



Comments of Argus Media to the California Independent System Operator on its BPM proposed revision request: “Commitment costs refinement 2012 – Greenhouse Gas cost adder”

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Argus Media appreciates the opportunity to respond to the California Independent System Operator (CAISO) on its December 3, 2012 Business Practice Manual Proposed Revision Request: “Commitment costs refinement 2012 - Greenhouse Gas cost adder.” Argus believes it can make a meaningful contribution to this discussion and is uniquely positioned to assist CAISO in building its methodology for cost-calculation indexation. Argus is an independent price reporting organization, not a market participant, and therefore our comments will focus primarily on Attachment K (Greenhouse Gas Allowance Index Price Calculation, Contribution to Cost-based Calculations, And Examples), which proposes the use of price indexes, including Argus’, for California Carbon Allowances in cost-based calculations.

Argus Media and its role in energy and emissions market indexation

As an independent price reporting organization, Argus Media publishes daily and weekly prices for US emissions markets. These spot markets represent the marginal clearing price in an open and arms-length market. These prices are used by energy companies, financial services and governments as price references or price benchmarks. The prices are used to index long term contracts, spot market contracts, derivatives transactions such as swaps, and are used in corporate internal transfer pricing, market analysis, performance measures, risk management analysis and capital investment decisions. Government entities also frequently use Argus spot market prices to determine taxation and royalty calculations.

Argus has an important role in the proper functioning of the energy markets. Confidence in the prices published by Argus creates confidence in the markets themselves, which in turn encourages liquidity, effective clearing of trades, accurate price discovery and overall market transparency.

Argus recognizes that its clients and other industry stakeholders expect it to meet the highest standards in the field of price reporting, and to value principles that support its important role. Argus has robust governance and

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illuminating the markets

operates a rigorous and transparent controls framework including an Editorial Code of Conduct and an ethics and compliance policy entitled Argus Global Compliance Policy, all publicly available on its website. As an independent price reporting organization, Argus is independent of the markets and has no vested interest in the level of any price that it reports. Argus has clear policies in place to avoid conflicts of interest and prohibits its employees from trading in the commodities or industries upon which it reports. A Global Compliance Officer oversees the company's compliance regime. This includes a rolling program of audits to ensure full and continuous adherence to the company's compliance policy.

Argus also respects transparency and disclosure by making its processes public, and by providing market information openly. Argus ensures that it has the resources to achieve these values, by hiring and retaining qualified and experienced staff, and regularly training employees. Argus maintains its credibility as an independent price reporting organization by consistently applying its methodologies for price identification, and thus maintaining its high and long-standing reputation.

Argus uses a market-appropriate methodology to assess prices in the markets it covers. Argus consults with the range of participants involved in different markets and publishes methodologies for each price report on its website. Each methodology is reviewed regularly to ensure that it always meets the needs of market participants and is in line with industry practice. Argus seeks to reflect the way markets are traded, rather than impose its own view.

The prices reported by Argus and other independent price reporting organizations allow the energy sector to operate efficiently and effectively to the benefit of consumers and producers. Term contracts can be indexed to a transparent spot market price at an active market center and counterparties can be sure that they are receiving fair market value. This same system of indexation can be trusted by government entities as a robust representation of market value for emissions allowances, including California Carbon Allowances.

CAISO Attachment K: Greenhouse Gas Allowance Price Calculation, Cost-based Bid Calculations, and Examples

We agree that the CAISO cost containment mechanism should use an average of commercially available price indexes of active allowance markets. This is the best way to account for generators' compliance costs under California's greenhouse gas cap-and-trade program.

Argus Air Daily is the leading provider of market price information for settlement in the over-the-counter markets. Argus price indexes are currently used by the US emissions markets for settlement of spot and forward trading. Argus currently publishes environmental market indexes for:

- Sulphur emission allowances in US SO₂ program trading (CAIR)
- Emission allowances in US annual and seasonal NO_x trading programs (CAIR)
- SO₂ and NO_x emissions in the Cross-state Air Pollution Rule markets
- Renewable energy certificates for markets in Connecticut; Massachusetts; New Jersey; Pennsylvania; Maryland; Ohio; California; and Texas, plus national and WECC voluntary Green-e wind
- CO₂ allowances in the Regional Greenhouse Gas Initiative
- California Carbon Allowance and offset markets

Argus was the first publisher of California Carbon Allowance indexes and remains the only publisher of daily price assessments and volume-weighted averages.

It is appropriate to incorporate an average of at least two commercially available market data sources in the index-creation methodology. Argus has published a daily price assessment for the December 2012 and

December 2013 delivery contracts for current vintage CCAs since August 2011, and has published a weekly assessment for California-compliant carbon offsets issued by the Climate Action Reserve since January 2011.

This breadth of market price identification and depth in emissions markets gives Argus a unique and compelling position as the leading price identification platform in California Carbon and other environmental markets.

Trading in California Carbon Allowances has been active on the Intercontinental Exchange (ICE) and the ICE is a relevant provider of price information. Index creation averaging Argus and ICE data is an appropriate methodology for allowance indexation, and will bridge differences between ICE CCA contracts and California Allowance Forward Trade Agreement contracts. The latter are the predominant over-the-counter contracts and pricing for these has sometimes differed from the exchange-traded variety. The markets for these products trade and settle separately.

Such distinctions are of crucial importance when examining the price identification function and provide independent price reporting organizations like Argus significant advantage over spot settlement based on financial derivatives prices on exchanges like ICE CCA trading. Large purchases for compliance are often done over the counter so that buyers can include specific provisions, such as credit requirements, performance assurance and delivery requirements. Using only exchange settlements could exclude such trades, leading to an index that does not accurately depict generators' actual compliance costs.

This has been avoided in other emissions markets through the widespread use of Argus emissions indexes, and Argus has been active in the development and settlement of California Carbon Allowance trading to date.

Argus conducts broad surveys of brokers, traders, generators and utilities to identify daily prices for environmental commodities. Assessments are available in the *Argus Air Daily* publication, the Argus website and via data feeds, and have become recognized for broad use in the emissions markets and those affected by them. As recently as this month, Argus-published prices have been reconfirmed as settlement value for emissions trading under Acid Rain and successor program's SO₂ allowances by the Coal Trading Association's standard trading contract. That contract uses Argus-published SO₂ price indexes to value sulphur adjustments in US and international coal supply agreements.

Forward delivery period selection and trading period

CAISO also proposes to use a spot price or the nearest forward period. But the most active delivery may actually be a contract for delivery beyond the prompt forward period. The value of liquidity is significant and Argus believes should be reflected in delivery period selection. Where there is a significant difference between the spot, prompt and most active deliveries, this should be considered in delivery selection. Argus publishes details of the transactions used in its index-creation process and this transactional basis would help CAISO select the most appropriate delivery period for this use.

Argus keeps close track of CCA and offset trades and diligently seeks to verify all trades reported each day. Market participants can access further details of the CCA assessment procedures in the *Argus Air Daily* methodology, available online at the following address:

<http://www.argusmedia.com/~media/Files/PDFs/Meth/add.ashx>. A copy of our methodology, current as of this comment document, has also been provided and should be considered a component of our comments to CAISO on this matter.

Conclusion

In conclusion, Argus considers that the CAISO should feel confident about its proposed index-creation methodology as detailed in Attachment K, "Greenhouse Gas Allowance Price Calculation, Cost-Based Bid Calculations, and Examples." Creating an index of published, commercially available spot allowance prices allows for accurate, robust and market-based calculation of Greenhouse Gas Allowance impact. Argus spot market price identification is an important element in ensuring that the CAISO process accurately reflects the

whole CCA market instead of trading on any single derivatives exchange. These published indexes are available now and Argus strives to enhance our products, including California Carbon Allowance prices in *Argus Air Daily*, continuously.

Argus welcomes the opportunity to work with CAISO on this matter and is glad to answer any questions that may arise from our comments.