



SB 540 - Pathways Initiative

SUMMARY

SB 540 provides the California Independent System Operator (CAISO) the authority necessary to implement the Pathways Initiative Proposal *if* it determines an independent regional organization (RO) meets specific requirements. The bill allows CAISO to tap into a wider market of electricity resources which studies have shown stand to provide significant benefits to Californians including cost savings, enhanced grid reliability, and reduced air pollution.

While prior attempts to create a wider regional market have failed out of concerns that California would lose control over its environmental policies, SB 540 enables an innovative approach that would secure the gains of an expanded market while protecting California's ability to set and enforce its own procurement, environmental, reliability, and other public policies.

PROBLEM

For many years, California's energy regulators have explored how they could optimize available energy supplies across other western states to expand our energy markets and enable an affordable, clean, and reliable grid.

Studies have shown that there are significant benefits for California in an expanded energy market. For example, a Stanford Woods Institute (2024) study found that an expanded market would relieve strain on the electric grid during extreme heat events—in an expanded market scenario the grid was strained 40% fewer hours.¹ A study commissioned by the California Energy Commission (CEC) found that under an expanded market, California would save nearly \$800 million per year and gas generation would fall by 31%, moving us closer to our 100% clean

¹ [Stanford Woods Institute: "Grid Regionalization in the West"](#)

energy goals while reducing air pollution.² However, these benefits only materialize if other states want to join the regional market, a market they are wary of if it's solely under California's control.

Several different proposals, that would reassure other Western states of California's willingness to work jointly, have made their way before the Legislature. Most recently, AB 538 (Holden, 2023) would have transformed CAISO into a regional transmission organization (RTO). However, these previous efforts have failed over reasonable concerns about losing control of the state's critical public policies.

The Pathways Proposal offers a way to solve these problems. Instead of creating an RTO, the Pathways Proposal creates an RO that only governs the market rules for energy markets while retaining CAISO's role as a California-governed balancing authority so that California and CAISO retain control over procurement, environmental, reliability, and other public policies.

CURRENT LAW

Existing law enables CAISO to, and instructs how it will, manage the transmission grid and related energy markets. It requires, among other things, that CAISO manage those markets in a manner that maximizes efficiency, reduces costs to consumers, protects public health and the environment, and ensures reliability. However, additional authority is required in order for CAISO and California utilities to use energy markets overseen by an RO as proposed by the Pathways Initiative.

THIS BILL

SB 540 enables the CAISO and California utilities to participate in energy markets governed by a separate, independent regional

² [Brattle: "Preliminary Day-Ahead Market Impacts Study"](#)

organization. If the RO meets specific criteria, CAISO would be authorized to enact a resolution allowing the RO's rules to govern CAISO's energy markets. The CAISO would continue to be the operator of the energy markets.

SB 540 does *not* transfer authority for transmission planning, transmission cost allocation, balancing authority functions, or reliability coordination—this authority would remain with the existing CAISO board structure. The bill also does not immediately authorize utilities to enter a market governed by an RO, CAISO must first demonstrate the RO meets a number of statutory requirements before moving control of the market rules to the RO including: confirming that California regulatory agencies and CAISO retain control over Renewables Portfolio Standard requirements, climate policy, other procurement requirements, transmission planning, CAISO's interconnection queue, and resource adequacy requirements; requiring that the RO provides a procedure for withdrawal from the market, should it no longer benefit California to participate; maintaining the capability to operate its own market, should California decide to withdraw from the RO; ensuring the RO is obligated to make decisions in an open process; making funding available for consumer advocates to engage in the process, and more.

The expanded market that SB 540 would enable will save ratepayers money, improve grid reliability, and reduce air pollution from power plants in California by:

- 1) Optimizing the use of generation, storage and transmission resources.
- 2) Securing California's ability to export excess renewables rather than curtailing them and importing them from other states when available.
- 3) Allowing California to draw upon a wider set of Western renewable resources when our grid is stressed.
- 4) Making less use of back-up diesel generators and the oldest, dirtiest gas plants during system peaks.

SB 540 will ensure that we reach our climate goals in the most cost-effective and reliable manner possible by tapping into a much wider set of Western resources—lowering energy bills, improving grid reliability, and reducing pollution in front-line communities, while also retaining control of our procurement, environmental, reliability, and other public policies.

SUPPORT

Coalition of California Utility Employees (co-sponsor)
State Association of Electrical Workers (co-sponsor)
Environmental Defense Fund (co-sponsor)
Natural Resources Defense Council (co-sponsor)
American Clean Power—California
California Community Choice Association
California Environmental Voters
Clean Energy Buyers Association
Pattern Energy
Peninsula Clean Energy

FOR MORE INFORMATION

Erika Romero
Policy Analyst
Erika.Romero@sen.ca.gov