

May 25, 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 Nos. RM10-13-\_\_\_\_, ER11-3973-\_\_\_\_, ER12-\_\_\_\_**

Dear Secretary Bose:

By this filing, the California Independent System Operator Corporation (“ISO”) respectfully submits revisions to the ISO tariff in compliance with Order No. 741.<sup>1</sup> The provisions establish the ISO as the central counterparty for all transactions settled by the ISO and make other revisions to accommodate this change of status. The ISO requests an effective date of September 1, 2012. The change must become effective at the beginning of a month in order to ensure legal clarity with respect to monthly settlement charges. An effective date approximately three months after filing will be consistent with the Commission’s direction in Order 741-A.<sup>2</sup>

## **I. BACKGROUND**

Through Order No. 741, issued on October 10, 2010, the Commission sought to improve the management of risk and the use of credit in organized markets operated by independent system operators and regional transmission organizations. The order required seven market modifications:

- (1) shortened settlement times to no more than seven days;
- (2) restrictions on the use of unsecured credit;
- (3) elimination of unsecured credit in all financial transmission rights or equivalent markets;
- (4) steps to address the risk that the organization may not be allowed to use netting and set-offs in bankruptcy proceedings;
- (5) establishment of minimum criteria for market participation;

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<sup>1</sup> *Credit Reforms in Organized Wholesale Markets*, 133 FERC ¶ 61,060 (2010), *on reh’g* Order No. 741-A, 134 FERC ¶ 61,126, *reh’g denied*, Order No. 741-B, 135 FERC ¶ 61,242 (2011).

<sup>2</sup> Order No. 741-A at P 25.

- (6) clarification regarding the organized market administrators' ability to invoke a "material adverse change" to demand additional collateral; and
- (7) a standardized grace period of no more than two days for curing collateral calls.

Order No. 741 initially established a June 30, 2011 compliance date. The ISO's compliance date for item (4) has been extended in a series of orders, however, beginning with Order No. 741-A,<sup>3</sup> to May 25, 2012.

The ISO has previously made its compliance filings for all requirements of Order 741-A, except item (4). This filing addresses the item (4) modifications required to address the risk that a bankruptcy court might prevent the organization from netting and set-offs. Section 35.47(d) of Title 18, Code of Federal Regulations, promulgated in Order No. 741, provides organized wholesale electric markets with four options for controlling this risk:

Establish a single counterparty to all market participant transactions, or require each market participant in an organized wholesale electric market to grant a security interest to the organized wholesale electric market in the receivables of its transactions, or provide another method of supporting netting that provides a similar level of protection to the market and is approved by the Commission. In the alternative, the organized wholesale electric market shall not net market participants' transactions and must establish credit based on market participants' gross obligations.

## II. STAKEHOLDER PROCESS

The ISO initiated its stakeholder process on Order No. 741 with a meeting in Folsom on February 2, 2011. With respect to item (4), the ISO presented the four approaches described in the Commission's regulation:

1. The ISO could become the central counterparty to all market transactions;
2. The ISO could require that market participants either grant the ISO a security interest in their market receivables; or
3. The ISO and stakeholders could develop an alternative that would offer the same degree of protection against the perceived risk, taking into account the Commission's statement that that it would not be sufficient to be more

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<sup>3</sup> *Id.*

specific in the tariff about the ISO's ability to net market payments.

In the alternative, the ISO could choose not to net transactions and to establish credit based on market participants gross transactions.<sup>4</sup>

Stakeholders indicated general support for the first approach. They expressed significant concerns regarding the second approach, particularly with regard to the potential impact on existing or potential lending agreements or bond covenants. Stakeholders also indicated that some market participants could not comply with an obligation to post security on a "gross obligation," as the increased collateral requirements would be substantial. The general consensus at the February 2, 2011 meeting was that the viability of this approach depended on a better understanding of the term "gross obligation" and, in particular, on the Commission granting NYISO's then-pending motion for clarification, which sought confirmation that netting financial obligations within categories of products and services would be consistent with requiring financial security based on the market participant's "gross obligation." Subsequently, the Commission issued Order No. 741-A, in which it denied that request.<sup>5</sup>

Neither the ISO nor any market participant was able to identify an alternative that might satisfy FERC's requirements for the third approach. Accordingly, based on the affirmative stakeholder interest in the central counterparty approach, the Commission's clarification that the gross obligation approach did not permit netting within product categories, and the lack of a viable alternative, the ISO proceeded to investigate potential issues that might arise from its central counterparty status and the mechanisms to resolve those issues.

During the period following the initial stakeholder meeting, the ISO has worked with outside advisors to understand and address the implications of becoming a central counterparty. This included obtaining rulings from the Internal Revenue Service and the Franchise Tax Board confirming that the change will not jeopardize the ISO's tax-exempt status. Based on the information it gleaned from these efforts, the ISO developed a discussion paper and draft tariff language which it posted on May 7, 2012, with a request for comments. The discussion paper is included with this filing as Attachment C.

The ISO conducted a stakeholder conference call to discuss comments on May 18, 2012, and posted revised tariff language on May 21. The ISO followed up with another stakeholder call on May 23.

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<sup>4</sup> See 18 C.F.R. § 35.47(d).

<sup>5</sup> Order No. 741-A at PP 18, 22-23.

### **III. TARIFF REVISIONS**

The proposed tariff revisions make three core changes. First, the ISO must become a counterparty to market transactions. To this end, the ISO proposes to revise section 11.29(a) to read, in part, as follows:

[T]he CAISO shall be the contracting counterparty, in its own name and right, to each Scheduling Coordinator, CRR Holder, Black Start Generator, or Participating TO for any purchase or sale of any product or service, or for any other transaction, that is financially settled by the CAISO under the CAISO Tariff.

The ISO also proposes to delete the sentence from section 22.13 that provides that the ISO is acting solely as an agent for scheduling coordinators in transactions for imbalance energy and ancillary services.

Section 11.29(a) includes an exception to counterparty status for energy procured for use in Mexico. For these transactions, the ISO will continue to act as an agent for the respective scheduling coordinators. This exception maintains the status quo in order to ensure compliance with applicable Mexican law. ISO New England included an analogous provision in its compliance tariff revisions to address restrictions on the ability of certain tax exempt members to sell energy to a central counterparty.<sup>6</sup>

This subsection also includes language to expressly confirm that the central counterparty status and every other subsection and aspect of Section 11.29 will apply prospectively only. Thus they will not apply to reruns or other adjustments of past trade dates.

Proposed section 11.29(b) includes language intended to maintain the status quo with respect to any product warranties. This provision is also similar to one filed by ISO New England.<sup>7</sup>

To more precisely define its status as counterparty, and to reduce the possibility that it could be misconstrued by a bankruptcy court to the disadvantage of market participants and the ISO, the ISO proposes to revise a few other tariff provisions. These include sections 11.29.7.2 and 11.29.8.7 (explicitly connecting the limitation of liability to statements about the ISO's obligation to pay), 11.29.10 (clarifying the obligation to pay invoices), and

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<sup>6</sup> See Market Rule I, Section III, as proposed by ISO-NE in its April 30, 2012, filing in Docket No. ER12-1651.

<sup>7</sup> The ISO also proposes to revise section 11.29 to add the word "net" to clarify the phrase "net amounts."

11.29.13.7 (clarifying that the setoff and recoupment rights are not intended to alter the provisions about invoicing).

Second, the ISO assumes the right to pursue collection on behalf of the market for any market participant defaults that cannot be covered through financial security. The ISO proposes to delete section 11.29.21, which places responsibility for pursuing collection of market participant defaults on scheduling coordinators. The proposed revisions to section 11.29.20 reassign this responsibility to the ISO.

Third, the ISO proposes certain revisions to ensure that, despite the two changes discussed above, the ISO will continue to be revenue neutral in the event of a default, with any shortfall due to the default being shared among market participants. This is consistent with the Commission's approval of similar provisions for PJM.<sup>8</sup> The proposed revisions to section 11.29.17.1 limit the liability of the ISO in the event of a default that cannot be recovered from financial security posted with the ISO. Specifically, the liability of the ISO to make payment for any given settlement period is limited so that the aggregate of the payments does not exceed the aggregate amount that has been paid to or recovered by the ISO for that settlement period.

The limitation of liability clause in section 11.29.17.1 accounts for use of both the CAISO Reserve Account and CAISO Penalty Reserve Account, which can be used to support market clearing on a temporary basis until a defaulted payment is recovered. The ISO proposes revision to two sections that govern the use of these accounts, 11.29.9.6.2.1 and 11.29.9.6.4.1, to clarify that any payments from the accounts must be replenished, and to ensure transparency of transactions through which these accounts are replenished and payment shortfalls are allocated to the market.

To conform the remainder of the tariff with these core changes, and clarify certain requirements regarding accounts, the ISO proposes minor revisions to a number of other provisions, such as deleting language indicating that payments by scheduling coordinators are due to other scheduling coordinators rather than to the ISO, and statements that market payments to the ISO are being held in trust by the ISO for market participants. Such conforming changes can be found in Sections 11.29.3(g), 11.29.9.1, 11.29.9.2, 11.29.9.4, 11.29.9.5, 11.29.9.6.2, 11.29.9.6.2.1, 11.29.9.6.4, 11.29.9.6.4.1, 11.29.11, 11.29.12, 11.29.16, 11.29.19.3, and the definitions of "CAISO Account," "CAISO Clearing Account" and "CAISO Reserve Account."

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<sup>8</sup> See Section 14B.4(e) of PJM's tariff amendment, filed May 5, 2010 in Docket No. ER10-1196, and conditionally accepted in *PJM Interconnection, L.L.C.*, 132 FERC ¶ 61,207 (2010).

The ISO is also proposing revisions to address potential unintended and problematic consequences of counterparty status. Proposed new section 4.5.3.14 requires each scheduling coordinator to provide a resale certificate or proof that the seller is exempt from sales or use taxes. Based on outside advice, the ISO does not believe that it will incur new tax liability as a result of the proposed tariff revisions. Nonetheless, the ISO has been advised to obtain such documentation to support the exemptions.

In addition, the ISO and its stakeholders have been concerned that the revision of section 11.29 could be misinterpreted to mean that the ISO is to be a purchasing/selling entity listed on an E-Tag, which could result in the ISO becoming the entity responsible for procuring emissions permits.<sup>9</sup> The general consensus of the stakeholders and the Air Resources Board is that the ISO should not be the entity with this responsibility. From the stakeholders' perspective, this is not desirable because the ISO would have to pass on additional costs to market participants. Moreover, ISO responsibility for procuring emissions permits would undermine the purpose of the greenhouse gas regulation because the ISO is not in a position to respond to the incentives by selecting a generation source with lower emissions. Consequently, for clarity, section 4.5.3.2.2 has been revised to add the following:

For purposes of E-Tags, the CAISO is not, and shall not be listed as, the "Purchasing Selling Entity"; title to Energy shall pass directly from the entity that holds title when the Energy enters the CAISO Controlled Grid to the entity that removes the Energy from the CAISO Controlled Grid, in each case in accordance with the terms of this CAISO Tariff.

#### **IV. REQUEST FOR WAIVER**

As a central counterparty, the ISO could be subject to Commission regulations governing the sale of energy at market-based rates. As a nonprofit corporation, and in its role as a revenue-neutral counter-party, however, the ISO

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<sup>9</sup> Under the final rule of the California Air Resources Board, posted on December 14, 2011, Final Regulation Order for the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, title 17, California Code of Regulations, section 95800 to 96023, liability for procuring the emissions permits associated with electricity imported into California rests with the party that brings the energy into the ISO grid. Specifically, section 95802 states that "[f]or electricity delivered between balancing authority areas, the electricity importer" – that is, the entity obligated to purchase emissions permits – "is identified on the NERC E-tag as the purchasing selling entity (PSE) on the last segment of the tag's physical path with the point of receipt located outside the state of California and the point of delivery located inside the state of California."

does not negotiate prices in its markets; the ISO operates solely as a conduit for sales by entities operating under market-based rate authority. The ISO therefore requests that the Commission waive two sets of requirements that might otherwise apply:

- Regulations regarding market-based rate authorization and wholesale sale of electric energy, capacity, and ancillary services at market-based rates.<sup>10</sup>
- EQR reporting requirements that arise from serving as a central counterparty.

The Commission has granted PJM a waiver of these provisions for the same reasons.<sup>11</sup>

The ISO also requests that the Commission clarify that the ISO will not be subject, under section 382.201 of the Commission's regulations, to any greater reporting obligations or annual charges than those to which it is currently subject. Counterparty status does not change the nature of the transmission services that the ISO provides.

## **V. COMMUNICATIONS**

Please direct communications regarding this filing to the following persons:

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\* Persons designated for service.

## **VI. ATTACHMENTS**

In addition to this transmittal letter, the following documents support the instant filing.

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<sup>10</sup> See 18 C.F.R. §§ 35.36-35.42

<sup>11</sup> See PJM Interconnection, L.L.C., 132 FERC ¶ 61,207 (2010), at PP 56-61.

- Attachment A**      Revised CAISO Tariff Sheets – Clean
- Attachment B**      Revised CAISO Tariff Sheets – Blackline
- Attachment C**      Discussion Paper posted May 7, 2012

**VII. CONCLUSION**

For the reasons discussed above, the ISO requests that the Commission approved the ISO's proposed tariff revisions as compliant with Order No. 741.

Respectfully submitted,

**By: /s/ Daniel J. Shonkwiler**

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## CERTIFICATE OF SERVICE

I hereby certify that I have served the foregoing document upon all parties listed on the official service list in the captioned 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 25<sup>th</sup> day of May, 2012.

*Anna Pascuzzo*  
Anna Pascuzzo

**Attachment A – Clean Tariff Language**  
**Order 741 Compliance Filing – Central Counterparty**  
**California Independent System Operator Corporation**  
**Fifth Replacement FERC Electric Tariff**  
**May 25, 2012**

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#### **4.5.3.14 Tax Compliance**

Providing, as described in the Business Practice Manuals, resale certificates or other proof acceptable to CAISO that its purchases of energy are exempt from any sales and use taxes that otherwise might apply.

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**4.5.3.2.2** Submitting Interchange Schedules prepared in accordance with all NERC, WECC and CAISO requirements, including providing E-Tags for all applicable transactions pursuant to WECC practices.

For purposes of E-Tags, the CAISO is not, and shall not be listed as, the “Purchasing Selling Entity”; title to Energy shall pass directly from the entity that holds title when the Energy enters the CAISO Controlled Grid to the entity that removes the Energy from the CAISO Controlled Grid, in each case in accordance with the terms of this CAISO Tariff.

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#### **11.29 CAISO as Counterparty; Billing and Payment;**

- (a) The CAISO shall be the contracting counterparty, in its own name and right, to each Scheduling Coordinator, CRR Holder, Black Start Generator, or Participating TO for any purchase or sale of any product or service, or for any other transaction, that is financially settled by the CAISO under the CAISO Tariff, except under the following circumstances:
  - (i) The CAISO shall not be the contracting counterparty for transactions that procure Station Power for a Generating Unit located in Mexico or for transactions that procure Energy or Ancillary Services within Mexico; for such transactions, the CAISO will not act as principal but instead as agent for and on behalf of the relevant Scheduling Coordinators.
  - (ii) The provisions of this Section 11.29 will not apply to the billing and payment of transactions associated with Trading Days that occurred prior

to September 1, 2012. Billing and payment of such transactions shall be governed by the terms of the tariff effective on the Trading Days.

- (b) The purchase of sale of any products or service, or any other transaction, that is financially settled by CAISO under this CAISO Tariff shall be deemed to occur within the State of California. To the extent permitted by applicable law, any warranties provided by the sellers to the CAISO of such products or services, whether express, implied or statutory, are hereby passed to the Business Associates who purchase such products or services from the CAISO on a “pass through basis” and to the extent not passed through, any such warranties are hereby assigned by the CAISO to the purchasing Business Associates. Sellers to the CAISO and Business Associates acknowledge that warranties on such products are limited to that offered by the seller to CAISO and will exist, if at all, solely between the seller to the CAISO and the purchasing Business Associate. AS BETWEEN THE PURCHASING BUSINESS ASSOCIATE AND THE CAISO AS COUNTERPARTY, NO EXPRESS OR IMPLIED WARRANTIES ARE MADE BY THE CAISO REGARDING THE PRODUCTS AND SERVICES SOLD BY THE CAISO AS COUNTERPARTY, AND ANY SUCH PRODUCTS AND SERVICES ARE PROVIDED ON AN “AS IS” AND “AS AVAILABLE” BASIS. THE CAISO MAKES NO WARRANTY OR REPRESENTATION THAT THE PRODUCTS OR SERVICES WILL BE UNINTERRUPTED OR ERROR FREE. PURCHASING BUSINESS ASSOCIATES HEREBY WAIVE, AND THE CAISO HEREBY DISCLAIMS, ALL OTHER WARRANTIES, EXPRESSED OR IMPLIED, INCLUDING, WITHOUT LIMITATION, ANY WARRANTY OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, TITLE AND NON-INFRINGEMENT. THE CAISO DOES NOT WARRANT THAT THE PRODUCTS AND SERVICES OFFERED WILL MEET CUSTOMER’S REQUIREMENTS. NO ORAL OR WRITTEN INFORMATION OR ADVICE GIVEN BY THE CAISO OR ANY AUTHORIZED REPRESENTATIVE OF THE

CAISO SHALL CREATE A WARRANTY OR IN ANY WAY INCREASE THE SCOPE OF ANY PASS THROUGH OR ASSIGNED WARRANTY. SOME JURISDICTIONS DO NOT ALLOW THE EXCLUSION OF IMPLIED WARRANTIES IN CERTAIN CIRCUMSTANCES, SO THE ABOVE EXCLUSION APPLIES ONLY TO THE EXTENT PERMITTED BY APPLICABLE LAW.

- (c) The CAISO will calculate for each charge the amounts payable by the relevant Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO for each Settlement Period of the Trading Day, and the amounts payable to that Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO for each charge for each Settlement Period of that Trading Day and shall arrive at a net amount payable for each charge by or to that Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO for each charge for that Trading Day. Each of these net amounts will appear in the Settlement Statements that the CAISO will provide to the relevant Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO.
- (d) The components of the Grid Management Charge will be included in an Initial Settlement Statement T+3B, and any Recalculation Settlement Statement with the other types of charges referred to in Section 11.

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### **11.29.3**

#### **Prepayments**

- (a) A Scheduling Coordinator or CRR Holder may choose to pay at an earlier date than the Payment Date specified in the CAISO Payments Calendar by way of prepayment provided it notifies the CAISO by electronic means before submitting its prepayment.
- (b) Prepayment notifications must specify the dollar amount prepaid.

- (c) Prepayments must be made by Scheduling Coordinators or CRR Holder via Fed-Wire into their CAISO prepayment account designated by the CAISO. The relevant Scheduling Coordinator or CRR Holder shall grant the CAISO a security interest on all funds in its CAISO prepayment account.
- (d) On any Payment Date the CAISO shall be entitled to cause funds from the relevant Scheduling Coordinator's or CRR Holder's CAISO prepayment account to be transferred to the CAISO Clearing Account in such amounts as may be necessary to discharge in full that Scheduling Coordinator's or CRR Holder's payment obligation arising in relation to that Payment Date by way of set-off or recoupment.
- (e) Any funds held in the relevant Scheduling Coordinator's or CRR Holder's CAISO prepayment account shall be treated as part of that Scheduling Coordinator's or CRR Holder's Financial Security.
- (f) Interest (or other income) accruing on the relevant Scheduling Coordinator's or CRR Holder's CAISO prepayment account shall inure to the benefit of that Scheduling Coordinator or CRR Holder and shall be added to the balance of its CAISO prepayment account on a monthly basis.
- (g) Funds held in a CAISO prepayment account by a Scheduling Coordinator or CRR Holder may be recouped, offset or applied by the CAISO to any outstanding financial obligations of that Scheduling Coordinator or CRR Holder to the CAISO.

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#### **11.29.7.2 Basis for Billing and Payment**

The Initial Settlement Statement T+3B and any Recalculation Settlement Statement shall constitute the basis for billing in accordance with this CAISO Tariff. The Initial Settlement Statement T+3B shall constitute the basis for billing for all charges in the first instance. The Recalculation Settlement Statements T+12B and T+55B shall constitute the basis for billing for adjustments to charges set forth in the Initial Settlement Statement T+3B. Each Scheduling Coordinator, CRR Holder, Black Start

Generator, and Participating TO shall pay any net debit and, subject to the limitations in Section 11.29.17.1, shall be entitled to receive any net credit shown in its Invoice or Payment Advice on the Payment Date, whether or not there is any dispute regarding the amount of the debit or credit.

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#### **11.29.8.7 Payment Pending Dispute**

Each Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO which receives an Invoice or Payment Advice shall pay any net debit and, subject to the limitations in Section 11.29.17.1, shall be entitled to receive any net credit shown in the Invoice or Payment Advice on the Payment Date, whether or not there is any dispute regarding the amount of the debit or credit. The provisions of Section 13 shall apply to the disputed amount.

#### **11.29.9 Payment Procedures**

##### **11.29.9.1 Payments By and to the CAISO**

All Scheduling Coordinators, CRR Holders, Black Start Generators, and Participating TOs shall discharge their obligations to pay the amounts owed by them and shall receive payments of all amounts owed to them solely in accordance with this CAISO Tariff.

##### **11.29.9.2 CAISO Accounts to be Established**

The CAISO is authorized to establish and maintain bank accounts and obtain lines of credit and other banking facilities (not exceeding an aggregate amount set by the CAISO Governing Board) necessary for the operation of its Settlement and billing procedures. Each such account shall be maintained at a bank or other financial institution in California. Unless otherwise specified in this CAISO Tariff the CAISO will recover all costs incurred in connection with these CAISO banking facilities through the appropriate component of the Grid Management Charge. The CAISO shall establish and operate the following accounts:

**11.29.9.2.1** A CAISO Clearing Account to and from which all payments under this Section 11.29 are made;

\* \* \*

**11.29.9.4 [Not Used]**

**11.29.9.5 No Co-Mingling**

To facilitate and better ensure accurate processing of payment defaults pursuant to Section 11.29.17.1, the CAISO shall not co-mingle any funds standing to the credit of a CAISO Account with its other funds and shall promptly withdraw any amounts paid into a CAISO Account representing amounts paid for the account of the CAISO.

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**11.29.9.6.2 Reserve Account**

The CAISO Reserve Account shall be available to the CAISO for the purpose of providing funds to clear the CAISO Clearing Account in the event that there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors. If there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors and clear the account on any Payment Date, due to payment default by one or more CAISO Debtors, the CAISO shall transfer funds from the CAISO Reserve Account to the CAISO Clearing Account to clear it by close of banking business on that Payment Date pursuant to Section 11.29.13.4. If the CAISO Reserve Account is drawn upon, the CAISO shall as soon as possible thereafter take any necessary steps against the defaulting Scheduling Coordinator or CRR Holder, including making any calculations or taking any other appropriate action, to replenish the CAISO Reserve Account including drawing on any credit support or other Financial Security provided by the defaulting Scheduling Coordinator or CRR Holder pursuant to Section 12 or serving demands on any defaulting Scheduling Coordinator or CRR Holder if Financial Security has been exhausted or if no Financial Security is available due to establishment of an Unsecured Credit Limit.

**11.29.9.6.2.1 Replenishing the CAISO Reserve Account Following Payment Default**

If the CAISO has debited the CAISO Reserve Account then:

- (a) If, after the CAISO has debited the CAISO Reserve Account on a Payment Date, the CAISO Bank receives a remittance from a CAISO Debtor which has not been (but should have been, if it had been received on a timely basis) credited to the CAISO Clearing Account by 10:00 am on the Payment Date and which required the debiting of the CAISO Reserve Account, such remittance shall be credited to the CAISO Reserve Account.
- (b) The proceeds of any enforcement of Financial Security and/or amounts recovered under proceedings shall be credited to the CAISO Reserve Account.
- (c) If, after taking reasonable action, the CAISO determines that the default amount (or any part) and/or Interest cannot be recovered on the next practicable Invoices, the CAISO shall notify Market Participants of the identity of the defaulting Business Associate together with the unrecoverable amounts and such amounts shall be allocated in accordance with Section 11.29.17 of the CAISO Tariff with corresponding credits to the CAISO Reserve Account..

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#### **11.29.9.6.4 CAISO Penalty Reserve Account**

- (a) The CAISO Penalty Reserve Account will be available to the CAISO for the purpose of using funds collected for late payments of amounts set forth in Invoices pursuant to Section 11.29.14(c) and for late postings of Financial Security pursuant to Section 12.5.2(c) to clear the CAISO Clearing Account in the event that there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors. If there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors and to clear the account on any Payment Date occurring on or after April 7, 2010, due to payment default by one or more CAISO Debtors, the CAISO shall transfer funds from the CAISO Penalty Reserve Account to the CAISO Clearing Account to clear it by close of banking business on that Payment Date pursuant to Section 11.29.13.4. If available funds in the CAISO Penalty Reserve Account are insufficient to clear the CAISO Clearing Account and the payment default is not cured, the payment default

will be allocated in accordance with the CAISO Tariff. After the payment default is allocated in accordance with the CAISO Tariff, any funds that are subsequently added to the CAISO Penalty Reserve Account can only be used to clear the CAISO Clearing Account pursuant to this Section 11.29.9.6.4 for payment defaults that occur after the funds were added to the CAISO Penalty Reserve Account. The CAISO Penalty Reserve Account will be an interest-bearing account separate from all other accounts maintained by the CAISO, and no other funds will be commingled in it at any time.

- (b) On December 31 of each year, the CAISO will draw any funds then available in the CAISO Penalty Reserve Account in excess of five (5) million dollars and will apply that excess to offset the following year's Grid Management Charge revenue requirement pursuant to Schedule 1 of Appendix F.
- (c) If the CAISO Penalty Reserve Account is drawn upon, the CAISO will as soon as possible thereafter take any necessary steps against the defaulting Scheduling Coordinator or CRR Holder, including making any calculations or taking any other appropriate action, to replenish the CAISO Penalty Reserve Account, including drawing on any credit support or other Financial Security provided by the defaulting Scheduling Coordinator or CRR Holder pursuant to Section 12 or serving demands on any defaulting Scheduling Coordinator if Financial Security has been exhausted or if no Financial Security is available due to establishment of an Unsecured Credit Limit.

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#### **11.29.9.6.4.1 Replenishment Following Payment Default**

If the CAISO has debited the CAISO Penalty Reserve Account, then:

- (a) If, after the CAISO has debited the CAISO Penalty Reserve Account on a Payment Date, the CAISO Bank receives a remittance from a CAISO Debtor which has not been (but should have been, if it had been received on a timely

basis) credited to the CAISO Clearing Account by 10:00 am on the Payment Date and which required the debiting of the CAISO Penalty Reserve Account, such remittance shall be credited to the CAISO Penalty Reserve Account, less any amounts due to Market Participants.

- (b) The proceeds of any enforcement of Financial Security and/or amounts recovered under proceedings shall be credited to the CAISO Penalty Reserve Account.
- (c) If, after taking reasonable action, the CAISO determines that the default amount (or any part) and/or Interest cannot be recovered, the CAISO shall notify Market Participants of the identity of the defaulting Business Associate together with the unrecoverable amounts and such amounts shall be allocated in accordance with Section 11.29.17 of the CAISO Tariff with corresponding credits to the CAISO Penalty Reserve Account.

#### **11.29.10 Billing And Payment**

The CAISO shall prepare and send to each Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO an Invoice or Payment Advice on Wednesday of each week. If Wednesday falls on a CAISO holiday, the CAISO will issue the Invoice or Payment Advice on the next Business Day. Each Invoice or Payment Advice shall show the amount that is payable by or to each Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO, which amount shall equal the positive or negative total of all net charges reflected on the relevant Settlement Statements, the Payment Date, being the date on which such amount is to be paid or received, and details of the CAISO Clearing Account to which any amounts owed by or to Scheduling Coordinators, CRR Holder, Black Start Generator or Participating TO is to be paid. Revenues owed from a Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO are expressed as a positive amount on an Invoice. Revenues owed to a Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO are expressed as a negative amount on a Payment Advice. Payments or charges for the items referred to in an Invoice or Payment Advice (except for the charges payable under long-term contracts) for each Trading Day shall be made four (4) Business Days after the date on which the weekly Invoice or Payment Advice is issued. If the fourth (4)

Business Day after an Invoice or Payment Advice is issued falls on a CAISO holiday, then the Payment Date for the Invoice or Payment Advice shall be the next Business Day.

\* \* \*

#### **11.29.11 Instructions For Payment**

Unless the CAISO instructs otherwise, each Scheduling Coordinator or CRR Holder shall remit to the CAISO Clearing Account the amount shown on the Invoice as payable by that Scheduling Coordinator or CRR Holder for value not later than 10:00 a.m. on the Payment Date. In the event of a verifiable error that would be reversed on a future Invoice or Payment Advice, the CAISO may instruct a Scheduling Coordinator or CRR Holder to reduce its payment in the amount of a specific charge reflected on an Invoice. Any such occurrence will not constitute a payment default under the CAISO Tariff. If the CAISO directs such a reduction in payment, it shall make offsetting adjustments on future Invoices or Payment Advices of Scheduling Coordinators, CRR Holders, Black Start Generators or Participating TOs that received settlement credits corresponding to the verifiably erroneous charge. The CAISO will inform those entities of the adjustments to their Invoices or Payment Advices.

#### **11.29.12 CAISO'S Responsibilities**

On the due date for payment of amounts shown in an Invoice, the CAISO shall ascertain whether all amounts required to be remitted to the CAISO Clearing Account have been credited to it. If any such amount has not been so credited, it shall ascertain which Scheduling Coordinators or CRR Holders have failed to pay the amount owed by them and it may, subject to any notice or cure provisions in this Section 11.29, exercise any rights available under the CAISO Tariff or under applicable law to recover any overdue amount.

\* \* \*

#### **11.29.13.7 Set-Off and Recoupment**

The CAISO is authorized to recoup, set off and apply any amount owed on any Payment Advice to which any defaulting CAISO Debtor is or will be entitled, in or towards the satisfaction of any of that CAISO Debtor's debts on any Invoice arising under the CAISO Settlement and billing process. Each CAISO Creditor and each CAISO Debtor expressly acknowledges the following application of funds: first to the

current month's Grid Management Charge, and then as described in 11.29.13.8 except as limited by Section 11.29.17. Nothing in this Section 11.29.13.7 shall be construed as affecting the methodology by which the CAISO determines the amounts of Invoices or Payment Advices.

\* \* \*

**11.29.16 Prohibition On Transfers**

The CAISO shall at no time instruct the CAISO Bank to transfer any sum from a CAISO Account to another account except as permitted under this CAISO Tariff.

**11.29.17 Alternative Payment Procedures**

**11.29.17.1 Pro Rata Reduction to Payments**

The obligation of the CAISO to pay Scheduling Coordinators, CRR Holders, Black Start Generators, Participating TOs, and any other Business Associates monies owed for a given settlement period shall be limited so that the aggregate liability of the CAISO for such payments does not exceed the sum of a) the amounts paid to the CAISO Clearing Account for that settlement period, b) additional amounts recovered by the CAISO by enforcing any Financial Security provided by a defaulting Scheduling Coordinator of CRR Holder to cover any shortfall for that settlement period, and c) amounts transferred to the CAISO Clearing Account from the CAISO Reserve Account and the CAISO Penalty Reserve Account to cover any shortfall for that settlement period. If it is not possible to clear the CAISO Clearing Account on a Payment Date because of an insufficiency of funds available in the CAISO Reserve Account or the CAISO Penalty Reserve Account, or by enforcing any Financial Security provided by a defaulting Scheduling Coordinator or CRR Holder, the CAISO shall, after deducting Grid Management Charge and FERC Annual Charges in accordance with Section 11.29.9.6.1, (1) first pay in full every CAISO Creditor whose net amounts receivable on the relevant Payment Date is less than \$5,000; and (2) second, reduce payments to all remaining CAISO Creditors proportionately to the net amounts payable to them on the relevant Payment Date to the extent necessary to clear the CAISO Clearing Account through a shortfall allocation. Each payment default amount allocated to CAISO Creditors through a shortfall allocation under this Section 11.29.17.1 that remains unpaid by the defaulting Scheduling Coordinator or CRR Holder will be allocated as set forth in Section 11.29.17.2. The provisions of this Section 11.29.17.1 shall not apply to non-payment of any penalty amount that a Scheduling Coordinator or CRR Holder has

disputed and FERC has specifically authorized the Scheduling Coordinator or CRR Holder to net its payment to the CAISO by the amount of the penalty in question in accordance with Section 37.9.3.

\* \* \*

### **11.29.19.3 Overpayment Held In Trust**

Until a CAISO Creditor refunds the overpayment to the CAISO, the CAISO Creditor shall be deemed to hold the amount of such overpayment on trust for CAISO.

\* \* \*

### **11.29.20 Defaults**

In addition to and not in lieu of any other events specified in this CAISO Tariff as constituting a default, the occurrence of any of the following events shall constitute a default under this CAISO Tariff:

- (a) If a Scheduling Coordinator or CRR Holder files a petition or otherwise commences, authorizes, or acquiesces in the commencement of a case, petition, proceeding, or cause of action under any bankruptcy or insolvency law or similar law for the protection of debtors or creditors; or
- (b) If a Scheduling Coordinator or CRR Holder has a petition, case, proceeding or cause of action filed or commenced against it and such case, petition, proceeding or cause of action is not withdrawn or dismissed within (30) days after such filing or commencement;

In the event of any default under the CAISO Tariff, the CAISO shall, in addition to any other remedies available at law in equity or under the CAISO Tariff, have the sole and exclusive right to take debt collection action against a Scheduling Coordinator or CRR Holder on account of a default under the terms of the CAISO Tariff. The CAISO shall make commercially reasonable endeavors to prevent any payment default or recover any default amount. The CAISO shall be entitled to recover from the defaulting Scheduling Coordinator or CRR Holder all costs and expenses associated with its collection efforts, including Interest, attorney's fees, and any related transaction costs as provided in Section 11.29.13.1. In the event of a default by a Participating TO, Black Start Generator, or other Business Associate, the provisions of this CAISO Tariff that apply to defaults by a Scheduling Coordinator or CRR Holder shall apply equally.

### 11.29.21 [Not Used]

\* \* \*

\* \* \*

### 22.13 Scheduling Responsibilities And Obligations

Nothing in this CAISO Tariff is intended to permit or require the violation of federal or California law concerning hydro-generation and Dispatch, including but not limited to fish release requirements, minimum and maximum dam reservoir levels for flood control purposes, and in-stream flow levels. In carrying out its functions, the CAISO will comply with and will have the necessary authority to give instructions to Participating TOs and Market Participants to enable it to comply with requirements of environmental legislation and environmental agencies having authority over the CAISO in relation to Environmental Dispatch and will expect that submitted Bids, including Self-Schedules will support compliance with the requirements of environmental legislation and environmental agencies having authority over Generators in relation to Environmental Dispatch.

\* \* \*

## Appendix A

### Master Definition Supplement

\* \* \*

#### - CAISO Account

The CAISO Clearing Account, the CAISO Reserve Account or such other accounts as the CAISO deems necessary or convenient for the purpose of efficiently implementing the funds transfer system under the CAISO Tariff.

\* \* \*

#### - CAISO Clearing Account

The account in the name of the CAISO with the CAISO Bank and owned by the CAISO to which payments are transferred.

\* \* \*

#### - CAISO Reserve Account

The account established for the purpose of holding cash which may be used in or towards clearing the CAISO Clearing Account.

\* \* \*

**Attachment B – Marked Tariff Language**  
**Order 741 Compliance Filing – Central Counterparty**  
**California Independent System Operator Corporation**  
**Fifth Replacement FERC Electric Tariff**  
**May 25, 2012**

\* \* \*

#### **4.5.3.14 Tax Compliance**

Providing, as described in the Business Practice Manuals, resale certificates or other proof acceptable to CAISO that its purchases of energy are exempt from any sales and use taxes that otherwise might apply.

\* \* \*

**4.5.3.2.2** Submitting Interchange Schedules prepared in accordance with all NERC, WECC and CAISO requirements, including providing E-Tags for all applicable transactions pursuant to WECC practices;

For purposes of E-Tags, the CAISO is not, and shall not be listed as, the “Purchasing Selling Entity”; title to Energy shall pass directly from the entity that holds title when the Energy enters the CAISO Controlled Grid to the entity that removes the Energy from the CAISO Controlled Grid, in each case in accordance with the terms of this CAISO Tariff.

\* \* \*

#### **11.29 CAISO as Counterparty; Billing and Payment-Process;**

- (a) The CAISO shall be the contracting counterparty, in its own name and right, to each Scheduling Coordinator, CRR Holder, Black Start Generator, or Participating TO for any purchase or sale of any product or service, or for any other transaction, that is financially settled by the CAISO under the CAISO Tariff, except under the following circumstances:
- (i) The CAISO shall not be the contracting counterparty for transactions that procure Station Power for a Generating Unit located in Mexico or for transactions that procure Energy or Ancillary Services within Mexico; for such transactions, the CAISO will not act as principal but instead as agent for and on behalf of the relevant Scheduling Coordinators.
- (ii) The provisions of this Section 11.29 will not apply to the billing and payment of transactions associated with Trading Days that occurred prior to September 1,

2012. Billing and payment of such transactions shall be governed by the terms of the tariff effective on the Trading Days.

(b) The purchase of sale of any products or service, or any other transaction, that is financially settled by CAISO under this CAISO Tariff shall be deemed to occur within the State of California. To the extent permitted by applicable law, any warranties provided by the sellers to the CAISO of such products or services, whether express, implied or statutory, are hereby passed to the Business Associates who purchase such products or services from the CAISO on a “pass through basis” and to the extent not passed through, any such warranties are hereby assigned by the CAISO to the purchasing Business Associates. Sellers to the CAISO and Business Associates acknowledge that warranties on such products are limited to that offered by the seller to CAISO and will exist, if at all, solely between the seller to the CAISO and the purchasing Business Associate. AS BETWEEN THE PURCHASING BUSINESS ASSOCIATE AND THE CAISO AS COUNTERPARTY, NO EXPRESS OR IMPLIED WARRANTIES ARE MADE BY THE CAISO REGARDING THE PRODUCTS AND SERVICES SOLD BY THE CAISO AS COUNTERPARTY, AND ANY SUCH PRODUCTS AND SERVICES ARE PROVIDED ON AN “AS IS” AND “AS AVAILABLE” BASIS. THE CAISO MAKES NO WARRANTY OR REPRESENTATION THAT THE PRODUCTS OR SERVICES WILL BE UNINTERRUPTED OR ERROR FREE. PURCHASING BUSINESS ASSOCIATES HEREBY WAIVE, AND THE CAISO HEREBY DISCLAIMS, ALL OTHER WARRANTIES, EXPRESSED OR IMPLIED, INCLUDING, WITHOUT LIMITATION, ANY WARRANTY OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, TITLE AND NON-INFRINGEMENT. THE CAISO DOES NOT WARRANT THAT THE PRODUCTS AND SERVICES OFFERED WILL MEET CUSTOMER’S REQUIREMENTS. NO ORAL OR WRITTEN INFORMATION OR ADVICE GIVEN BY THE CAISO OR ANY AUTHORIZED REPRESENTATIVE OF THE CAISO SHALL CREATE A WARRANTY OR IN ANY WAY INCREASE THE SCOPE OF ANY PASS THROUGH OR ASSIGNED WARRANTY. SOME JURISDICTIONS DO NOT ALLOW THE EXCLUSION OF IMPLIED

WARRANTIES IN CERTAIN CIRCUMSTANCES, SO THE ABOVE EXCLUSION  
APPLIES ONLY TO THE EXTENT PERMITTED BY APPLICABLE LAW.

(c) The CAISO will calculate for each charge the amounts payable by the relevant Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO for each Settlement Period of the Trading Day, and the amounts payable to that Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO for each charge for each Settlement Period of that Trading Day and shall arrive at a net amount payable for each charge by or to that Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO for each charge for that Trading Day. Each of these net amounts will appear in the Settlement Statements that the CAISO will provide to the relevant Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO.

(d) The components of the Grid Management Charge will be included in an Initial Settlement Statement T+3B, and any Recalculation Settlement Statement with the other types of charges referred to in Section 11.

\* \* \*

### 11.29.3

#### **Prepayments**

- (a) A Scheduling Coordinator or CRR Holder may choose to pay at an earlier date than the Payment Date specified in the CAISO Payments Calendar by way of prepayment provided it notifies the CAISO by electronic means before submitting its prepayment.
- (b) Prepayment notifications must specify the dollar amount prepaid.
- (c) Prepayments must be made by Scheduling Coordinators or CRR Holder via Fed-Wire into their CAISO prepayment account designated by the CAISO. The relevant Scheduling Coordinator or CRR Holder shall grant the CAISO a security interest on all funds in its CAISO prepayment account.

- (d) On any Payment Date the CAISO shall be entitled to cause funds from the relevant Scheduling Coordinator's or CRR Holder's CAISO prepayment account to be transferred to the CAISO Clearing Account in such amounts as may be necessary to discharge in full that Scheduling Coordinator's or CRR Holder's payment obligation arising in relation to that Payment Date by way of set-off or recoupment.
- (e) Any funds held in the relevant Scheduling Coordinator's or CRR Holder's CAISO prepayment account shall be treated as part of that Scheduling Coordinator's or CRR Holder's Financial Security.
- (f) Interest (or other income) accruing on the relevant Scheduling Coordinator's or CRR Holder's CAISO prepayment account shall inure to the benefit of that Scheduling Coordinator or CRR Holder and shall be added to the balance of its CAISO prepayment account on a monthly basis.
- (g) Funds held in a CAISO prepayment account by a Scheduling Coordinator or CRR Holder may be recouped, offset or applied by the CAISO to any outstanding financial obligations of that Scheduling Coordinator or CRR Holder to the CAISO ~~or to other Scheduling Coordinators or CRR Holders under this CAISO~~ [Tariff](#).

\* \* \*

#### **11.29.7.2 Basis for Billing and Payment**

The Initial Settlement Statement T+3B and any Recalculation Settlement Statement shall constitute the basis for billing in accordance with this CAISO Tariff. The Initial Settlement Statement T+3B shall constitute the basis for billing for all charges in the first instance. The Recalculation Settlement Statements T+12B and T+55B shall constitute the basis for billing for adjustments to charges set forth in the Initial Settlement Statement T+3B. Each Scheduling Coordinator, CRR Holder, Black Start Generator, and Participating TO shall pay any net debit and, [subject to the limitations in Section](#)

[11.29.17.1](#), shall be entitled to receive any net credit shown in ~~its~~ Invoice or Payment Advice on the Payment Date, whether or not there is any dispute regarding the amount of the debit or credit.

\* \* \*

#### **11.29.8.7 Payment Pending Dispute**

Each Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO which receives an Invoice or Payment Advice shall pay any net debit and, [subject to the limitations in Section 11.29.17.1](#), shall be entitled to receive any net credit shown in the Invoice or Payment Advice on the Payment Date, whether or not there is any dispute regarding the amount of the debit or credit. The provisions of Section 13 shall apply to the disputed amount.

#### **11.29.9 Payment Procedures**

##### **11.29.9.1 ~~All Payments By and to Be Made Through~~ the CAISO**

All Scheduling Coordinators, CRR Holders, Black Start Generators, and Participating TOs shall discharge their obligations to pay the amounts owed by them and shall receive payments of all amounts owed to them [solely in accordance with](#)~~under~~ this CAISO Tariff ~~only through the CAISO~~.

##### **11.29.9.2 ~~CAISO Accounts to be Established~~**

The CAISO is authorized to establish and maintain bank accounts ~~held in trust for Market Participants~~ and obtain lines of credit and other banking facilities (not exceeding an aggregate amount set by the CAISO Governing Board) necessary for the operation of its Settlement and billing procedures. [Each such account shall be maintained at a bank or other financial institution in California.](#) Unless otherwise specified in this CAISO Tariff the CAISO will recover all costs incurred in connection with these CAISO banking facilities through the appropriate component of the Grid Management Charge. The CAISO shall establish and operate the following accounts:

**11.29.9.2.1** A CAISO Clearing Account to and from which all payments [under this Section 11.29](#) are made;

\* \* \*

##### **11.29.9.4 ~~[Not Used]Declaration of Trust~~**

~~All CAISO Accounts established pursuant to Section 11.29.9.2 shall be opened and operated by the CAISO on trust for Market Participants, in accordance with this CAISO Tariff. Each such account shall be maintained at a bank or other financial institution in California and shall bear a name indicating that it is a trust account.~~

#### **11.29.9.5 No Co-Mingling**

To facilitate and better ensure accurate processing of payment defaults pursuant to Section 11.29.17.1,  
~~the~~The CAISO shall not co-mingle any funds standing to the credit of a CAISO Account with its other funds and shall promptly withdraw any amounts paid into a CAISO Account representing amounts paid for the account of the CAISO.

\* \* \*

#### **11.29.9.6.2 Reserve Account**

The CAISO Reserve Account shall be available to the CAISO for the purpose of providing funds to clear the CAISO Clearing Account in the event that there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors. If there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors and clear the account on any Payment Date, due to payment default by one or more CAISO Debtors, the CAISO shall transfer funds from the CAISO Reserve Account to the CAISO Clearing Account to clear it by close of banking business on that Payment Date pursuant to Section 11.29.13.4. If the CAISO Reserve Account is drawn upon, the CAISO shall as soon as possible thereafter take any necessary steps against the defaulting Scheduling Coordinator or CRR Holder, including making any calculations or taking any other appropriate action, to replenish the CAISO Reserve Account including drawing on any credit support or other Financial Security provided by the defaulting Scheduling Coordinator or CRR Holder pursuant to Section 12 or serving demands on any defaulting Scheduling Coordinator or CRR Holder if Financial Security has been exhausted or if no Financial Security is available due to establishment of an Unsecured Credit Limit.

~~The proceeds of drawings under any line of credit, other credit facility, or other Financial Security of the CAISO Reserve Account shall be held on trust for CAISO Creditors. If the CAISO Reserve Account is~~

~~replenished as provided for in this Section 11.29.9.6.2, any credits shall be held on trust for all CAISO Creditors.~~

#### **11.29.9.6.2.1 \_\_Replenishing the CAISO Reserve Account Following Payment Default**

If the CAISO has debited the CAISO Reserve Account then:

- (a) If, after the CAISO has debited the CAISO Reserve Account on a Payment Date, the CAISO Bank receives a remittance from a CAISO Debtor which has not been (but should have been, if it had been received on a timely basis) credited to the CAISO Clearing Account by 10:00 am on the Payment Date and which required the debiting of the CAISO Reserve Account, such remittance shall be credited to the CAISO Reserve Account.
- (b) The proceeds of any enforcement of Financial Security and/or amounts recovered under proceedings shall be credited to the CAISO Reserve Account.
- (c) If, after taking reasonable action, the CAISO determines that the default amount (or any part) and/or Interest cannot be recovered on the next practicable Invoices, the CAISO shall notify Market Participants of the identity of the defaulting Business Associate together with the unrecoverable amounts and such amounts shall be allocated in accordance with Section 11.29.17 of the CAISO Tariff with corresponding credits to the CAISO Reserve Account.

\* \* \*

#### **11.29.9.6.4 CAISO Penalty Reserve Account**

- (a) The CAISO Penalty Reserve Account will be available to the CAISO for the purpose of using funds collected for late payments of amounts set forth in Invoices pursuant to Section 11.29.14(c) and for late postings of Financial Security pursuant to Section 12.5.2(c) to clear the CAISO Clearing Account in the event that there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors. If there are insufficient funds in the CAISO Clearing Account to pay CAISO Creditors and to clear the account on any Payment Date occurring on or after April 7, 2010, due to payment

default by one or more CAISO Debtors, the CAISO shall transfer funds from the CAISO Penalty Reserve Account to the CAISO Clearing Account to clear it by close of banking business on that Payment Date pursuant to Section 11.29.13.4. If available funds in the CAISO Penalty Reserve Account are insufficient to clear the CAISO Clearing Account and the payment default is not cured, the payment default will be allocated in accordance with the CAISO Tariff. After the payment default is allocated in accordance with the CAISO Tariff, any funds that are subsequently added to the CAISO Penalty Reserve Account can only be used to clear the CAISO Clearing Account pursuant to this Section 11.29.9.6.4 for payment defaults that occur after the funds were added to the CAISO Penalty Reserve Account. The CAISO Penalty Reserve Account will be an interest-bearing account separate from all other accounts maintained by the CAISO, and no other funds will be commingled in it at any time.

- (b) On December 31 of each year, the CAISO will draw any funds then available in the CAISO Penalty Reserve Account in excess of five (5) million dollars and will apply that excess to offset the following year's Grid Management Charge revenue requirement pursuant to Schedule 1 of Appendix F.
- (c) If the CAISO Penalty Reserve Account is drawn upon, the CAISO will as soon as possible thereafter take any necessary steps against the defaulting Scheduling Coordinator or CRR Holder, including making any calculations or taking any other appropriate action, to replenish the CAISO Penalty Reserve Account, including drawing on any credit support or other Financial Security provided by the defaulting Scheduling Coordinator or CRR Holder pursuant to Section 12 or serving demands on any defaulting Scheduling Coordinator if Financial Security has been exhausted or if no Financial Security is available due to establishment of an Unsecured Credit Limit.

~~(d) The proceeds of drawings under any line of credit, other credit facility, or other Financial Security of the CAISO Penalty Reserve Account will be held on trust for CAISO Creditors to which amounts are owed on any Payment Date occurring on or after April 7, 2010. If the CAISO Penalty Reserve Account is replenished as provided for in this Section 11.29.9.6.4, any credits shall be held on trust for CAISO Creditors to which amounts are owed on any Payment Date occurring on or after April 7, 2010.~~

\* \* \*

#### **11.29.9.6.4.1 Replenishment Following Payment Default**

If the CAISO has debited the CAISO Penalty Reserve Account, then:

- (a) If, after the CAISO has debited the CAISO Penalty Reserve Account on a Payment Date, the CAISO Bank receives a remittance from a CAISO Debtor which has not been (but should have been, if it had been received on a timely basis) credited to the CAISO Clearing Account by 10:00 am on the Payment Date and which required the debiting of the CAISO Penalty Reserve Account, such remittance shall be credited to the CAISO Penalty Reserve Account, less any amounts due to Market Participants.
- (b) The proceeds of any enforcement of Financial Security and/or amounts recovered under proceedings shall be credited to the CAISO Penalty Reserve Account.
- (c) If, after taking reasonable action, the CAISO determines that the default amount (or any part) and/or Interest cannot be recovered, the CAISO shall notify Market Participants of the identity of the defaulting Business Associate together with the unrecoverable amounts and such amounts shall be allocated in accordance with Section 11.29.17 of the CAISO Tariff with corresponding credits to the CAISO Penalty Reserve Account.

### 11.29.10 Billing And Payment

The CAISO shall prepare and send to each Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO an Invoice or Payment Advice on Wednesday of each week. If Wednesday falls on a CAISO holiday, the CAISO will issue the Invoice or Payment Advice on the next Business Day. Each Invoice or Payment Advice ~~shall will~~ show ~~the amount that is payable~~~~amounts which are to be paid~~ by or to each Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO, which amount shall equal the positive or negative total of all net charges reflected on the relevant Settlement Statements, the Payment Date, being the date on which such ~~amount is~~~~amounts are~~ to be paid or received, and details of the CAISO Clearing Account to which any amounts owed by or to Scheduling Coordinators, CRR Holder, Black Start Generator or Participating TO ~~are is~~ to be paid. Revenues owed from a Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO are expressed as a positive amount on an Invoice. Revenues owed to a Scheduling Coordinator, CRR Holder, Black Start Generator or Participating TO are expressed as a negative amount on a Payment Advice. Payments or charges for the items referred to in an Invoice or Payment Advice (except for the charges payable under long-term contracts) for each Trading Day shall be made four (4) Business Days after the date on which the weekly Invoice or Payment Advice is issued. If the fourth (4) Business Day after an Invoice or Payment Advice is issued falls on a CAISO holiday, then the Payment Date for the Invoice or Payment Advice shall be the next Business Day.

\* \* \*

### 11.29.11 Instructions For Payment

Unless the CAISO instructs otherwise, each Scheduling Coordinator or CRR Holder shall remit to the CAISO Clearing Account the amount shown on the Invoice as payable by that Scheduling Coordinator or CRR Holder for value not later than 10:00 a.m. on the Payment Date. In the event of a verifiable error that would be reversed on a future Invoice or Payment Advice, the CAISO may instruct a Scheduling Coordinator or CRR Holder ~~not to~~ ~~reduce its~~~~remit~~ payment in the amount of a specific charge ~~reflected~~~~shown~~ on an Invoice. Any such occurrence will not constitute a payment default under the CAISO Tariff. If the CAISO directs such a reduction in payment, it shall make offsetting adjustments on future Invoices or Payment Advices of Scheduling Coordinators, CRR Holders, Black Start Generators or

Participating TOs that received settlement credits corresponding to the verifiably erroneous charge. The CAISO will inform those entities of the adjustments to their Invoices or Payment Advices. payment amount would otherwise be payable to identified Market Participants, the CAISO will inform those entities that they will not be receiving payment for any specific corresponding Charge Code on a Payment Advice.

#### **11.29.12 CAISO'S Responsibilities**

On the due date for payment of amounts shown in an Invoice, the CAISO shall ascertain whether all amounts required to be remitted to the CAISO Clearing Account have been credited to it. If any such amount has not been so credited, it shall ascertain which Scheduling Coordinators or CRR ~~Holder~~Holder have failed to pay the amount owed by them and it may, subject to any notice or cure provisions in this Section 11.29, exercise any rights available under the CAISO Tariff or under applicable law ~~take steps~~ to recover any overdue amount.

\* \* \*

#### **11.29.13.7 Set-Off and Recoupment**

-The CAISO is authorized to recoup, set off and apply any amount owed on any Payment Advice to which any defaulting CAISO Debtor is or will be entitled, in or towards the satisfaction of any of that CAISO Debtor's debts on any Invoice arising under the CAISO Settlement and billing process. Each CAISO Creditor and each CAISO Debtor expressly acknowledges the following application of funds: first to the current month's Grid Management Charge, and then as described in 11.29.13.8 except as limited by Section 11.29.17. Nothing in this Section 11.29.13.7 shall be construed as affecting the methodology by which the CAISO determines the amounts of Invoices or Payment Advices ~~unless otherwise specified in accordance with Section 11.29.17.~~

\* \* \*

#### **11.29.16 Prohibition On Transfers**

-The CAISO shall at no time instruct the CAISO Bank to transfer any sum from a CAISO Account to another account except as permitted ~~(not being a CAISO Account) unless that account is a Settlement Account or the amount is owed to the CAISO~~ under this CAISO Tariff.

## 11.29.17        Alternative Payment Procedures

### 11.29.17.1        Pro Rata Reduction to Payments

The obligation of the CAISO to pay Scheduling Coordinators, CRR Holders, Black Start Generators, Participating TOs, and any other Business Associates monies owed for a given settlement period shall be limited so that the aggregate liability of the CAISO for such payments does not exceed the sum of a) the amounts paid to the CAISO Clearing Account for that settlement period, b) additional amounts recovered by the CAISO by enforcing any Financial Security provided by a defaulting Scheduling Coordinator of CRR Holder to cover any shortfall for that settlement period, and c) amounts transferred to the CAISO Clearing Account from the CAISO Reserve Account and the CAISO Penalty Reserve Account to cover any shortfall for that settlement period. If it is not possible to clear the CAISO Clearing Account on a Payment Date because of an insufficiency of funds available in the CAISO Reserve Account or the CAISO Penalty Reserve Account, or by enforcing any Financial Security provided by a defaulting Scheduling Coordinator or CRR Holder, the CAISO shall, after deducting Grid Management Charge and FERC Annual Charges in accordance with Section 11.29.9.6.1, (1) first pay in full every CAISO Creditor whose net amounts receivable on the relevant Payment Date is less than \$5,000; and (2) second, reduce payments to all remaining CAISO Creditors proportionately to the net amounts payable to them on the relevant Payment Date to the extent necessary to clear the CAISO Clearing Account through a shortfall allocation. ~~The CAISO shall account for such reduction in the CAISO ledger accounts as amounts due and owing by the non-paying CAISO Debtor to each CAISO Creditor whose payment was so reduced.~~

Each payment default amount allocated to CAISO Creditors through a shortfall allocation under this Section 11.29.17.1 that remains unpaid by the defaulting Scheduling Coordinator or CRR Holder will be allocated as set forth in Section 11.29.17.2. The provisions of this Section 11.29.17.1 shall not apply to non-payment of any penalty amount that a Scheduling Coordinator or CRR Holder has disputed and FERC has specifically authorized the Scheduling Coordinator or CRR Holder to net its payment to the CAISO by the amount of the penalty in question in accordance with Section 37.9.3, ~~in which case the non-payment amount will be allocated exclusively to the CAISO penalty trust account and not allocated to CAISO Creditors.~~

\* \* \*

### 11.29.19.3 Overpayment Held In Trust

Until a CAISO Creditor refunds the overpayment to the CAISO, the CAISO Creditor shall be deemed to hold the amount of such overpayment on trust for ~~CAISO~~any CAISO Creditor which may have been underpaid in consequence of such overpayment, pro rata to the amount of the underpayment.

\* \* \*

### 11.29.20 Defaults

In addition to and not in lieu of any other events specified in this CAISO Tariff as constituting a default, the occurrence of any of the following events shall constitute a default under this CAISO Tariff:

~~Each CAISO Creditor shall give notice to the CAISO before instituting any action or proceedings in any court against a CAISO Debtor to enforce payments due to it.~~

- (a) If a Scheduling Coordinator or CRR Holder files a petition or otherwise commences, authorizes, or acquiesces in the commencement of a case, petition, proceeding, or cause of action under any bankruptcy or insolvency law or similar law for the protection of debtors or creditors; or
- (b) If a Scheduling Coordinator or CRR Holder has a petition, case, proceeding or cause of action filed or commenced against it and such case, petition, proceeding or cause of action is not withdrawn or dismissed within (30) days after such filing or commencement;

In the event of any default under the CAISO Tariff, the CAISO shall, in addition to any other remedies available at law in equity or under the CAISO Tariff, have the sole and exclusive right to take debt collection action against a Scheduling Coordinator or CRR Holder on account of a default under the terms of the CAISO Tariff. The CAISO shall make commercially reasonable endeavors to prevent any payment default or recover any default amount. The CAISO shall be entitled to recover from the defaulting Scheduling Coordinator or CRR Holder all costs and expenses associated with its collection efforts, including Interest, attorney's fees, and any related transaction costs as provided in Section 11.29.13.1. In the event of a default by a Participating TO, Black Start Generator, or other Business Associate, the provisions of this CAISO Tariff that apply to defaults by a Scheduling Coordinator or CRR Holder shall apply equally.

### ~~11.29.21 [Not Used] Proceedings to Recover Overdue Amounts~~

#### ~~11.29.21.1 Proceedings Brought by the CAISO~~

~~Without prejudice to the right of any Scheduling Coordinator, CRR Holder, Black Start Generator, or Participating TO to bring such proceedings as it sees fit in connection with matters related to the recovery of amounts owed to it, the CAISO may bring proceedings against any Scheduling Coordinator or CRR Holder on behalf of those Scheduling Coordinators, CRR Holders, Black Start Generators, or Participating TOs who have indicated to the CAISO their willingness for the CAISO first so to act, for the recovery of any amounts due by that Scheduling Coordinator or CRR Holder, if the CAISO has first reached agreement with the Scheduling Coordinators, CRR Holders, Black Start Generators, or Participating TOs as to the appropriate remuneration, is indemnified to its reasonable satisfaction, and receives such Financial Security as it may reasonably request against all costs, claims, expenses (including legal fees) and liabilities which it will or may sustain or incur in complying with such instructions.~~

#### ~~11.29.21.2 Evidence of Unpaid Amount~~

~~The CAISO shall, on request, certify in writing the amounts owed by a CAISO Debtor that remain unpaid and the CAISO Creditors to whom such amounts are owed and shall provide certified copies of the relevant Initial Settlement Statement T+3B and the Recalculation Settlement Statements, Invoices, Payment Advices, and other documentation on which the CAISO's certificate was based to the CAISO Debtor and the relevant CAISO Creditors. A CAISO certificate given under this Section 11.29.21.2 may be used as prima facie evidence of the amount due by a CAISO Debtor to CAISO Creditors in any legal proceedings.~~

\* \* \*

### **22.13 Scheduling Responsibilities And Obligations**

Nothing in this CAISO Tariff is intended to permit or require the violation of federal or California law concerning hydro-generation and Dispatch, including but not limited to fish release requirements, minimum and maximum dam reservoir levels for flood control purposes, and in-stream flow levels. In carrying out its functions, the CAISO will comply with and will have the necessary authority to give instructions to Participating TOs and Market Participants to enable it to comply with requirements of environmental legislation and environmental agencies having authority over the CAISO in relation to

Environmental Dispatch and will expect that submitted Bids, including Self-Schedules will support compliance with the requirements of environmental legislation and environmental agencies having authority over Generators in relation to Environmental Dispatch. ~~In contracting for Ancillary Services and Imbalance Energy the CAISO will not act as principal but as agent for and on behalf of the relevant Scheduling Coordinators.~~

\* \* \*

## Appendix A

### Master Definition Supplement

\* \* \*

#### - CAISO Account

The CAISO Clearing Account, the CAISO Reserve Account or such other ~~trust~~ accounts as the CAISO deems necessary or convenient for the purpose of efficiently implementing the funds transfer system under the CAISO Tariff.

\* \* \*

#### - CAISO Clearing Account

The account in the name of the CAISO with the CAISO Bank ~~and owned by the CAISO~~ to which payments are ~~required to be~~ transferred ~~for allocation to CAISO Creditors in accordance with their respective entitlements.~~

\* \* \*

#### - CAISO Reserve Account

The account established for the purpose of holding cash ~~deposits~~ which may be used in or towards clearing the CAISO Clearing Account.

\* \* \*

**Attachment C – Discussion Paper**

**Order 741 Compliance Filing – Central Counterparty**

**California Independent System Operator Corporation**

**Fifth Replacement FERC Electric Tariff**

**May 25, 2012**



**Discussion Paper:**  
**Order 741 Compliance – Central Counterparty**  
**Tariff Revisions**

**May 7, 2012**

## 1. BACKGROUND

This paper accompanies the release of tariff language for compliance with FERC Order 741. Order 741 imposed several requirements on ISOs and RTOs for the purpose of enhancing credit practices. The ISO has already complied with all of the requirements except one – the rule that ISOs and RTOs must adopt tariff provisions to enhance the legal basis for netting settlement payments. The ISO plans to comply with this requirement by adopting the proposed tariff language, which makes the ISO a central counterparty to market transactions.

The ISO's stakeholder process on this issue has been on hold since the initial stakeholder meeting about Order 741, which was held in Folsom on February 2, 2011. During that initial meeting the ISO presented the three alternatives FERC set forth in Order 741:

1. Become the central counterparty to all market transactions,
2. Require market participants either grant the ISO a security interest in their market receivables or else post collateral on their "gross" obligation, or
3. An alternative that would offer the same degree of protection against the perceived risk. The Commission stated explicitly that it would not be sufficient to be more specific in the tariff about the ISO's ability to net market payments.

Based on the discussion at the February 2, 2011 stakeholder meeting and the subsequent written comments, stakeholders' clear preference was for the first approach – becoming a central counterparty. There was significant stakeholder concern about the second approach – taking a security interest in market participants' receivables from the ISO or, as a fallback, requiring that market participants post collateral based on their gross obligations.<sup>1</sup> Neither the ISO nor any market participant was able to identify an

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<sup>1</sup> With respect to the possibility of taking a security interest in market participants' receivables, stakeholders were concerned that such a requirement would be in tension with existing or potential lending agreements or bond covenants. The general consensus appeared to be that the viability of this approach depended on a better understanding of the fallback rule, which was that market participants that could not grant a security interest must post security on their "gross obligation." Shortly after that meeting, FERC issued its February 17 order on rehearing or clarification from Order 741, which took an unexpectedly strict view of this requirement. NYISO had asked FERC to clarify that its longstanding practice of netting financial obligation within categories of products and services, which had not been addressed in the Order 741 proceedings, was consistent with requiring financial security based on the market participant's "gross obligation." FERC denied that request. In light of that ruling, the "gross obligation" that market participants must secure would include the entire day-ahead energy obligation of load-serving utilities, without netting self-supplied generation. The group expressed concern that market participants could not secure this obligation as the increased collateral requirements would be substantial.

alternative that might satisfy FERC's requirements for the third approach. Accordingly, given the lack of viable alternatives and affirmative interest in the central counterparty approach from many stakeholders, ISO staff has been pursuing the central counterparty approach.

Since then, as the ISO explained in motions filed with FERC to extend the deadline for compliance,<sup>2</sup> the ISO has been worked with the Internal Revenue Service and the Franchise Tax Board to confirm that the change will not jeopardize the ISO's tax-exempt status. In addition, the ISO has conferred with its external auditor, insurance broker and other advisors to better understand the implications of becoming a central counterparty.

On April 25, 2012, the ISO asked FERC for a further extension of the compliance deadline in order to proceed with a full stakeholder process on this issue, together with a second initiative concerning inter-SC trades. Both initiatives are central to the ISO's pending request with the CFTC, to exempt the ISO's market from regulation under the Commodity Exchange Act. FERC extended the ISO's compliance deadline in an order issued April 30, but allowed less time than the ISO requested. To comply with that order and the new compliance deadline, the ISO revised the plan that it had proposed to FERC in two ways. First, it will separate the stakeholder process for inter-SC trades and eliminate the policy step that it had proposed, which was intended mainly to address that issue. Second, the deadlines for commenting on this proposed tariff language are shorter than normal, and thus do not include a second round of written comments.

## **2. STAKEHOLDER PROCESS**

The ISO is publishing draft tariff language on May 7

Written comments are due on the tariff language by May 14.

The ISO will hold a stakeholder call to discuss the comments on May 18.

The ISO will publish revised tariff language on May 21.

A call to discuss the revised tariff language will be held on May 23.

The ISO will file the tariff amendment on May 25.

## **3. CHANGE TO CENTRAL COUNTERPARTY STATUS**

To reorient stakeholders to this issue and facilitate review of the tariff language on the abbreviated schedule, this section explains the change to central counterparty status.

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<sup>2</sup> See, e.g., *Joint Motion of ISO New England Inc., California Independent System Operator Corporation and New York Independent System Operator Requesting Extension of Time to Submit Compliance Filing*, Docket No. RM10-13-000 (August 15, 2011).

Order 741 describes the requirement only in general terms. The most extended description is that ISOs and RTOs should “clarify the ISO’s/RTO’s legal status to take title to transactions, thereby becoming the central counterparty for transactions in an effort to establish mutuality in the transactions as legal support for set-off in bankruptcy.”<sup>3</sup> As explained below, the changes required are primarily legal rather than practical. While central counterparty status will change the legal underpinnings of certain market transactions, very little will change in terms of what market participants do.

### **A. Practical Consequences of Change to Central Counterparty**

The primary change for scheduling coordinators in terms of practical consequences will be how the ISO and market participants respond to payment default by a market participant. Currently, market participant creditors are responsible for pursuing collection from the defaulting market participant debtor, including filing claims in any bankruptcy proceeding. The ISO’s involvement is limited to setting off collateral and payments that would otherwise be due to a bankrupt entity, and collecting on debts to the ISO itself as opposed to the market, such as GMC or ISO-administered trust funds.

As a central counterparty, the ISO would assume the role of collecting the default amount on behalf of other market participants, and then distribute any funds it collects. This would include filing any claims in the bankruptcy proceeding of the defaulting market participant. The change to central counterparty status will not require software changes. It will require minor changes to Business Practice Manuals such as the configuration guides for Shortfall Adjustment (CC5910) and Financial Adjustments (CC5900, 5901, 5912).

Otherwise, the change should not affect the business of market participants. Rules about bidding, scheduling and market operations will not change. Nor will the ISO’s corporate structure change, as the ISO does not plan to establish a separate corporate entity to serve as counterparty.

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<sup>3</sup> FERC Order No. 741, 133 FERC ¶ 61,060 (2010), P 82. See also P 94 (“Mutuality was identified by several participants as important in allowing the ISOs and RTOs to perform this vital function, who asserted that mutuality was most easily achieved by the market administrator ‘taking title’ or being the buyer to all sellers and seller to all buyers in all transactions in the market”) & P 116 (“Organized wholesale electric markets typically arrange for settlement and netting of transactions entered into between market participants and the market administrator, but do not take title to the underlying contract position of a participant at the time of settlement. The Commission is concerned that, if a market participant files for bankruptcy protection, it may argue against setting-off amounts owed against amounts to be paid to an ISO or RTO, which could lead to a larger default in the market that must be socialized among all other participants”).

The ISO's process for billing and payment will not change, and the ISO will continue, in the event of a payment default by a market participant, to setoff or recoup collateral and other amounts that would be due to the defaulting market participant in order to cover the default. Central counterparty status is intended to solidify the legal bases for a setoff in these circumstances.

The ISO will continue to remain financially neutral after market participant defaults. If a debtor defaults on a market obligation and the ISO is not holding sufficient collateral to cover the default amount, the shortfall will be allocated to other market participants consistent with the current default loss allocation formula. The ISO will have no liability to the market participants who bear part of the loss, only a responsibility to pursue collection.

Finally, as explained in more detail below, the ISO believes that a central counterparty structure will not result in other material changes to the ISO's business or additional costs that would have to be passed along to market participants.

## **B. Explanation of Tariff Changes**

Conversion to central counterparty status involves three core changes, and related changes to conform language in other sections to the core provisions. In addition, scheduling coordinators will have to provide the ISO with resale certificates valid in California, Nevada and Arizona, or other proof acceptable to the ISO that its purchases of energy are exempt from sales and use taxes that would otherwise apply.

First, rather than acting as an agent for scheduling coordinators, as stated currently in Section 22.13, the ISO will be a counterparty to market transactions. The critical sentence in Section 22.13 will be deleted and replaced with the following in Section 11.29:

[T]he CAISO shall be for all purposes the contracting counterparty, in its own name and right, to each Scheduling Coordinator, CRR Holder, Black Start Generator, or Participating TO for any purchase or sale of any product or service, or for any other transaction, that is financially settled by the CAISO under the CAISO Tariff.

Section 11.29 includes an exception to this rule for energy procured for use in Mexico. For these transactions, the current rule that the ISO is an agent for the respective scheduling coordinators will remain in effect. This provision is intended to maintain the status quo regarding obligations for compliance with applicable Mexican law. A similar provision is included in the tariff changes filed by ISO New England for its conversion to counterparty status, in order to address restrictions on the ability of certain tax exempt members to sell energy to a central counterparty.

In the same section, the ISO also includes a provision intended to maintain the status quo with respect to any product warranties. This provision is also similar to one filed by ISO New England.

Second, responsibility for pursuing collection on market participant defaults will be reassigned to the ISO. This involves deleting Section 11.29.21, which currently places this responsibility on scheduling coordinators, and the revision of Section 11.29.20 to place this responsibility on the ISO.

To conform to these two rules, smaller revisions are made to a number of other provisions, such as deleting language indicating that payments by scheduling coordinators are due to other scheduling coordinators rather than the ISO, and statements that market payments to the ISO are being held in trust by the ISO for market participants. Such conforming changes can be found in Sections 11.29.3(g), 11.29.9.1, 11.29.9.4, 11.29.9.5, 11.29.9.6.2, 11.29.11, 11.29.12, 11.29.19.3, and the definitions of “CAISO Clearing Account” and “CAISO Reserve Account.”

Third, consistent with the rule that FERC approved for PJM when it became a central counterparty, the ISO’s tariff will continue to provide that, in the event of a default, the ISO will be revenue neutral and the shortfall will be shared among market participants. Although this does not change current ISO practice, the expression of the rule must change as a result of the first two changes described above. This is affected through Section 11.29.17.1, which limits the liability of the ISO in the event of a default that cannot be recovered from financial security posted with the ISO. In addition, a few other tariff provisions are clarified in order to reduce the possibility that they could be misconstrued by a bankruptcy court to the disadvantage of the ISO and the market. See Sections 11.29 (adding the word “net” to clarify the phrase “net amounts”), 11.29.7.2 and 11.29.8.7 (explicitly connecting the limitation of liability to statements about the ISO’s obligation to pay), 11.29.10 (clarifying the obligation to pay invoices), and 11.29.13.7 (clarifying that the setoff and recoupment rights are not intended to alter the provisions about invoicing).

In addition to these core and conforming changes, certain provisions are revised to address discrete issues.

Due to pending reruns as well as lawsuits relating to the energy crisis, it is important to clarify that these changes will be prospective only. Under the current tariff, these amounts are due from the defaulting debtor (the California Power Exchange in the case of the energy crisis) directly to the market creditors, each of whom was required to pursue collection itself. Under the filed-rate doctrine, the change to central counterparty status will not affect these old reruns and outstanding balances because the change is prospective only. However, to avoid any doubt, and to ensure that this amendment

does not interfere with the ultimate clearing of the markets from the crisis era, Section 11.29 states explicitly that certain provisions are effective only for trade dates following the effective date of the amendment. A related change is made in Section 11.29.17.2.8.

#### **4. OTHER IMPLICATIONS OF CENTRAL COUNTERPARTY STATUS**

In addition, the ISO has analyzed other potential implications of becoming a central counterparty, including taxes, accounting costs, state greenhouse gas regulation, and FERC regulation of wholesale energy transactions. For the most part, the ISO has been able to confirm that the change to central counterparty status will not materially affect the ISO.

##### **A. Tax Exempt Status and Other Bond Covenants**

As noted above, the ISO has confirmed with the IRS and the California Franchise Tax Board that becoming a central counterparty will not jeopardize the ISO's tax exempt status under federal or state law.

##### **B. Other Taxes**

The ISO has also worked with outside advisors to identify any taxes that might be assessed on the ISO as a result of central counterparty status, because any taxes would have to be passed through to market participants. Although the ISO is still working to document and implement its solutions to certain tax issues and to minimize related administrative burden, its conclusion from the review is that the ISO will not incur taxes as a result of the change.

The ISO is advised that the best way to document this exemption from certain taxes is to obtain a resale certificate from every scheduling coordinator, or proof that the seller is exempt from sales or use taxes. Accordingly, this is required in the draft tariff provisions, as noted above.

##### **C. Accounting and Auditing**

The ISO had earlier expressed a concern to FERC that serving as a central counterparty could complicate its financial reporting and increase significantly the costs associated with its annual financial audit and with validating transactions. After further review with its outside auditors, the ISO has become comfortable with netting all market transactions entered as a central counterparty on the ISO's balance sheet and for purposes of revenue recognition. Although the ISO will have to make further disclosures, particularly around the valuation of CRRs, the total increase in ISO expenses should be minimal.

## D. State Regulation of Greenhouse Gasses

As the California Air Resources Board was preparing greenhouse gas regulations, some asked whether the ISO might become liable for procuring emissions permits on imported power, particularly imports that enter the ISO grid at points located outside the geographic boundaries of California. If the ISO were to bear that liability, rather than the electricity importer, the purpose of greenhouse gas regulation would be undermined, because the ISO cannot respond to the incentives by selecting a generation source with lower emissions. In addition, the ISO would have to pass on the additional costs to grid users. The ISO raised this concern at FERC. Importers have raised this same issue with the Air Resources Board.

As events have unfolded, however, this issue does not appear to pose a concern with respect to the ISO becoming a central counterparty. Under the final rule of the Air Resources Board, posted on December 14, 2011,<sup>4</sup> liability for the emissions permits associated with electricity imports rests with the party that injected the energy into the ISO grid, and does not depend on other factors that might implicate the central counterparty. Specifically, section 95802 states that “[f]or electricity delivered between balancing authority areas, the electricity importer” – that is, the entity obligated to purchase emissions permits – “is identified on the NERC E-tag as the purchasing-selling entity (PSE) on the last segment of the tag’s physical path with the point of receipt located outside the state of California and the point of delivery located inside the state of California.”<sup>5</sup> The ISO does not accept e-tags that identify the ISO as the purchasing-selling entity, and has installed software to reject any such tags automatically.<sup>6</sup> The ISO’s rule is consistent with NERC and NAESB standards, which

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<sup>4</sup> Final Regulation Order for the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, title 17, California Code of Regulations, section 95800 to 96023.

<sup>5</sup> The complete definition reads:

“Electricity Importers” are marketers and retail providers that deliver imported electricity. For electricity delivered between balancing authority areas, the electricity importer is identified on the NERC E-tag as the purchasing-selling entity (PSE) on the last segment of the tag’s physical path with the point of receipt located outside the state of California and the point of delivery located inside the state of California. For facilities physically located outside the state of California with the first point of interconnection to a California balancing authority’s transmission and distribution system, the importer is the facility operator or scheduling coordinator. Federal and state agencies are subject to the regulatory authority of ARB under this article, and include Western Area Power Administration (WAPA), Bonneville Power Administration (BPA) and California Department of Water Resources (DWR).

<sup>6</sup> The only exception involves emergency imports, where the ISO can be identified on the e-tag as the purchasing-selling entity. While the ISO must address this issue, it is not exacerbated by becoming the central counterparty.

allow parties to reject e-tags for contractual reasons. Given this legal framework, state greenhouse gas law does not appear to pose an obstacle to central counterparty status.

### **E. Federal Regulatory Requirements for Wholesale Electricity Transactions**

As a central counterparty, the ISO will become a buyer and seller of energy at wholesale, and thus may be subject to additional regulatory requirements. PJM faced a similar issue in its conversion to central counterparty status. In that case, FERC agreed to waive two sets of requirements that otherwise might have applied to PJM:

- Regulations regarding market-based rate authorization and wholesale sale of electric energy, capacity, and ancillary services at market-based rates. See 18 C.F.R. §§ 35.36-35.42
- EQR reporting requirements that arise from serving as a central counterparty.

See PJM Interconnection, L.L.C., 132 FERC ¶ 61,207 (2010), at PP 56-61. The ISO plans to ask FERC for the same waiver that it granted PJM.

### **5. QUESTIONS ABOUT THE PROPOSED TARIFF LANGUAGE**

The ISO wants to maximize the effectiveness of this stakeholder process and the likelihood that any questions or concerns can be resolved before the amendment is filed with FERC. To that end, the ISO encourages stakeholders to ask questions before initial written comments are due on May 14, and at any time during the process. Please submit questions to Kevin King, [kking@caiso.com](mailto:kking@caiso.com).