rates, terms, and conditions of service.

27. The CAISO states that in the alternative set of changes, section 12.1.1 includes a description of the means by which the CAISO determines the unsecured credit limits of four types of market participants. Section 12.1.1 also describes the eight-step process the CAISO uses for calculating unsecured credit limits for entities other than unrated governmental entities, as well as the process used for calculating unsecured credit limits for unrated governmental entities. The CAISO notes that it added several defined terms to Appendix A of the tariff to explain the terms now included in this section.

28. New section 12.1.1.1 of the alternative set of changes includes the credit strength indicators contained in the first two paragraphs of section A-1.3 of the Credit Guide. Section 12.1.1.2 contains provisions regarding financial statements that are required of market participants and firm transmission rights (FTR) bidders. New section 12.1.2.1 lays out additional procedures applicable to certain types of financial security. Finally, the CAISO states that section 12.4 contains provisions regarding reviews of a CAISO

request for additional financial security and the dispute process applicable to a CAISO request for additional financial security.

b. Comments

29. Six Cities argue that the Commission should require the CAISO to include the Credit Guide in its tariff. They state that the Credit Guide the CAISO proposes to post on its website contains information that is critical to the CAISO's determination of unsecured credit limits.

30. Six Cities point out that section 12.1.1.1 of the tariff and section A-1.3 of the Credit Guide give the CAISO discretion to reduce by up to 100 percent the unsecured credit limit that would otherwise be granted based on the quantitative criteria laid out in other sections of the tariff and the Credit Guide. Six Cities argue that the Commission should require the CAISO to: (1) further explain how it will consider qualitative factors; and (2) include language in the tariff clarifying that whenever the CAISO has discretion with respect to implementing its credit policy, it must exercise such discretion in a non-discriminatory manner.

31. Cities/M-S-R and TANC state that the CAISO's proposed alternative set of changes should be disregarded as it is not in compliance with the Initial Order. Cities/M-S-R argue that under the Initial Order, the CAISO does not have an option not to file the Credit Guide as part of its tariff.

32. Cities/M-S-R and TANC argue that the CAISO proposal in the alternative set of changes to include a description of the eight-step process used to calculate unsecured credit limits, instead of including the entire process, contravenes the Initial Order. Cities/M-S-R state that the CAISO's description of the eight-step process would not contain the substance of how unsecured credit limits are calculated and the unfiled version of the Credit Guide would be the governing force of the entity-specific unsecured credit limit process. Further, Cities/M-S-R and TANC state that the CAISO's failure to include sample calculations of how unsecured credit limits are determined in the alternative set of changes defies the Initial Order. They also requested typographical changes to the CAISO's proposal.

c. The CAISO's Answer

33. In its answer, the CAISO asserts that it has fully complied with the Initial Order. The CAISO avers that the description of the eight-step process for calculating an entity's unsecured credit limit is sufficient to satisfy the Commission's "rule of reason." Based on this description, the CAISO contends, market participants and FTR bidders can be assured that the CAISO cannot change the basic means of how those calculations are made without receiving approval from the Commission. Further, the CAISO states, the

alternative set of changes contains a provision entitling a market participant or FTR bidder to a written analysis as to how the provisions were applied in setting its unsecured credit limit.

34. Regarding the level of detail contained in the description of the process for calculating an entity's unsecured credit limit, the CAISO explains that it anticipates that the detailed tables and calculations implementing the eight-step process may need to change often, and that certain procedures may undergo further refinement as the CAISO and market participants gain experience with the new provisions.

35. The CAISO maintains that no further explanation regarding its application of the qualitative factors listed in the tariff is needed. The CAISO notes that these factors are explicitly identified in the *Policy Statement* and that the CAISO did not propose any changes to them in the alternative tariff sheets filed on July 11. Moreover, the CAISO asserts that it need not include language in the tariff stating that it must exercise its discretion in implementing its credit policy in a non-discriminatory manner. Rather, the CAISO believes that the FPA already forbids the CAISO or any other public utility from exercising such discretion in a manner that is unduly discriminatory.

36. The CAISO agrees with Cities/M-S-R and TANC that minor corrections should be made to provisions contained in the first set of changes. The CAISO states that, if the alternative set of changes are not accepted by the Commission, the CAISO should make the corrections to the first set of changes suggested by commenters.

d. Commission Determination

37. Consistent with our grant of rehearing on this issue above, we find that the CAISO's alternative compliance filing has struck a reasonable balance by describing the CAISO's credit practices in the tariff and providing additional details in the Credit Guide, which it will post on the CAISO website. As stated above, given the frequency with which some components of the unsecured credit limit calculation process are updated, having such details in the tariff would be impractical and would present a burden to the CAISO and stakeholders in keeping the tariff up-to-date. Therefore, we accept the alternative set of changes submitted by the CAISO, with certain modifications.

38. Under the Commission's "rule of reason," a rule, standard or practice that significantly affects the rates, terms and conditions of transmission service must be included into a public utility's tariff.¹³ Because the CAISO's process for calculating an entity's unsecured credit limit significantly affects the terms and conditions of service, it

¹³ *Supra* note 6.

must be included in the CAISO's tariff.¹⁴ The description of this process that the CAISO proposes in section 12.1.1 of the alternative revisions filed on July 11 is not detailed enough to provide market participants or the Commission with a thorough understanding of how the CAISO will make this calculation. We therefore direct the CAISO to make a compliance filing to substitute for alternate section 12.1.1 the tariff the language contained in sections 12.1.1A through 12.1.1.A2 of the first set of revisions included in the July 11 compliance filing.

39. In addition, the proposed definition for Material Change in Financial Condition contains references to "tangible net worth" and "net assets" – both of which the CAISO now proposes to be defined terms in the tariff.¹⁵ To be accurate, these two terms should be capitalized in the definition of Material Change in Financial Condition.

40. We direct the CAISO to submit a compliance filing within 60 days of the date of this order to incorporate these changes.

2. August 9 Supplemental Compliance Filing

a. The CAISO's Supplemental Compliance Filing

41. In its August 9 compliance filing, as corrected, the CAISO submitted modifications to its tariff to include measures for calculating unsecured credit limits for local publicly-owned electric utilities, measures for calculating unsecured credit limits for unrated governmental entities that receive federal or state government appropriations, and the addition of two new definitions to Appendix A of the CAISO tariff.

42. The proposed tariff revisions state that a local publicly-owned electric utility that has a governing body with ratemaking authority and has submitted an application for an unsecured credit limit will be entitled to a credit limit of \$1 million without regard to its assets. The CAISO states that a local publicly-owned electric utility may request an unsecured credit limit based on net assets in order to establish a credit limit of greater than \$1 million. Further, local publicly-owned electric utilities that operate through a joint powers agreement, or similar agreement, may aggregate a portion of their unsecured credit limit (equal to or less than \$1 million) to one or more other local publicly-owned electric utilities that operate through a joint powers agreement.

¹⁴ *Id.* We find that this is also consistent with the requirements of Order No. 890. *Preventing Undue Discrimination in Transmission Service*, Order No. 890, 71 Fed. Reg. 12,266 at P 1657 (Mar. 15, 2007), FERC Stats. & Regs. ¶ 31,241 (2007).

¹⁵ Proposed Alternate First Revised Sheet No. 512.

43. The CAISO states it recognizes the need for an alternative measure to assign credit limits to certain not-for-profit entities that are creditworthy but would not qualify for an unsecured credit limit under the existing tariff language or the alternative approach. The CAISO proposes that unrated governmental entities that receive appropriations from the federal or state government and have applied for an unsecured credit limit will be entitled to a credit limit of the lower of \$250 million or the amount appropriated for the purpose of procuring energy and energy-related services for the applicable fiscal year.

44. The CAISO notes that the location of the proposed amendments in the August 9 compliance filing may differ, depending on which set of revisions the Commission accepts from its July 11 compliance filing. If the Commission accepts the first set of proposed revisions, these amendments would be included in new sections A.4 and A.5 of the Credit Guide. If the Commission accepts the alternative set of proposed revisions, the amendments would be included in new sections 12.1.1.4 and 12.1.1.5 of the tariff.

45. Finally, the CAISO requests that the Commission waive the 60-day prior notice requirement and permit the August 9 filing to become effective on May 14, 2006 – the same date that the CAISO’s original filing in this proceeding became effective.¹⁶ The CAISO states that granting the waiver would ensure that local publicly-owned electric utilities and unrated governmental entities would be subject to the alternative measures for determining unsecured credit limits effective at the same time the revisions to the CAISO’s credit policy went into effect.

b. Comments

46. Western and NCPA request that the Commission approve the revisions to the CAISO’s credit policy submitted in the CAISO’s August 9 supplemental compliance filing.

c. Commission Determination

47. We conditionally accept the CAISO’s proposal for calculating unsecured credit limits for local publicly-owned electric utilities and unrated governmental entities that receive federal or state appropriations. Because we earlier accepted the CAISO’s alternate set of changes proposed in its July 11 compliance filing, and thereby eliminated the Credit Guide as Appendix Z to the tariff, the proposed tariff sheets contained in the August 9 supplemental compliance filing are incompatible with how the CAISO tariff will read. Therefore, we direct the CAISO to file tariff sheets within 60 days of this order that incorporate into section 12 the methodology for calculating unsecured credit limits for publicly-owned electric utilities or unrated government entities that receive federal or

¹⁶ Initial Order at P 1 & Ordering P A.

state appropriations we approved above. For good cause shown, we will grant the CAISO's request for waiver of the 60-day prior notice requirement and accept the filing effective May 14, 2006.

The Commission orders:

(A) The requests for rehearing of the Initial Order are hereby granted in part and denied in part, as described in the body of this order.

(B) The alternate set of changes submitted by the CAISO in its July 11 compliance filing is accepted subject to conditions and modifications, as discussed in the body of this order.

(C) The CAISO's supplemental tariff sheets, filed August 9, are accepted effective May 14, 2006.

(D) The CAISO is hereby directed to submit a compliance filing, as discussed in the body of this order, within 60 days of the date of this order.

By the Commission.

(S E A L)

Philis J. Posey,
Deputy Secretary.