

126 FERC 61,285  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

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

California Independent System Operator Corporation      Docket No. ER09-589-000

ORDER ACCEPTING TARIFF REVISIONS

(Issued March 30, 2009)

1. On January 29, 2009, the California Independent System Operator Corporation (CAISO) filed revisions to its Market Redesign and Technology Upgrade (MRTU) tariff to modify its credit policy provisions.<sup>1</sup> As discussed below, the Commission accepts the tariff revisions effective March 31, 2009.

**I. The CAISO's Filing**

2. The MRTU tariff requires market participants that submit schedules or transact in the CAISO markets to either satisfy certain creditworthiness requirements or post financial security to provide assurance that they can meet their present and future financial obligations. Section 12 of the MRTU tariff describes the calculation of unsecured credit limits, creditworthiness requirements and the requirements for posting financial security. Additionally, section 12 details the circumstances under which a market participant can be found to fail to satisfy those requirements and steps the CAISO can take in response.<sup>2</sup>

---

<sup>1</sup> FERC Electric Tariff, Second Replacement Volume Nos. I and II.

<sup>2</sup> The CAISO notes that further implementation details regarding the credit provisions in section 12 are found in the applicable Business Practice Manual available on the CAISO website.

3. The CAISO states that since the California energy crisis of 2000-2001, it has periodically evaluated whether changes should be made to its credit policy in order to ensure that market participants satisfy creditworthiness standards or post financial security sufficient to cover all of their financial obligations in the CAISO settlement process and discourage defaults in the CAISO's markets.<sup>3</sup>

4. The CAISO requests that its tariff revisions be made effective as of March 31, 2009, which is the date that the CAISO anticipates MRTU will be implemented. The primary tariff changes proposed by the current filing include the following: (1) lowering the maximum unsecured credit limit<sup>4</sup> for any market participant from the current \$250 million to a proposed \$150 million; (2) modifying the process for determining the unsecured credit limit of a market participant from the current eight-step process to a simpler and more financially conservative six-step process; and, (3) modifying and enhancing the provisions of the tariff that are used to mitigate credit-related risk.<sup>5</sup>

5. The CAISO proposes two major changes to the process used to determine a market participant's unsecured credit limit. First, the CAISO proposes to no longer utilize the default probabilities calculated by the credit-risk analysis firm Moody's KMV. Instead, the CAISO proposes to utilize "Moody's KMV Equivalent Rating" (defined as the rating that effectively translates the Moody's KMV Estimated Default Frequency into a comparable credit agency rating), because the CAISO believes the Moody's KMV Equivalent Rating will yield less volatile results. Secondly, the CAISO proposes to determine unsecured credit limits using the lowest credit agency rating, rather than the average of such available ratings, as is utilized under the current tariff provisions. According to the CAISO, the purpose of this change is to employ more financially conservative criteria for determining unsecured credit limits. The CAISO also states that these revisions describe with greater specificity how it will calculate a market participant's tangible net worth and net assets and make adjustments for assets that are particularly volatile or that may be unavailable to settle a claim related to CAISO market obligations.

---

<sup>3</sup> CAISO transmittal letter at 2.

<sup>4</sup> The CAISO defines unsecured credit limit as "The level of credit established for a Market Participant or CRR [congestion revenue right] Holder that is not secured by any form of Financial Security, as provided for in Section 12." FERC Electric Tariff, Second Replacement Volume No. II, Original Sheet No. 963.

<sup>5</sup> The CAISO's proposed tariff revisions resulted from a stakeholder process that it undertook between September and December of 2008. *See* CAISO transmittal letter at 3.

## **II. Notice of Filings and Responsive Pleadings**

6. Notice of the February 5, 2009 filing was published in the *Federal Register*, 74 Fed. Reg. 7,415 (2009), with interventions or protests due on or before February 19, 2009.

7. The following parties filed timely motions to intervene: The City of Los Angeles Department of Water and Power; Sacramento Municipal Utility District; The Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California; Mirant Energy Trading, LLC, Mirant Delta, LLC, and Mirant Potrero; the California Department of Water Resources State Water Project; Northern California Power Agency (NCPA); The City of Santa Clara, California and M-S-R Public Power Agency; Transmission Agency of Northern California; and Reliant Energy, Inc.

8. Southern California Edison Company (SoCal Edison), Dynegy Morro Bay LLC, Dynegy Moss Landing, LLC, Dynegy Oakland, LLC, Dynegy South Bay, LLC (collectively, Dynegy), Powerex Corp. (Powerex), Modesto Irrigation District (Modesto), J.P. Morgan Ventures Energy Corporation and BE CA, LLC (collectively, J.P. Morgan), NRG Power Marketing LLC, Cabrillo Power I LLC, Cabrillo Power II LLC, El Segundo Power LLC, Long Beach Generation LLC (collectively, NRG) and Western Power Trading Forum (WPTF) filed timely motions to intervene and comments or protests. The CAISO filed an answer to the motions to intervene and comments, motion to file answer and answer to the protests. NCPA filed an answer.

## **III. Discussion**

### **A. Procedural Matters**

9. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2008), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

10. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2008), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We accept the answers filed by the CAISO and NCPA because each has provided information that assisted us in our decision-making process.

### **B. Substantive Matters**

#### **1. Lowering of the maximum unsecured credit limit**

11. The CAISO states that as currently set forth in sections 12.1.1 and 12.1.1.1, the maximum unsecured credit limit for any market participant is \$250 million. The CAISO notes that in a previous proceeding it explained that it might consider lowering the cap in

a future tariff amendment to reduce the risk participants in CAISO markets.<sup>6</sup> In this proceeding, the CAISO states it proposes to modify sections 12.1.1 and 12.1.1.1 to lower the maximum unsecured credit limit for any market participant to \$150 million.

12. The CAISO states that it is lowering the maximum unsecured credit limit after considering the maximum unsecured credit limits established by its peer Independent System Operators (ISOs) and Regional Transmission Organizations (RTOs), the historical estimated aggregate liabilities<sup>7</sup> of market participants in comparison to their maximum unsecured credit limits in recent years, and how estimated aggregate liabilities may change as a result of the implementation of MRTU. Further, the CAISO states the reduction of the maximum unsecured credit limit represents an appropriate step toward a more conservative credit policy in response to recent market participant defaults experienced in other ISO markets during 2008 and represents a compromise between the differing views of stakeholders regarding what the maximum unsecured credit limit should be.<sup>8</sup>

**a. Comments and Protests**

13. SoCal Edison supports the CAISO's desire for more conservative unsecured credit limits, but is concerned that a reduction to \$150 million at market start-up without the CAISO having a clear understanding of MRTU market exposure could dramatically increase credit and collateral obligations for market participants.<sup>9</sup> SoCal Edison notes that the CAISO has indicated that it is likely market participants' exposure to MRTU

---

<sup>6</sup> The CAISO cites the March 7, 2006 Transmittal Letter at 6-7, submitted in Docket No. ER06-700-000.

<sup>7</sup> The CAISO defines estimated aggregate liability as "The sum of a Market Participant's or CRR Holder's known and reasonably estimated potential liabilities for a specified time period arising from charges described in the CAISO Tariff, as provided for in Section 12." FERC Electric Tariff, Second Replacement Volume No. II, Original Sheet No. 865.

<sup>8</sup> CAISO transmittal letter at 4. The CAISO also explains that CAISO management recommends further reducing the maximum unsecured credit limit to \$50 million following the start of the CAISO's payment acceleration program, which the CAISO anticipates will be implemented within a few months after MRTU is implemented. Accordingly, the CAISO expects that it will make an additional tariff amendment in the future to reduce the maximum unsecured credit limit to \$50 million.

<sup>9</sup> SoCal Edison comments at 3.

market charges could increase to around twice the current, pre-MRTU amount based on reasonable expectations of a market participant's day-ahead market activity.<sup>10</sup> SoCal Edison states that a potential two-fold increase in market participants' estimated aggregate liability could create situations where a stakeholder's collateral requirements dramatically increase during the initial months of MRTU and remain at such increased levels until the markets stabilize. SoCal Edison also notes that in addition to the increase in a market participant's estimated aggregate liability, market participants may also experience an increase in the frequency of additional collateral requests as the CAISO transitions into MRTU.<sup>11</sup>

14. SoCal Edison proposes an alternative to the CAISO's proposal to lower the maximum unsecured credit limit for any market participant to \$150 million, effective concurrent with the start-up of the MRTU markets. SoCal Edison recommends that the reduction of the maximum unsecured credit limit take effect at the same time the CAISO implements its payment acceleration initiative.<sup>12</sup> SoCal Edison states that aligning the reduction in the maximum unsecured credit limit with the payment acceleration initiative will provide sufficient time for both the CAISO and market participants to adjust to actual market exposure under MRTU.

15. J.P. Morgan opposes the CAISO's proposal to continue to extend unsecured credit to market participants. J.P. Morgan recommends that the Commission reject the CAISO's proposal to extend the use of unsecured credit up to a cap of \$150 million. J.P. Morgan states that other commodity markets do not permit the use of unsecured credit; all participants in those markets must be fully collateralized. According to J.P. Morgan, the CAISO filing takes an incremental step in the right direction by reducing the unsecured credit limit from \$250 million to \$150 million, but J.P. Morgan states the proposal does not go far enough and fails to mitigate the risk posed to participants from the continued extension of unsecured credit to certain market participants. Moreover, J.P. Morgan asserts that the continued extension of unsecured credit in the CAISO's markets places the responsibility to manage credit risk on the CAISO and its staff. J.P. Morgan

---

<sup>10</sup> SoCal Edison cites the CAISO Board of Governors Memorandum dated 12/8/08. <http://www.caiso.com/2098/2098b3f758490.pdf>.

<sup>11</sup> *Id.*

<sup>12</sup> SoCal Edison cites the CAISO's payment acceleration criteria and timeline: <http://www.caiso.com/2338/2338dad5673d0.pdf>. The CAISO timeline anticipates an implementation date of October 1, 2009.

argues that such a responsibility would be best managed by expert risk managers and market participants themselves.

16. Should the Commission decide not to eliminate the use of unsecured credit in the CAISO's markets, J.P. Morgan proposes that a second-best alternative would be to reduce the maximum amount of unsecured credit to \$50 million, rather than the CAISO's proposed \$150 million.<sup>13</sup>

17. NRG states the CAISO's proposal does not adequately protect market participants against the risk that another market participant could default and require the market participants to bear the costs of that default. NRG argues that the proposal to reduce the amount of unsecured credit available to a market participant from \$250 million to \$150 million is an important first step, but that it does not go far enough in reducing credit risks, because it does not impose an appropriate unsecured credit limit on families of affiliated market participants, and is not consistent with best practices across the other RTO and ISO regions.<sup>14</sup>

18. NRG states that the \$150 million limit on unsecured lines of credit proposed by the CAISO in this proceeding is significantly higher than the maximum unsecured credit limits employed in the other organized markets. NRG points out that PJM, the only other market with a \$150 million cap on unsecured credit, has filed with the Commission a request to reduce the amount of unsecured credit available to individual market participants to \$50 million, with a total exposure limit of \$150 million for affiliated companies.<sup>15</sup>

---

<sup>13</sup> J.P. Morgan comments at 9. J.P. Morgan goes on to note that PJM Interconnection, L.L.C. (PJM) has recently filed proposed tariff revisions to reduce its maximum unsecured credit allowance from \$150 million to \$50 million in Docket No. ER09-650-000; the Midwest Independent Transmission System Operator, Inc. (MISO) has an established unsecured credit limit of \$50 million; ISO New England Inc. and New York Independent System Operator have established maximum unsecured credit limits of \$75 million; and the Southwest Power Pool has an established unsecured credit limit of \$25 million.

<sup>14</sup> NRG protest at 2.

<sup>15</sup> PJM proposed to reduce "by two-thirds the Unsecured Credit Allowance for individual member companies, including a reduction in the maximum from the current \$150 million to \$50 million and the establishment of a \$150 million affiliated group aggregate Unsecured Credit Allowance cap;" among other changes. See February 3, 2009 filing by PJM in Docket No. ER09-650-000 at 6-7.

19. NRG states that the CAISO proposal appears to only impose credit limits on individual market participants and does not impose a total credit limit on corporate families. According to NRG, extending \$150 million each to multiple affiliated companies represents an unreasonable credit risk and must be addressed before the Commission finds the proposed modifications just and reasonable. Specifically, NRG requests the Commission require the CAISO to modify Section 12.1.1 of the proposed tariff to read as follows: "The CAISO shall determine the Unsecured Credit Limit for each Market Participant or affiliated group of Market Participants in accordance with the procedures set forth in the applicable Business Practice Manual. The maximum Unsecured Credit limit for any Market Participant shall be set at \$50 million, and for a group of affiliated Market Participants shall be set at \$150 million."

20. Powerex argues that the CAISO's proposal to continue extending individual market participants \$150 million of unsecured credit subjects other market participants to an unacceptable amount of risk in the CAISO markets, especially under the new market design where all trades are cleared through the CAISO. In view of the significant problems with extending large amounts of unsecured credit in organized wholesale electricity markets, Powerex suggests the CAISO's proposed unsecured credit limit is not just and reasonable, and the Commission should require the CAISO to lower its unsecured credit limit further.

21. Powerex notes that ISO/RTO markets inherently involve some level of credit risk for market participants. Powerex states its concern by reference to the Commission's 2004 *Policy Statement on Electric Creditworthiness*,<sup>16</sup> in ISO/RTO markets, "credit is collectively extended by market participants to each individual market participant. As a result, if one market participant defaults, it falls upon the remaining participants to make up the shortfall (i.e., the default risk is mutualized)."<sup>17</sup> Powerex argues that unsecured credit increases these inherent risks by allowing entities to participate in markets without adequate assurances they can pay the obligations they incur. Powerex contends that the higher the permissible unsecured credit limit, the higher the market's exposure to large defaults, and the higher the credit risk to individual market participants.<sup>18</sup> Powerex notes

---

<sup>16</sup> *Policy Statement on Electric Creditworthiness*, 109 FERC ¶ 61,186 (2004) (Creditworthiness Policy Statement).

<sup>17</sup> *Id.* P 5.

<sup>18</sup> Powerex protest at 8, citing *Credit and Capital Issues Affecting the Electric Power Industry*, Technical Conference Transcript at 92, Docket No. AD09-2-000 (Jan. 13, 2009) (comments of Robert Ludlow, Vice President and Chief Financial Officer, ISO New England).

that the CAISO itself has acknowledged on prior occasions that lowering the amount of unsecured credit allowed in its markets reduces credit risk to other market participants.<sup>19</sup> Despite these risks, according to Powerex, the CAISO has not provided any compelling rationale in support of what Powerex considers the extreme level of unsecured credit proposed here.

22. Powerex states that the CAISO's proposed unsecured credit limit is inconsistent with the amount of unsecured credit extended by other organized electricity markets. In addition, Powerex states it is also problematic given the CAISO's imminent implementation of a new market design on March 31, 2009, certain regulatory and economic risks faced by California entities, and the CAISO's existing long payment and settlement timeframes. Powerex argues these features increase the possibility of defaults in the CAISO's markets, and make the high level of unsecured credit extended by the CAISO in its markets more troubling.<sup>20</sup>

23. Powerex contends that the addition of a day-ahead market will mean that the CAISO will go from being predominantly a transmission provider with a balanced energy market to a major financial clearinghouse with unbalanced markets. As recently described by other market participants, the CAISO's implementation of a day-ahead market "will result in a quantum jump in the amount of money flowing through the CAISO's settlements."<sup>21</sup> Given the increased amount of dollars that will be flowing through the CAISO, and the fact that the MRTU market design shifts from a balanced (predominantly bilateral) market to a centrally cleared CAISO market, Powerex asserts that participants under MRTU may now come close to using the full amount of the CAISO's proposed unsecured credit limit.

24. Powerex contends that a final problem with the CAISO's proposed high unsecured credit limit results from the CAISO's lengthy settlement and payment cycle. Noting that under the current CAISO Tariff, the average cash clearing cycle takes 80 days from the trading day to the date payment is due, Powerex argues that long settlement periods add

---

<sup>19</sup> *Id.* citing CAISO March 2006 Credit Policy Amendments, Transmittal Letter at 6-7, filed in Docket No. ER06-700-000 (Mar. 7, 2006); CAISO Compliance Filing and Status Report, Transmittal Letter at 3, filed in Docket No. ER06-700-003 (July 11, 2006).

<sup>20</sup> Powerex protest at 10.

<sup>21</sup> Powerex protest at 11, citing *Joint Response of Pacific Gas and Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company to the CAISO's MRTU Readiness Certification* at 5, filed in Docket No. ER06-615-038 (Feb. 6, 2009).



significant credit risk in ISO/RTO markets.<sup>22</sup> According to Powerex, the CAISO is only proposing to accelerate its payment schedule well after MRTU startup.<sup>23</sup>

25. Powerex states that the preferable solution for these significant problems would be for the CAISO to eliminate the use of unsecured credit from its markets entirely. Powerex understands this may not be feasible at present. However, at the very least, Powerex asserts that the CAISO should decrease its maximum unsecured credit limit significantly below the proposed level of \$150 million. Powerex requests that until payment acceleration and new loss-sharing rules are implemented, the CAISO should lower the unsecured credit limit to a much lower amount, no higher than \$25 million. Powerex notes that the CAISO has indicated it will lower the unsecured credit limit to \$50 million once payment acceleration is implemented. Powerex contends if losses are to be allocated to only one-half of market participants, it is reasonable to reduce the unsecured credit limit to one-half of the proposed amount. At such time as the loss-sharing rules are changed and payment acceleration is implemented, Powerex suggests that the unsecured credit limit could be increased to the \$50 million amount currently envisioned by the CAISO.

**b. The CAISO's Answer**

26. In its answer, the CAISO reiterates that its proposed maximum limit on unsecured credit of \$150 million represents a compromise between the differing views of stakeholders on the issue and that the proposal reflects a step toward a more conservative credit policy. The CAISO points out that it has already reduced its maximum limit on unsecured credit from a situation in which, prior to 2006 there was no maximum limit on unsecured credit. More importantly, the CAISO points out that it has already signaled its intention to lower the unsecured credit limit further following the start of its payment acceleration program, anticipated to occur within a few months following the commencement of MRTU.<sup>24</sup>

---

<sup>22</sup> *Id.* at 12, citing Creditworthiness Policy Statement, 109 FERC ¶ 61,186 at PP 21-23. "The size of credit risk exposure is, in large part, a function of the length of time between completion of the various parts of electricity transactions, i.e., the provision of service, the billing for service, and the payment of service." *Id.* at P 21.

<sup>23</sup> *Id.*, citing CAISO transmittal letter at n.7.

<sup>24</sup> CAISO answer at 3.

27. In addition, the CAISO points out that the maximum unsecured credit limit is only a maximum. The CAISO states that the extension of unsecured credit is determined on a case-by-case basis, utilizing qualitative and quantitative criteria as set forth in the tariff, some of which are also subject to proposed adjustment in the tariff revisions currently under consideration.<sup>25</sup> The CAISO indicates that it frequently assigns unsecured credit limits to market participants that are lower than the maximum, and in some instances are zero. The CAISO also points out that the creditworthiness and financial condition of a market participant's affiliates is among the criteria utilized in determining unsecured credit limits. Thus, the CAISO submits that it is unnecessary to specify a single unsecured credit limit that applies to all affiliates on a blanket basis.

28. The CAISO recognizes that its maximum unsecured credit limit is higher than those of other ISOs and RTOs, as was pointed out by protesters. The CAISO argues that this difference in limits is justified by the longer settlement cycles that are anticipated at the outset of MRTU, until payment acceleration is implemented. Finally, by way of response to Powerex's suggestion that the CAISO should not offer unsecured credit at all, the CAISO points out that every ISO and RTO currently offers some level of unsecured credit. The CAISO contends that the elimination of unsecured credit as an available option in the current proceeding would be a disruption to the market participants who rely on its credit policy.<sup>26</sup>

**c. NCPA's Answer**

29. In its answer NCPA states that the CAISO has filed a package of changes to its MRTU tariff credit policies that has been fully vetted in the CAISO stakeholder process. NCPA notes that it did not support every element of the package, but recognizes that the CAISO has attempted to balance the competing interests of net buyers and sellers in what all parties appear to concede will be markets of much greater scope against the backdrop of relatively uncertain financial markets. NCPA opposes the pleadings of interveners seeking a Commission directive to the CAISO to dramatically reduce or eliminate the amount of unsecured credit liability that the CAISO makes available to participants in its MRTU markets. NCPA states that because collateral is not a cost-free proposition, some amount of unsecured credit is desirable for all creditworthy market participants to increase flexibility of operations and keep overall costs to ratepayers lower than it would otherwise be.

---

<sup>25</sup> *Id.* at 4.

<sup>26</sup> *Id.* at 7.

30. NCPA states that credit requirements in any market must represent a balance between the interests of net buyers and net sellers.<sup>27</sup> NCPA states that the Commission has recognized that a requirement that load-serving entities post collateral for every market exposure would impose significant costs on market participants (and their ratepayers) and would represent a serious barrier to entry into the markets.<sup>28</sup> NCPA supports the CAISO's accelerated payment schedule, since more rapid settlements will reduce the amount of potential credit liability market participants have at stake at any given point in time.

31. NCPA states that any consideration of changes to unsecured credit limits beyond what the CAISO has proposed herein must consider the ultimate costs to ratepayers and the potential impact on smaller market participants who need flexibility in their operations.<sup>29</sup> According to NCPA, if the Commission wants the CAISO to undertake further changes in its collateral policies under MRTU, the Commission should require a balanced process.

32. NCPA states that it has joined a complaint filed by the California Municipal Utilities Association (CMUA) on March 4, 2009 in Docket No. EL09-38-000, where CMUA seeks to put into place an interim payment mechanism designed to ensure that sellers are fully compensated for their costs while the CAISO investigates any invoices of unusually large size (in simulations, many market participants have received simulated charges for many multiples of what they pay for similar service under the current tariff). According to NCPA, this proposal would avoid financial strain on buyers while protecting sellers. In short, rather than refusing to pay bills, NCPA states that it is

---

<sup>27</sup> NCPA answer at 3. NCPA argues that the Commission has recognized in its *Policy Statement on Electric Creditworthiness*, 109 FERC ¶ 61,186 (2004) that in organized markets, an ISO must serve as a gatekeeper to ensure that market participants are sufficiently collateralized to stand behind their transactions and ensure payment in a market where parties can no longer assess the risk of particular counterparties but are instead at risk for shortfalls in the market as a whole.

<sup>28</sup> *Id.* citing *Creditworthiness Policy Statement*, 109 FERC ¶ 61,186 at P 19.

<sup>29</sup> *Id.* at 5, NCPA notes that concerns about collateral costs are not unique to small entities. In its comments in the instant docket, SoCal Edison seeks a delay in the implementation of the reduction of unsecured credit limits proposed herein until some operational experience is gained under MRTU. SoCal Edison fears "unnecessary financial strain" from "an endless cycle of weekly collateral requests from CAISO" that could needlessly affect the financial positions of market participants. SoCal Edison comments at 3-4.

participating in efforts to have a safety mechanism in place to keep money flowing in the event that the types of unusually large billings observed in simulation occur in the real market.

**d. Commission Determination**

33. The Commission accepts the CAISO's tariff revisions to reduce the maximum unsecured credit limit from \$250 million to \$150 million. The CAISO's proposed reduction in the maximum unsecured credit limit to \$150 million represents an appropriate balance between limiting market participants' exposure to default risk, while allowing market participants to participate in MRTU markets without having to post unduly large amounts of financial security.

34. The Commission disagrees with the protestor's argument that the CAISO's proposed maximum unsecured limit is unreasonably high and should be reduced to align with other ISO/RTOs. We agree with the CAISO that the lower maximum unsecured credit limits in other ISO/RTOs is in part a function of shorter settlement cycles compared to the anticipated settlement cycle at the commencement of MRTU. The Commission also notes that CAISO intends to further reduce its maximum unsecured credit limit to \$50 million upon implementation of its payment acceleration program,<sup>30</sup> which the CAISO states is anticipated to occur within a few months following the commencement of MRTU. The Commission finds that a proposed maximum unsecured credit limit of \$150 million, considering the CAISO's current settlement process, is just and reasonable and we will not, at this time, direct the CAISO to lower its maximum unsecured credit limit, beyond the proposed \$150 million.

35. The Commission also rejects NRG's protest that the CAISO should impose a separate \$150 million maximum unsecured credit limit for groups of affiliated market participants. As noted by the CAISO in its answer, section 12.1.1.4 of the MRTU tariff, provides that the CAISO consider the creditworthiness and financial condition of a market participant's affiliates when determining whether and the extent to which that market participant is entitled to an unsecured credit limit. Further, section 12.1.1.4 of the MRTU tariff states, "The CAISO may determine that the maximum Unsecured Credit Limit specified in Section 12.1.1 applies to the combined activity of such Affiliates." The MRTU tariff contains sufficient protections, which allow the CAISO to limit the

---

<sup>30</sup> CAISO transmittal letter at 4. The CAISO explains that CAISO management recommends further reducing the maximum unsecured credit limit to \$50 million following the start of the CAISO's payment acceleration program, which the CAISO anticipates will be implemented within a few months after MRTU is implemented.

overall amount of unsecured credit of affiliated market participants. In the absence of evidence that the CAISO has failed to appropriately implement these protections, we decline to impose additional requirements.

36. The Commission also rejects SoCal Edison's request that the maximum unsecured credit limit remain at \$250 million at the commencement of MRTU and be reduced to \$150 million only upon implementation of the CAISO's payment acceleration program. The Commission agrees with the CAISO that the reduction to \$150 million is an appropriate move towards a more conservative credit policy, represents an appropriate balancing of interests among stakeholders and is also 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.

37. The Commission rejects J.P. Morgan's request to eliminate the use of unsecured credit in the CAISO markets as a collateral attack on the Commission's previous orders approving the use of unsecured credit in CAISO markets.<sup>31</sup> Further, as noted by the CAISO in its answer, the Commission has previously rejected the notion of eliminating unsecured credit in ISO and RTO markets.<sup>32</sup>

## 2. Enhanced Mitigation of Credit-Related Risk

38. The CAISO states that it proposes changes to enhance the tariff provisions that are used to mitigate credit-related risk. The CAISO notes that these revisions resulted from comparing the CAISO's credit policy to the credit policies of other ISOs and RTOs.<sup>33</sup>

39. The CAISO states it proposes to revise sections 12.1.3.1.1, 12.4, 12.4.1, and 12.4.2 to reduce the amount of time allowed for market participants to post additional financial security requested by the CAISO from five to three business days. The CAISO also proposes to revise section 12.1.3.1.1 to state that a market participant's estimated aggregate liability represents the amount owed to the CAISO for the obligations for the number of trading days outstanding at a given time, based on the CAISO's payments calendar plus five trading days, in lieu of an additional seven trading days.

---

<sup>31</sup> *Cal. Indep. Sys. Operator Corp.*, 114 FERC ¶ 61,119 (2005); *Cal. Indep. Sys. Operator Corp.*, 115 FERC ¶ 61,170, at P 20 (2006).

<sup>32</sup> Creditworthiness Policy Statement, 109 FERC ¶ 61, 186 at P 19.

<sup>33</sup> CAISO transmittal letter at 5.

40. The CAISO also proposes to add new sections 12.5.2 and 12.5.3 to provide for CAISO enforcement actions against market participants that fail to timely post additional financial security and that fail to timely pay an amount set forth in an invoice from the CAISO.

41. The CAISO states that the CAISO will send a warning letter to a market participant after the second time that the market participant is delinquent during a rolling twelve-month period. After the third time that a market participant is late to post additional financial security during a rolling twelve-month period, the CAISO states that it may require the market participant to post additional financial security. That amount may be as high as the highest level of the market participant's estimated aggregate liability during the preceding twelve months, and the CAISO will hold the additional financial security for at least twelve months. If the market participant is late again in posting additional financial security, the additional financial security may be held for a longer period of time.

42. Similarly, the CAISO states that after the third time that a market participant is late in paying the amount set forth in an invoice during a rolling twelve-month period, the CAISO proposes that it may revoke the market participant's unsecured credit limit and require the market participant to post cash to secure its financial obligations. These measures will continue in effect for at least twelve months and possibly longer if the market participant is late again in paying an amount set forth in an invoice.

43. In addition, the CAISO states that it proposes to revise section 12.6.2 to limit the amount that a CRR holder or candidate CRR holder can allocate to a CRR auction to ninety percent of available credit. The tariff currently permits a one hundred percent allocation. The CAISO states that the tariff change will provide an adequate reserve of available credit for market participants to engage in other market activities.

**a. Comments and Protests**

44. Modesto opposes the CAISO's proposal to reduce the amount of time allowed for market participants to post additional financial security from five to three business days. Modesto states that three days is too short a time period for Modesto to comply with requests for additional financial security and therefore, Modesto states it is at risk of undesirable and unnecessary credit scenarios. Modesto states that it typically directs its accounts payable department by 3:00 p.m. on any given business day to make a payment to the CAISO in order to ensure payment is received by the CAISO by 10:00 a.m. the next day. Modesto notes that, as a result, it would have roughly two business days to respond to a request by the CAISO that it post additional financial security. Modesto states this short turn-around may be impossible to comply with, if key personnel are unavailable during that two business day window. Modesto requests that the

Commission direct the CAISO to maintain five business days as the deadline by which to post additional financial security requested by the CAISO.

45. Modesto does not object to the CAISO's proposal to revise section 12.6.2 to limit the amount that a CRR holder or candidate CRR holder can allocate to a CRR auction to ninety percent of available credit, but questions why the ninety percent limit is appropriate. Modesto states that it would be more appropriate to determine the amount of credit available based on the amount owed to the CAISO.

**b. The CAISO's Answer**

46. The CAISO notes that J.P. Morgan, Powerex and WPTF all support its proposal to reduce the time period for satisfying a CAISO request for additional financial security from five days to three. In response to Modesto's objection, the CAISO notes that if a posting takes Modesto two business days, Modesto would still have an additional business day in which to make a required posting.<sup>34</sup> The CAISO states that its proposal allows market participants at least as much time to make required financial security postings as is provided by other ISOs and RTOs, and states that its proposal is the result of benchmarking the CAISO's credit policies against those of other ISOs and RTOs.

**c. Commission Determination**

47. We accept the CAISO's tariff revisions to mitigate credit-related risk. Further, we agree with the CAISO that its proposal to reduce the number of business days allowed for market participants to post additional financial security should mitigate credit-related risk, while still providing adequate time for market participants to satisfy requests for additional financial security.

48. We deny Modesto's request that we direct the CAISO to maintain a five business day window to post additional financial security. As discussed above, we find CAISO's proposal to reduce the amount of time allowed for market participants to post additional financial security requested by the CAISO from five to three business days to be an appropriate provision for the CAISO. Further, the three business day limit is consistent with tariff requirements approved by the Commission for other ISOs and RTOs.<sup>35</sup> The

---

<sup>34</sup> CAISO answer at 8.

<sup>35</sup> PJM Interconnection, L.L.C., FERC Electric Tariff, Sixth Revised Volume No. 1, Third Revised Sheet No. 523D states, "PJM may require the Participant to provide Financial Security within two Business Days, in an amount and form approved by PJM." Midwest ISO, FERC Electric Tariff, Third Revised Volume No. 1, First Revised Sheet No. 1217 states, "The Participant will have two (2) Business Days from receipt of written

Commission finds that three business days is a reasonable period of time, for a market participant to post additional financial security.

### **3. Payment Default Allocation Methodology**

49. The CAISO's existing methodology for allocating losses from a payment default is provided at section 11.29.9.6.2.1(c) of its MRTU tariff.<sup>36</sup> The CAISO makes no mention of the methodology for allocating losses upon default in payments, and proposes no changes to this methodology in connection with its tariff filing in this docket. All of the tariff revisions proposed in connection with this filing involve section 12 of the CAISO's MRTU tariff. Rather, by this filing the CAISO proposes to amend its credit policies as represented in section 12 of the MRTU tariff. As noted by J.P. Morgan, the CAISO has affirmatively decided to defer consideration of changing the way losses from a payment default are allocated to a separate stakeholder process likely to be commenced after the inception of MRTU.<sup>37</sup> Nevertheless, J.P. Morgan, WPTF and Powerex have all protested the CAISO's decision to not propose tariff amendments associated with its payment default allocation methodology in this docket.

#### **a. Comments and Protests**

50. J.P. Morgan disagrees with the CAISO's decision to defer addressing the payment default allocation methodology. J.P. Morgan asserts that this is a critical missing piece of the CAISO's proposal. J.P. Morgan believes the existing payment default allocation methodology is unjust, unreasonable, and discriminatory. J.P. Morgan recommends that the Commission direct the CAISO to modify the default allocation methodology to

---

notification (three (3) Business Days if notification occurs after noon Eastern Daylight Time) to provide the required Financial Security, in an amount and form approved by the Transmission Provider.”

<sup>36</sup> Section 11.29.9.6.2.1(c) provides as follows: “If after taking reasonable action the CAISO determines that the default amount (or any part) and/or Interest cannot be recovered, such amounts shall be deemed to be owing by those Market Participants who were CAISO Creditors on the relevant Payment Date pro rata to the net payments they received on that Payment Date and shall be accounted for by way of a charge in the next Settlement Statements of those CAISO Creditors.”

<sup>37</sup> J.P. Morgan comments at 10, citing a December 8, 2008 CAISO Governing Board memorandum entitled “*Decision on Credit Policy Enhancements*,” at 1-2, posted at <http://www.caiso.com/2098/20988a9a1ea70.html>.



allocate the cost of defaults of any unsecured creditor to either those market participants that voluntarily rely on unsecured credit or, consistent with the practices in place in other organized electricity markets, all market participants based on gross billings in the market. Additionally, J.P. Morgan states that the cost of any other defaults should be allocated to all market participants based on gross billings. Alternatively, J.P. Morgan recommends that the Commission immediately initiate a section 206 proceeding and order a paper hearing process to expeditiously address this issue.

51. WPTF believes the current allocation of default risk to be unjust and unreasonable and urges the Commission, *sua sponte*, to direct the CAISO to change its default allocation before MRTU is implemented. WPTF requests that the Commission direct the CAISO to allocate defaults in its markets in the same way that other independent system operators do so, namely, to all market participants *pro rata* based on the gross absolute value of energy injections and withdrawals.<sup>38</sup> WPTF asserts that this change is necessary if the Commission approves the proposed interim payment mechanism and thus modifies the long-standing “pay and dispute” provisions of the CAISO tariff.<sup>39</sup> WPTF urges the Commission to resolve and correct the default allocation provisions when acting on the CAISO’s January 16, 2009, MRTU Readiness Certification.

52. Powerex contends that the risks that result from the high level of unsecured credit permitted by the CAISO become unreasonable when considered with the CAISO’s policies for allocating uncollected debts from defaulting market participants. Powerex argues that these provisions, which allocate losses from market participant defaults solely to net creditors, are unduly discriminatory and therefore must be revised in order for the Commission to approve the credit policy enhancements proposed by the CAISO in this proceeding. Powerex asserts that although the CAISO has not proposed to revise its default loss-sharing provisions in the instant filing, the Commission cannot consider the reasonableness of the CAISO’s credit proposal without also addressing its default loss-sharing mechanism.

53. Powerex asserts that the CAISO itself has recognized that its policy of “short paying net suppliers to the market creates a disincentive for suppliers to participate in the CAISO market.”<sup>40</sup> Powerex states that the Commission has also previously recognized that mutualized loss-sharing and credit policies that fail to mitigate default risks were

---

<sup>38</sup> WPTF protest at 3-4.

<sup>39</sup> CAISO 4th Replacement Tariff, Section 11.29.8.7.

<sup>40</sup> Powerex protest at 19, citing a CAISO Credit Policy White Paper at 26.

likely to “dampen” the willingness of entities to participate in ISO/RTO markets.<sup>41</sup> Powerex contends this risk would appear to be even greater where the ISO/RTO allocates the risk of defaults only to those entities selling into the markets. Powerex contends the CAISO’s default loss-sharing provisions are also problematic given the large amount of unsecured credit that the CAISO permits. Powerex requests that the Commission direct the CAISO to implement a more equitable loss-sharing mechanism immediately, so that any changes can be made prior to, or as soon as possible after, MRTU implementation.

**b. The CAISO’s Answer**

54. The CAISO opposes suggestions that the Commission should either direct it to revise the existing policy for allocating the costs of payment defaults or establish an investigation on the issue pursuant to section 206 of the Federal Power Act (FPA).<sup>42</sup> The CAISO notes that the proposed tariff revisions in this proceeding do not contain any proposed revisions regarding payment default allocation. As a result, the CAISO states that the parties’ requests are beyond the scope of this proceeding and should be rejected.<sup>43</sup>

55. The CAISO states that its management has committed to continued evaluation of the issue of payment default allocation and recommends that the matter be further discussed in a stakeholder process that is likely to commence after the start-up of MRTU. The CAISO suggests that parties interested in discussing the issue should do so in the course of the stakeholder process. Additionally, the CAISO notes that parties have the opportunity to file a complaint with the Commission pursuant to section 206 of the FPA.<sup>44</sup>

56. Finally, the CAISO states that resolution of any issues regarding payment default allocation should not be tied in any way to the implementation of MRTU. The CAISO notes that it submitted a filing to the Commission in January that certifies its readiness to implement MRTU on March 31, 2009, provided that certain milestones and assumptions are satisfied.<sup>45</sup> The CAISO contends that the implementation of MRTU, and the

---

<sup>41</sup> *Id.* at 17, citing *Creditworthiness Policy Statement*, 109 FERC ¶ 61,186 at P 18.

<sup>42</sup> 16 U.S.C. § 824e (2006).

<sup>43</sup> CAISO answer at 10.

<sup>44</sup> *Id.*

<sup>45</sup> *See California Independent System Operator Corporation, MRTU Readiness Certification*, Docket No. ER06-615-038 (January 15, 2009).

satisfaction of necessary milestones and assumptions, are unrelated to the question of whether the existing tariff provisions concerning payment default allocation should be modified.<sup>46</sup>

**c. NCPA's Answer**

57. In its answer, NCPA states it would not necessarily oppose a change in the CAISO's policy for allocation of default among market participants. NCPA is both a load serving entity and a generation owner. As a result, NCPA asserts that it is sometimes a net buyer in the market and sometimes a net seller. NCPA contends that a change to the allocation of default risk could be worth considering, but only as part of an overall review of credit policies and the interests of all market participants. However, the solution to the credit concerns of net sellers to the CAISO market cannot be the elimination of unsecured credit, which provides some protection to load-serving entities from what can be very expensive collateral costs for each and every liability.<sup>47</sup>

**d. Commission Determination**

58. We deny the J.P. Morgan, WPTF and Powerex protests requesting that the Commission direct the CAISO to alter its currently effective payment default allocation process in this proceeding. We agree with the CAISO that the issue is beyond the scope of this proceeding. The CAISO has proposed no revisions to the payment default allocation process in this proceeding and the protesting parties have not demonstrated that the existing payment default allocation process accepted by the Commission renders the MRTU tariff unjust, unreasonable or unduly discriminatory. However, we note that the CAISO's management has committed to continued evaluation of the issue and recommends that the matter be further discussed in a stakeholder process. We support this recommendation and encourage the CAISO to complete that process quickly.

59. We also deny the J.P. Morgan, WPTF, and Powerex requests that we initiate a proceeding under section 206 of the FPA and order a paper hearing process to address the CAISO's default allocation methodology. We find these requests too broad and without sufficient substantiation to warrant relief. Parties seeking Commission action must, at a minimum, make specific allegations and provide some basis to question the reasonableness of an accepted tariff.<sup>48</sup> Accordingly, the requests to initiate proceedings

---

<sup>46</sup> CAISO answer at 10-11.

<sup>47</sup> NCPA answer at 4.

<sup>48</sup> *Algoma Group v. Wis. Pub. Serv. Corp.*, 61 FERC ¶ 61,265, at 61,959 (1992).

Docket No. ER09-589-000

20

under FPA section 206 are rejected. The rejection is without prejudice to the parties' filing of a properly developed complaint.

The Commission orders:

The CAISO tariff filing is hereby accepted, to be effective on March 31, 2009, the anticipated date of MRTU implementation, as discussed in the body of this order.

By the Commission.

( S E A L )

Kimberly D. Bose,  
Secretary.

Document Content(s)

ER09-589-000.DOC.....1-20