141 FERC ¶ 61,237
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
Cheryl A. LaFleur, and Tony T. Clark.

California Independent System Operator Corporation — Docket No. ER13-219-000

ORDER ON PROPOSED TARIFF REVISIONS

(Issued December 20, 2012)

1. On October 29, 2012, the California Independent System Operator Corporation (CAISO) submitted, pursuant to section 205 of the Federal Power Act (FPA),[1] proposed revisions to its tariff to include greenhouse gas compliance costs in the calculations set forth in the CAISO tariff for determining certain costs. In this order we find that, in general, CAISO's proposal to incorporate the costs of the greenhouse gas allowances into the calculation of generating units' variable costs is just and reasonable. However, CAISO has not demonstrated that its alternative methodology for calculating the price at any time that a greenhouse gas allowance price index is unavailable is just and reasonable. Accordingly, as discussed below, we conditionally accept in part and reject in part the proposed tariff revisions and direct CAISO to submit a compliance filing within 15 days of the issuance of this order.

I. Background

2. Beginning in 2013, the State of California will implement a greenhouse gas cap and trade program (California Program).[2] The California Program will apply to electric power generation, as well as various other sources of greenhouse gases. The regulations

[1] 16 U.S.C. § 824d (2006).

[2] *See* California Global Warming Solutions Act of 2006, Cal. Health & Safety Code §§ 38500-38599.

implementing the greenhouse gas cap will be administered by the California Air Resources Board (CARB).[3]

3. Under the California Program, the greenhouse gas cap will apply to the emissions of in-state generators that use combustible fuels, including natural gas, coal, and oil and to the emissions of similar types of generation imported from outside of California. The overall greenhouse gas cap for 2013 will be set at two percent below 2012's forecasted emissions. The cap will decline an additional two to three percent each year until 2020. At this point, the cap will be set at about 15 percent below 2012 levels.[4]

4. The California Program's primary compliance instrument will be allowances issued by CARB for periodic auctions and also available through bilateral trading.[5] CARB will distribute allowances by allocating them at no cost to various load serving entities. These load serving entities will be required to place a portion of their allocated allowances into a consignment account. CARB will auction off allowances from this account along with any allowances that were not allocated to other entities covered by the regulations, including generation owners and power importers. The load serving entities will be required to use the auction proceeds to offset increased costs due to the California Program or for energy efficiency programs.

5. As a result of the California Program, each resource subject to the greenhouse gas regulations will bear a per-megawatt-hour cost associated with the greenhouse gas allowances needed for its energy output. The cost of allowances to generation facilities varies with the output of the facility, and as such this cost is expected to be included in the variable cost and energy bids from affected units. Inclusion of these costs by the affected units will have an impact on the wholesale price of electricity in California and potentially other states in the western region.

II. The CAISO Filing

6. As explained below, the CAISO filing establishes an approach for incorporating the costs of the greenhouse gas allowances as a variable cost of generation in the calculation of resource commitment costs (start-up and minimum load costs), default

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[3] *See* Cal. Health & Safety Code § 38550.

[4] Entities subject to the regulation will also be able to meet up to eight percent of their obligations with offsets. These offsets will be issued for things like reforestation projects and greenhouse gas reduction actions entities undertook prior to the initial compliance period.

[5] An allowance will convey the right to emit a metric ton of CO_2 equivalents.

energy bids, and generated bids.[6] CAISO states that since greenhouse gas emissions are proportional to a generating unit's energy output, the cost of the greenhouses gas allowances should be included in CAISO's calculation of the generating units' variable costs. Additionally, CAISO states that it is just and reasonable to include greenhouse gas costs as an additional component of the variable costs calculated in its tariff because it will allow generators to recover emissions allowance costs incurred as a result of the California Program.

7. CAISO states that it is adopting the approach recommended by CAISO's Department of Market Monitoring in a white paper that included proposed equations for incorporating the allowance costs. Furthermore, CAISO states that its proposed approach is comparable to the approach that ISO-NE adopted in order to incorporate greenhouse gas allowance costs incurred pursuant to the Regional Greenhouse Gas Initiative (RGGI).[7]

8. Specifically, with regard to the calculation of start-up and minimum load costs for natural gas-fired resources,[8] section 30.4.1.1.1 includes a greenhouse gas cost adder for each resource registered with CARB as having a compliance obligation.[9] The cost adder is calculated as the product of the resource's fuel requirement per start-up, the greenhouse

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[6] CAISO calculates generating units' variable energy costs for energy, start-up, minimum load, and transitions between multi-stage generator configurations. While market participants submit these energy bid components, CAISO calculates each generating unit's actual variable costs for these components using set formulas. CAISO uses these variable energy costs to: (1) create default energy bids used for market power mitigation; (2) calculate bid caps for minimum load and start-up costs; (3) create energy, minimum load and start-up bids in the event a market participant does not submit a required bid; and (4) calculate daily transition costs based on current gas prices to dispatch multi-stage generators. Bids for imported energy include only an energy component. CAISO does not calculate default energy bids for imported energy because import bids are not subject to local market power mitigation. Transmittal Letter, Attachment C, Department of Market Monitoring, Tariff Amendment to Allow Recovery of Greenhouse Gas Compliance Costs at 7 (October 29, 2012).

[7] Transmittal Letter at 5.

[8] CAISO notes that it is proposing to break out existing tariff section 30.4.1.1 into new sections 30.4.1.1.1, 30.4.1.1.2 and 30.4.1.1.3. Transmittal Letter at 4-5.

[9] Under the California Program, the greenhouse gas cap will apply to the emissions of in-state generators that use combustible fuels, including natural gas, coal, and oil that emit at least 25,000 $mtCO_2$ equivalents annually.

gas emissions rate authorized by CARB,[10] and the applicable greenhouse gas allowance price.[11] Section 30.4.1.1.1 also states that minimum load costs for such resources include a greenhouse gas cost adder for each registered resource. The cost adder is calculated as a product of the resource's fuel requirement at minimum load, the greenhouse gas emissions rate authorized by CARB, and the applicable greenhouse gas allowance price.[12]

9. Section 30.4.1.1.2 addresses start-up costs and minimum load costs for non-natural gas-fired resources. The greenhouse gas allowance costs for each such resource registered with CARB as having a compliance obligation will be provided to CAISO by the resource's scheduling coordinator.[13] According to CAISO, because the set of non-natural gas-fired resources is smaller than the set of natural gas-fired resources, a one-size fits all approach to these costs cannot be used, and it is not practical to develop unique cost indices based on fuel type.[14]

10. New section 39.6.1.6.2[15] states that, for resources that are registered with CARB as having a compliance obligation, CAISO will calculate a projected greenhouse gas allowance price component to be used in establishing maximum start-up and minimum load costs after the twenty-first day of each month, and these costs will be posted on the

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[10] The greenhouse gas emissions rate authorized by CARB can be calculated under U.S. Environmental Protection Agency regulations. Currently, the greenhouse gas emission rate is 0.053165 $mtCO_2$ /mmBTU. Transmittal Letter, Attachment D at 7.

[11] Transmittal Letter at 5. The greenhouse gas allowance price is calculated pursuant to new section 39.7.1.1.1.4 of the CAISO tariff.

[12] Transmittal Letter at 5.

[13] *Id.* at 6. According to CAISO, the information provided by the scheduling coordinator must be consistent with the information provided to CARB. Furthermore, if the scheduling coordinator does not provide sufficient data for CAISO to determine the unit's proxy costs, CAISO will determine that the unit's start-up and minimum load costs are zero. *Id.*

[14] *Id.*

[15] CAISO modified section 39.6.1.6 to add that the calculation of the projected proxy cost will include a projected greenhouse gas allowance price component for resources with a compliance obligation. Transmittal Letter at 6.

CAISO website by the end of the month.[16] The projected greenhouse gas allowance price component will be calculated by averaging the applicable daily greenhouse gas allowance prices calculated over the first twenty days of the month using the methodology set forth in section 39.7.1.1.1.4.[17]

11. With regard to the calculation of default energy bids and generated bids,[18] each natural gas-fired resource registered with CARB as having a compliance obligation, CAISO will calculate a greenhouse gas cost adder as the product of the resource's incremental heat rate, the greenhouse gas emissions rate authorized by CARB, and the applicable greenhouse gas allowance price.[19] Section 39.7.1.1.1.2(b) states that for non-natural gas-fired resources registered with CARB as having a compliance obligation, the greenhouse allowance cost will be provided to CAISO by the scheduling coordinator.[20]

12. As noted above, section 39.7.1.1.1.4 sets forth the methodology for calculating the greenhouse gas allowance price. To calculate the greenhouse gas allowance price, CAISO will use different greenhouse gas price indices for the day-ahead market and the real-time market for each trading day, and each greenhouse gas price index will be

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[16] Section 39.6.1.6.2 also states that the projected greenhouse gas allowance price component will be applicable when scheduling coordinators elect the registered cost option until a new greenhouse gas allowance price component is calculated and posted on the CAISO website. Transmittal Letter at 6.

[17] *Id.* at 6-7.

[18] CAISO will create a generated bid when the scheduling coordinator fails to enter a bid for a resource that is required to submit available capacity consistent with the bidding provisions of section 30 and the generated bid will be based on published pricing data for greenhouse gas allowances. Generated bid components will be calculated as set forth in sections 30 and 40.6.8.

[19] Transmittal Letter at 7. CAISO asserts that this equation tracks the one proposed by the Department of Market Monitoring, is just and reasonable and is comparable to the approaches used by the independent system operators responsible for implementation of the RGGI costs.

[20] *Id.* at 7-8.

calculated on a daily basis using at least two prices from two or more publications identified in the Business Practice Manual.[21]

13. If a greenhouse gas price index is unavailable, CAISO will use the most recent available greenhouse gas price index. If one or more published prices are determined by CAISO not to reflect market fundamentals or if the published prices are not available for an extended period, CAISO will establish the greenhouse gas allowance price using the alternative methodology specified in the Business Practice Manual.[22] The average of the daily values calculated pursuant to section 39.7.1.1.1.4 also will be used to calculate the projected greenhouse gas allowance price component to be used in establishing maximum start-up and minimum load costs under section 39.6.1.6.2. Thus, section 39.6.1.6.2 states that CAISO will calculate a projected greenhouse gas allowance price using the alternative methodology specified in the Business Practice Manual if the values calculated pursuant to section 39.7.1.1.1.4 do not reflect market fundamentals.[23]

14. CAISO contends that the alternative methodology was included to address stakeholder concerns that CAISO should have sufficient flexibility to address the potential risks that published prices might not always reflect sufficient market liquidity or stability to be meaningful or might not be available for an extended period. According to CAISO, if this occurs the tariff amendments would permit CAISO to establish a default greenhouse gas allowance price pursuant to the Business Practice Manual alternative methodology using the best information that is available at the time.[24]

15. CAISO contends that the tariff amendments are just and reasonable because they provide for the recovery of additional costs that resources with a CARB compliance obligation will incur as of January 1, 2013.[25] CAISO requests an effective date of January 1, 2013 because that is the date that CARB intends to implement its cap and trade program. CAISO also requests that the Commission issue its order by

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[21] *Id.* at 8. The real-time market price for any given trading day will use the most recently published greenhouse gas price index, and the day-ahead market for that same trading day will use the greenhouse gas price index published one day earlier. *Id.*

[22] *Id.*

[23] *Id.* at 9.

[24] *Id.*

[25] *Id.* at 1.

December 28, 2012 to provide CAISO with several days after the order's issuance to allow for the deployment of the necessary software and business systems.[26]

III. Notice and Responsive Pleadings

16. Notice of CAISO's filing was published in the *Federal Register*, 77 Fed. Reg. 66,827 (2012), with interventions, comments, and protests due on or before October 29, 2012. Timely motions to intervene raising no substantive issues were filed by: Electric Power Supply Association; the J.P. Morgan Companies;[27] the NRG Companies;[28] Southern California Edison Company; Northern California Power Agency; the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (Six Cities); PacifiCorp; The City of Santa Clara, California and M-S-R Public Power Agency; Modesto Irrigation District; and Powerex Corporation. Timely motions to intervene and comments were filed by: California Department of Water Resources State Water Project (SWP), and Pacific Gas and Electric Company (PG&E). A timely motion to intervene and protest was filed by Calpine Corporation (Calpine). Portland General Electric Company (Portland) submitted a motion to intervene out-of-time on November 21, 2012. CAISO submitted an answer to protests and comments. On December 3, 2012, PacifiCorp filed a Motion for Technical Conference.

17. In its comments, SWP contends that CAISO's proposal in section 39.7.1.1.1.4 fails to fully describe how it will calculate the greenhouse gas allowance price that it will use if one or more published prices are determined by CAISO not to reflect market fundamentals or if published prices are not available for an extended period. SWP objects to CAISO's failure to provide information regarding the alternative methodology other than to state that the alternative methodology will be described in CAISO's Business Practice Manual. SWP requests that the Commission require CAISO to provide the missing details.[29]

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[26] *Id.* at 10.

[27] The J.P. Morgan Companies include J.P. Morgan Ventures Energy Corporation, and BE CA LLC.

[28] The NRG Companies include NRG Power Marketing LLC; Cabrillo Power I LLC; Cabrillo Power II LLC; El Segundo Power, LLC; High Plains Ranch II LLC; Long Beach Generation LLC; NRG Solar Alpine; NRG Solar Borrego I LLC; NRG Solar Blythe LLC; NRG Solar Roadrunner LLC; and Avenal Solar Holdings LLC.

[29] SWP November 19, 2012 Motion to Intervene and Comments at 1-2 (SWP Comments).

18. In response, CAISO states that it expects the narrow circumstances in which the alternate methodology will come into play to occur rarely, if at all. According to CAISO, the alternate methodology will serve solely as a backstop to the generally applicable methodology set forth in section 39.7.1.1.1.4. CAISO claims that it proposed the alternative methodology in response to stakeholders concerns that CAISO should have the flexibility to address the potential risk that published prices might not reflect sufficient market liquidity or stability to be meaningful or might be unavailable for an extended period. If such an event occurs, the tariff revisions would permit CAISO to establish a default greenhouse gas price using the best information available.[30]

19. PG&E recommends that the Commission order CAISO to produce a technical paper further detailing two aspects of the CAISO proposal. First, PG&E contends that, with regard to the greenhouse gas emissions rate authorized by CARB, additional clarification is needed concerning when and how CAISO will receive this information from CARB and how this information will be used.[31] Second, PG&E contends that additional information is needed as to the specific greenhouse gas price indices CAISO will use and the methodology by which CAISO will determine the relevant greenhouse gas prices from these indices.[32]

20. In reply, CAISO contends that when and how CAISO will receive the greenhouse gas emissions rate from CARB is an implementation detail that does not affect the use of that rate, or the justness and reasonableness of that rate. CAISO asserts that it is working with CARB to ensure that it receives the emissions rate in a timely manner.[33] CAISO also claims that there is no need for a technical paper explaining how the greenhouse gas emissions rate will be used. According to CAISO, sections 30.4.1.1.1 and 39.7.1.1.1.1(b) specify exactly how CAISO will utilize the emissions rate received from the CARB. CAISO contends that the emissions rate has no use to CAISO other than as a component of the calculations set forth in these tariff sections.[34]

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[30] CAISO November 28, 2012 Answer to Motions to Intervene and Comments, Motion to File Answer, and Answer to Protest at 6-7 (CAISO Answer).

[31] PG&E November 19, 2012 Motion to Intervene and Comments at 3 (PG&E Comments).

[32] *Id.* at 3-4.

[33] CAISO Answer at 3.

[34] *Id.*

21. CAISO also objects to PG&E's contention that CAISO should produce a technical paper that states the specific indices CAISO will use and the methodology by which CAISO will determine the greenhouse gas allowance price from the indices. CAISO notes that on November 9, 2012, it posted proposed revisions to the Business Practice Manual that set forth implementation details related to the tariff amendment at issue in this proceeding for stakeholder review. According to CAISO, the revised Business Practice Manual includes details regarding the specific indices and the methodology for determining the greenhouse gas allowance price pursuant to those indices. CAISO contends that the Business Practice Manual is the more appropriate location for details such as the name of the indices and other implementation details that may need to be changed quickly. CAISO claims that this flexibility is appropriate in the area of greenhouse gas costs due to the absence of historic information and the need to make midcourse corrections concerning implementation details in a faster and more efficient manner.[35]

22. While Calpine generally supports the methodology proposed to calculate the costs of compliance with the California Program,[36] Calpine objects to CAISO's reliance on unaveraged daily index prices for greenhouse gas allowances. Specifically, Calpine contends that CAISO's proposed reliance on daily index prices for greenhouse gas allowances, rather than an averaging of daily index prices, does not comport with the Commission's precedent on minimum standards for any energy price index used in a Commission-approved tariff.[37] Further, Calpine asserts that the Commission's *Policy Statement on Natural Gas and Electric Price Indices*[38] and the subsequent Staff Report[39] militate in favor of using a rolling average of daily index prices over multiple days. In addition, Calpine argues that, given that California's greenhouse gas allowance market is brand new and will likely exhibit illiquidity and price instability, and that greenhouse gas allowance price index developers will have no track record from which to evaluate index quality, it is imperative that section 39.7.1.1.1.4 incorporate averaging of daily

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[35] *Id.* at 4-5.

[36] Calpine November 19, 2012 Protest at 1 (Calpine Protest).

[37] *Id.* at 3 (citing *Policy Statement on Natural Gas and Electric Price Indices,* 104 FERC ¶ 61,121 (2003); *Staff Report on Natural Gas and Electricity Price Indices,* Docket Nos. PL03-3-004 and AD03-7-004 (May 5, 2004); *Cal. Indep. Sys. Operator Corp.,* 108 FERC ¶ 61,022 (2004); *Cal. Indep. Sys. Operator Corp.,* 105 FERC ¶ 61,140 (2003); and *WestConnect*, 126 FERC ¶ 61,105 (2009)).

[38] 104 FERC ¶ 61,121 (2003) (Policy Statement).

[39] *Staff Report on Natural Gas and Electricity Price Indices,* Docket Nos. PL03-3-004 and AD03-7-004 (May 5, 2004) (Staff Report).

greenhouse gas index prices, across both available price index developers and consecutive days. Accordingly, Calpine recommends using a rolling three-day average of each index publisher's daily index prices to smooth out the effects of expected volatility and illiquidity of the new California greenhouse market.

23. CAISO argues that Calpine has failed to explain why CAISO's proposal is not just and reasonable. In support, CAISO notes that "[p]ursuant to section 205 of the FPA, the Commission limits its evaluation of a utility's proposed tariff revisions to an inquiry into whether the rates proposed by a utility are reasonable – and not to extend to determining whether a proposed rate schedule is more or less reasonable to alternative rate designs."[40] Further, regarding Calpine's assertion that the Commission's Policy Statement and Staff Report militate in favor of using a rolling average of daily index prices over multiple days, CAISO argues that Calpine does not cite to any directive in the Policy Statement that indicates CAISO's proposed approach of using daily index prices, without a rolling average, is not just and reasonable.[41] Further, according to CAISO, the Staff Report and Policy Statement do not speak to using a rolling average of daily index prices. CAISO argues that, instead, the Commission found that price indices may be determined either by averaging across several index developers for the same time period or averaging over several time periods from the same developer.[42] Therefore, CAISO requests that the Commission find that its proposal is just and reasonable and accept the proposal as filed.

24. In its motion for a technical conference, PacifiCorp requests that the Commission institute a technical conference to address the impact of the California Program on the energy markets in the west.[43] PacifiCorp believes that the California Program will result in higher locational marginal prices at nodes on the borders with the CAISO system.[44] According to PacifiCorp, to the extent that the California Program increases wholesale energy prices at the CAISO border nodes, it will likely increase the cost of energy that

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[40] CAISO Answer at 9 (citing *Cal. Indep. Sys. Operator Corp.*, 141 FERC ¶ 61,135, at P 44 n.43 (2012), quoting *City of Bethany v. FERC*, 727 F.2d 1131, 1136 (D.C. Cir. 1984)).

[41] CAISO Answer at 10.

[42] *Id.*

[43] PacifiCorp December 3, 2012 Motion for Technical Conference at 1 (PacifiCorp Motion).

[44] *Id.* at 6.

PacifiCorp purchases at these nodes to serve its customers.[45] Finally, PacifiCorp is concerned that prices in the Western Electricity Coordinating Council (WECC) will rise in unison with the California prices even if the WECC prices do not include greenhouse gas allowance costs.[46]

IV. Discussion

A. Procedural Matters

25. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2012), the timely, unopposed motions to intervene serve to make the entities that filed them parties to the proceeding.

26. Pursuant to Rule 214(d) of the Commission's Rules of Practice and Procedure, 18 C.F.R § 385.214(d) (2012), the Commission will grant Portland's late-filed motion to intervene given its interest in this proceeding, the early stage of the proceeding, and the absence of undue prejudice or delay.

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

28. With regard to PacifiCorp's motion for a technical conference, we find that PacifiCorp's request exceeds the scope of this proceeding. This proceeding addresses the narrow issue of whether CAISO's proposed methodology for including greenhouse gas allowance costs in the calculations set forth in the CAISO tariff for determining resource commitment costs, default energy bids and generated bids is just and reasonable. In contrast, PacifiCorp requests a broad investigation into the effect of the California Program on the energy markets in the west. Thus, we finding that the current proceeding is not the appropriate forum in which to raise and address these issues. Therefore, we deny the motion for technical conference.

B. Substantive Matters

29. With the exceptions discussed below, we conditionally accept the proposed tariff revisions to become effective on January 1, 2013, as requested. As a general matter, we find that it is reasonable to incorporate the emissions costs of the greenhouse gas allowances into the calculation of generating units' variable costs as calculated in

[45] *Id.* at 7.

[46] *Id.* at 8.

CAISO's tariff. Such a revision is required in order to provide generators a reasonable opportunity to recover their variable energy costs incurred as a result of the California Program.

30. We find that CAISO's proposed methodology to include the greenhouse gas allowance cost adder is just and reasonable. Generally, for natural gas-fired units that are obligated to comply with the California Program, CAISO's proposed greenhouse gas allowance cost adder contains three components: (1) the generators' heat rate or fuel requirements; (2) the greenhouse gas emissions rate authorized by CARB; and (3) the applicable greenhouse gas allowance price, which is based on specific allowance price indices. For non-natural gas-fired units that are obligated to comply with the California Program, the variable costs will be provided to CAISO by the applicable scheduling coordinator and must be consistent with the information submitted to the CARB and are subject to review by CAISO pursuant to the tariff. This methodology will properly account for the variable costs of generation and provide generators a reasonable opportunity to recover their costs. Accordingly, we accept these proposed revisions.

31. Similarly, we find that CAISO's proposal to establish a greenhouse gas allowance price by averaging at least two prices from two or more publications is just and reasonable, and will accept this aspect of the proposal. We are not persuaded by Calpine's arguments that CAISO's proposal to use the average of daily greenhouse gas allowance prices is not just and reasonable. Calpine relies on the Commission's guidance regarding the types of price indices that jurisdictional entities can use provided in the Policy Statement. In the subsequent Staff Report, staff noted that using a composite index made by averaging more than one index can avoid gaps in index availability. The Staff Report therefore suggested that entities may choose to average across several index developers for the same time period or average over several time periods from the same developer.[47] We find that CAISO's proposal is consistent with this element of the Staff Report's guidance because CAISO will average across several index developers for the same time period.

32. Furthermore, as CAISO explains, the Policy Statement does not discuss the merits of using daily price indices versus rolling averages of daily price indices. Thus, Calpine's arguments are not supported by the Policy Statement. Indeed, we find that Calpine failed to explain why CAISO's proposal is not just and reasonable. Calpine instead explains why it believes its own proposal is superior to CAISO's proposal. However, the issue here is whether or not CAISO's proposal is just and reasonable. We find that it is. We find that the greenhouse gas allowance price established from the daily price indices will strike the right balance between sufficiently reflecting the daily fluctuation in greenhouse gas allowance prices and ensuring that generators have the

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[47] Staff Report at 56-57.

opportunity to recover their costs. Accordingly, we will accept CAISO's proposal to use the average of daily greenhouse gas allowance prices as just and reasonable.

33. Finally, we do not agree with PG&E that additional clarification is needed regarding when and how CAISO will communicate with CARB, and how CAISO will use the greenhouse gas emissions rate authorized by CARB. As an initial matter, how CAISO will receive the greenhouse gas emissions rate authorized by CARB does not affect the rate itself. Furthermore, we find that the level of detail CAISO uses to explain the emissions rate is reasonable and consistent with the level of detail in explanations for similar mechanisms in the CAISO tariff. Accordingly, we will not require CAISO to provide additional detail or produce a technical paper as requested by PG&E.

1. <u>Alternative Methodology</u>

34. While we accept CAISO's proposal to include a greenhouse gas allowance cost adder in the variable cost of generation, we find that CAISO has not demonstrated that its alternative methodology for calculating the greenhouse gas allowance price is just and reasonable and that this alternative methodology may be unjust, unreasonable, unduly discriminatory or preferential or otherwise unlawful. CAISO proposes to incorporate the alternative methodology as a backstop, in the event that published prices are determined by CAISO not to reflect market fundamentals or if the published prices are not available for an extended period. We note that this methodology has yet to be finalized and was just recently made available for stakeholder review.[48] Furthermore, the details of the proposed methodology were not presented to the Commission since CAISO elected to include the alternative methodology in its Business Practice Manual rather than in its tariff.

35. We conclude that any alternative methodology for calculating greenhouse gas allowance costs must be included in the tariff rather than in the Business Practice Manual. Generally, when a public utility adopts a rule, standard or practice that significantly affects its rates, the Commission requires the public utility to make a filing pursuant to FPA section 205 to amend its tariff.[49] The Commission uses a "rule of reason" test to determine which rules, standards, and practices significantly affect rates and services and must be included in the tariff.[50] The Commission has stated that the rule

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[48] *See* CAISO Answer at 7-8.

[49] *Preventing Undue Discrimination and Preference in Transmission Service*, Order No. 890, FERC Stats. & Regs. ¶ 31,241, at P 1633 (2007) (citing *City of Cleveland v. FERC*, 773 F.2d 1368, 1376 (D.C. Cir. 1985)) (Order No. 890).

[50] *Id.* P 1649.

of reason test requires a case-by-case analysis of what is in the tariff as opposed to what may be included in the Business Practice Manual.[51]

36. In this instance, we find that any alternative method for calculating greenhouse gas allowance costs adopted by CAISO will clearly affect rates for service and as a consequence should be detailed in the tariff. Therefore, we have determined that if CAISO elects to use an alternative methodology, it must file a tariff amendment seeking Commission acceptance of its chosen method. Accordingly, we will reject CAISO's proposed alternative methodology, without prejudice to it submitting in a separate filing under FPA section 205, its finalized methodology as part of its tariff.

37. Finally, we note that in the description of the alternative methodology which CAISO provided to the Commission, CAISO extends to itself very broad discretion to determine when use of the alternative methodology may be necessary.[52] We are concerned about the lack of objective standards in the proposed formulation of the alternative methodology. We encourage CAISO to consider whether more objective criteria can be developed which will still afford CAISO the necessary flexibility to respond to unusual events.

2. <u>Greenhouse Gas Allowance Price Indices</u>

38. CAISO proposes to state the price indices it will use to calculate the greenhouse gas allowance price in the Business Practice Manual, rather than in the tariff. CAISO also proposes to remove from its tariff the natural gas price indices it uses for the default energy bid and state the indices in the Business Practice Manual. CAISO explains that it made this modification to recognize that the indices and names of indices used to calculate the natural gas may change over time, and that maintaining this information in the Business Practice Manual will enable CAISO to make the change promptly.

39. We find that CAISO has not provided sufficient justification as to why price indices, which significantly affect CAISO's rates, are more appropriately kept in the Business Practice Manual rather than the tariff. Since the price indices CAISO will use to calculate the greenhouse gas allowance price that will be paid to generators significantly affects rates, that information must be in the tariff. The Commission took this approach when it required the very provisions CAISO is proposing to remove from

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[51] *See Cal. Indep. Sys. Operator Corp.*, 122 FERC ¶ 61,271, at P 17 (2008) (citing *Cal. Indep. Sys. Operator Corp.*, 116 FERC ¶ 61,274, at P 1370 (2006)).

[52] In proposed section 39.7.1.1.1.4, CASIO states that it will use the alternative methodology if "one or more published prices **are determined by the CAISO** not to reflect market fundamentals or if published prices are not available for an extended period." (Emphasis added).

section 39.7.1.1.1.3 to be in the tariff. In that case, the Commission agreed with a protestor that "CAISO should specify in its MRTU Tariff the price indices it will rely on."[53] CAISO has not provided sufficient justification to change the Commission's prior finding. Therefore, we direct CAISO to submit a compliance filing that incorporates the names of the specific price indices for use in determining the greenhouse gas allowance price and default energy bid into the tariff within 15 days of the issuance of this order. We believe that this determination also addresses PG&E's concern that more information is needed with regard to the specific indices that CAISO will use to establish the greenhouse gas allowance price.

<u>The Commission orders</u>:

(A) CAISO's proposed tariff revisions are hereby conditionally accepted in part and rejected in part to become effective on January 1, 2013, as requested, as discussed in the body of this order.

(B) CAISO is hereby directed to submit a compliance filing within 15 days of issuance of this order to include in its tariff the greenhouse gas emissions allowance price indices it will use to calculate the greenhouse gas allowance price and remove all references and discussion of the alternative methodology, as discussed in the body of this order.

(C) PacifiCorp's Motion for Technical Conference is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

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[53] *Cal. Indep. Sys. Operator Corp.*, 119 FERC ¶ 61,076, at P 502 (2007).