

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

**California Independent System) Docket No. ER09-1681-000
Operator Corporation)**

**ANSWER TO MOTIONS TO INTERVENE AND COMMENTS, MOTION TO FILE
ANSWER, AND ANSWER TO PROTESTS, OF THE CALIFORNIA
INDEPENDENT SYSTEM OPERATOR CORPORATION**

The California Independent System Operator Corporation (“ISO”)¹ hereby files its answer to the motions to intervene and comments submitted in this proceeding in response to the ISO’s submittal on September 4, 2009 of an amendment to the ISO tariff (“September 4 Tariff Amendment”) to reduce the maximum unsecured credit limit for market participants from the current level of \$150 million to \$50 million, in connection with the planned implementation of the ISO’s payment acceleration program.² The ISO also hereby submits a motion to file an answer and its answer to the sole protest submitted in this proceeding, by SCE.³

¹ The ISO is also sometimes referred to as the CAISO.

² The following entities filed motions to intervene and/or comments in this proceeding: the City of Santa Clara, California, d/b/a Silicon Valley Power, and the M-S-R Public Power Agency; Modesto Irrigation District (“MID”); Northern California Power Agency (“NCPA”); NRG Power Marketing LLC, Cabrillo Power I LLC, Cabrillo Power II LLC, El Segundo Power, LLC, Long Beach Generation LLC, Dynegy Morrow Bay, LLC, Dynegy Moss Landing Bay, LLC, Dynegy Oakland, LLC, Dynegy South Bay, LLC, RRI Energy, Inc., J.P. Morgan Ventures Energy Corporation, and BE CA LLC (collectively, “Joint Parties”); Pacific Gas and Electric Company (“PG&E”); Powerex Corp. (“Powerex”); and Southern California Edison Company (“SCE”). In addition, the California Public Utilities Commission submitted a motion of intervention in the proceeding.

³ The ISO submits this answer pursuant to Rules 212 and 213 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 385.213 (2009). The ISO requests waiver of Rule 213(a)(2), 18 C.F.R. § 385.213(a)(2), to permit it to make an answer to SCE’s protest. Good cause for this waiver exists here because the answer will aid the Commission in understanding

The ISO does not object to any of the motions to intervene. Most of the parties that submitted comments indicate their support for the proposed tariff changes.⁴ Only PG&E and SCE raised any objections to the tariff changes. For the reasons explained below, the Commission should accept the September 4 Tariff Amendment as filed and should reject the arguments made by PG&E and SCE.

I. Answer

A. The ISO's Proposed Reduction of the Maximum Unsecured Credit Limit from \$150 Million to \$50 Million Is Just and Reasonable.

PG&E and SCE argue that the ISO has failed to demonstrate that it is necessary to reduce the maximum unsecured credit limit from \$150 million to \$50 million.⁵ Under the legal standard for considering tariff changes filed pursuant to Section 205 of the Federal Power Act, however, the ISO is not required to show that the proposed reduction is "necessary," only that it is just and reasonable.

As the ISO explained in its transmittal letter supporting the September 4 Tariff Amendment, reducing the maximum unsecured credit limit to \$50 million is appropriate. The ISO will not reiterate its transmittal letter discussion except to note that in its order accepting the ISO's proposed reduction of the maximum

the issues in the proceeding, provide additional information to assist the Commission in the decision-making process, and help to ensure a complete and accurate record in this case. See, e.g., *Entergy Services, Inc.*, 116 FERC ¶ 61,286, at P 6 (2006); *Midwest Independent Transmission System Operator, Inc.*, 116 FERC ¶ 61,124, at P 11 (2006); *High Island Offshore System, L.L.C.*, 113 FERC ¶ 61,202, at P 8 (2005).

⁴ Joint Parties at 5-6; MID at 5-6; NCPA at 3; Powerex at 4-5.

⁵ PG&E at 3; SCE at 3.

unsecured credit limit from \$250 million to \$150 million, the Commission acknowledged that the reduction to \$150 million was “a logical step in the CAISO’s plan to eventually reduce the maximum unsecured credit limit to \$50 million upon the implementation of the CAISO’s payment acceleration program.”⁶ Therefore, in the September 4 Tariff Amendment, the ISO simply took the next planned step to reduce the maximum unsecured credit limit to \$50 million.

There is no merit to the assertions of PG&E and SCE that the implementation of a maximum unsecured credit limit of \$50 million will impose unreasonable costs on market participants.⁷ The fact that market participants may incur some costs in complying with ISO credit requirements is a necessary element of a credit policy that is tailored to protect the market against the risks of outstanding liabilities of market participants. In fact, within the past six months, the Commission determined that it was just and reasonable for another independent system operator to reduce its maximum unsecured credit limit from \$150 million to \$50 million. In April 2009, the Commission authorized PJM Interconnection L.L.C. (“PJM”) to implement a \$50 million maximum unsecured credit allowance (the PJM version of the maximum unsecured credit limit), and did so based on a rationale very similar to the ISO’s rationale for the reduction of the maximum unsecured credit limit in this proceeding, namely, to reflect a reduction in the number of days in the payment calendar.⁸

⁶ *California Independent System Operator Corp.*, 126 FERC ¶ 61,285, at P 36 (2009).

⁷ PG&E at 3-4; SCE at 3.

⁸ *PJM Interconnection, L.L.C.*, 127 FERC ¶ 61,017, at P 35 (2009) (“PJM Credit Policy Order”).

B. The Existence of Congestion Revenue Rights Auctions Does Not Justify a Higher Unsecured Credit Limit.

PG&E and SCE argue that the maximum unsecured credit limit should not be reduced to \$50 million but should instead remain at \$150 million, on the grounds that the collateral requirement for participation in the annual congestion revenue right (“CRR”) auction will not change under the reduced cash clearing cycle pursuant to the payment acceleration program, and therefore the overall collateral requirement (*i.e.*, the sum of the collateral requirement for participation in the annual CRR auction plus the collateral requirement for all other purposes) will not necessarily decrease at the same 70 percent rate as the reduced cash clearing cycle under payment acceleration.⁹ In addition, SCE asserts that, if the Commission approves the reduction of the maximum unsecured credit limit to \$50 million, the Commission should also require the ISO to temporarily increase the maximum unsecured credit limit to \$150 million for the month in which the annual CRR auction occurs.¹⁰

The ISO should not be required to maintain the current maximum unsecured credit limit of \$150 million based on pre-CRR auction credit requirements that apply for a relatively short period during the time of the auction. Collateral to cover pre-CRR auction credit requirements must be posted two business days prior to the auction. Any excess collateral is returned after awards are made and the new portfolio value is calculated, approximately four business days after the auction. The balance of this CRR auction-related collateral is

⁹ PG&E at 4-5; SCE at 3.

¹⁰ SCE at 4-5.

returned when the auction settles, approximately 3-4 weeks after the auction concludes. Given the short duration of the pre-CRR auction credit requirements, it would be inappropriate to require the ISO to maintain maximum unsecured credit limits at a level higher than otherwise justified.

Also, SCE's proposal to temporarily increase the maximum unsecured credit limit to \$150 million for the month of the annual CRR auction is flawed because the ISO does not differentiate between collateral posted for a CRR auction and collateral posted for other market activities. Therefore, SCE's proposal would allow market participants to obtain higher levels of unsecured credit during that month for market activities that have nothing to do with the annual CRR auction, thus increasing the mutualized default risk for the entire market.

Moreover, maintaining a higher unsecured credit limit for the CRR auction would be inconsistent with the Commission's recognition that similar financial products present unique risks that justify the elimination of unsecured credit. In the PJM Credit Policy Order, the Commission approved the *elimination* of the use of the unsecured credit allowance for financial transmission rights (PJM's version of CRRs) because "the FTR market presents unique risks that justify PJM's proposed credit policy revisions."¹¹ Unlike PJM, the ISO is not proposing to eliminate the use of the unsecured credit limit for CRRs. However, the fact that the Commission approved PJM's proposed elimination of the use of the unsecured credit allowance for financial transmission rights strongly suggests

¹¹ PJM Credit Policy Order at P 36.

that it is appropriate for the ISO to reduce the maximum unsecured credit limit from its current level, even if that reduction may require some market participants to rely less on unsecured credit and correspondingly more on financial security for the purpose of providing sufficient collateral to participate in the annual CRR auction.

Like the ISO, almost all of the other independent system operators and regional transmission organizations have market designs that include the use of tradeable financial rights for transmission congestion.¹² The market designs of those organizations also include maximum unsecured credit limits, but the maximum unsecured credit limits are not increased based on liabilities associated with tradeable financial rights.¹³ There is no reason for the Commission to require the ISO alone to maintain a higher maximum unsecured credit limit specifically to accommodate the collateral requirement for participation in the annual CRR auction.

¹² See Transmission, Markets and Services Tariff of ISO New England Inc., FERC Electric Tariff No. 3, at Sections III.5 and III.7 (addressing use of financial transmission rights under ISO New England market design); Open Access Transmission, Energy and Operating Reserve Markets Tariff of Midwest Independent Transmission System Operator, Inc., FERC Electric Tariff, Fourth Revised Volume No. 1, at Section IV (addressing use of financial transmission rights under Midwest ISO market design); Open Access Transmission Tariff of New York Independent System Operator, Inc., FERC Electric Tariff, Original Volume No. 1, at Section 1.44e and Attachment M (addressing use of transmission congestion credits under New York ISO market design); Operating Agreement of PJM, Third Revised Rate Schedule No. 24, at Section 5.2.2 (addressing use of financial transmission rights under PJM market design); Electric Reliability Council of Texas Protocols at Section 7.5 (addressing use of transmission congestion rights under ERCOT market design). The Southwest Power Pool does not offer financial transmission rights. *Southwest Power Pool, Inc.*, 126 FERC ¶ 61,244, at P 14 (2009).

¹³ See Transmission, Markets and Services Tariff of ISO New England, FERC Electric Tariff No. 3, Section I, Exhibit IA, at Section II(B)(2)(a); Open Access Transmission, Energy and Operating Reserve Markets Tariff of Midwest ISO, FERC Electric Tariff, Fourth Revised Volume No. 1, Attachment L, at Section II(C); Market Services Tariff of New York ISO, FERC Electric Tariff, Original Volume No. 2, Attachment K, at Section IV(B); Open Access Transmission Tariff of PJM, FERC Electric Tariff, Sixth Revised Volume No. 1, Attachment Q, at Section II(B) (Sixth Revised Sheet No. 523G); ERCOT Protocols at Section 16.8.1.5.2

Further, within the next couple of months the ISO will take steps to reduce the collateral requirement for participation in the annual and monthly CRR auctions. In August 2009, the ISO initiated a stakeholder process to develop enhancements to its CRR policy, including its policy regarding CRR credit requirements. The ISO is working with stakeholders on the CRR policy enhancements.¹⁴ Among other things, the proposed changes would reduce the minimum credit requirements for monthly auctions and would eliminate the requirements for collateral to back a negatively valued bid (though the credit margin requirement for negatively valued bids would still be required). The ISO plans to seek approval from its Governing Board for the credit policy enhancements in December 2009, and will then submit the credit policy enhancements that require tariff changes for Commission approval in January 2010.¹⁵ The ISO expects that these changes will reduce participant concerns about the amount of collateral required to take part in CRR auctions. Even without these changes, however, the ISO's reduction of the unsecured credit limit remains just and reasonable as explained in the September 4 Tariff Amendment and above.

¹⁴ Materials provided by the ISO in this stakeholder process, and stakeholder comments, are posted on the ISO's website at <http://www.caiso.com/2403/24037c20669e0.html>.

¹⁵ The ISO is still developing its schedule regarding the CRR policy enhancements not related to credit policy.

II. Conclusion

For the reasons explained above, the Commission should approve the reduction of the maximum unsecured credit limit to \$50 million as proposed by the ISO in the September 4 Tariff Amendment.

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Dated: October 13, 2009

CERTIFICATE OF SERVICE

I hereby certify that I have served the foregoing documents upon all of the parties listed on the official service list for the above-referenced proceeding, 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 Washington, D.C. this 13th day of October, 2009.

/s/ Bradley R. Miliauskas
Bradley R. Miliauskas