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April 17, 2009

By Hand

Kimberly D. Bose, Secretary
Federal Energy Regulatory Commission
888 First Street N.E.
Washington, D.C. 20426

**Re: New York Independent System Operator, Inc.'s Proposed Tariff Revisions to the
Credit Requirements for Virtual Transactions; Docket No. _____**

Dear Ms. Bose:

Pursuant to Section 205 of the Federal Power Act,¹ the New York Independent System Operator, Inc. ("NYISO"), by counsel, hereby submits revisions to Attachment W of its Open Access Transmission Tariff ("OATT") and to Attachment K of its Market Administration and Control Area Services Tariff ("Services Tariff") to better align the credit requirements for Virtual Transactions with market risk.² As stated in the December 5 Filing in Docket No. ER09-378-000, the NYISO is in the process of implementing an integrated credit management system ("CMS") that will allow the NYISO to automate many of the credit calculations and processes administered by the credit department.³ In conjunction with the implementation of CMS, the NYISO is reassessing the credit requirements for each of its markets to determine the extent to which the NYISO can use automation to enhance its credit analyses and fine-tune the credit requirements for each of its markets, as appropriate, to match market risk.

The NYISO automated the credit requirements for its TCC market with the deployment of CMS-Phase 1 in February.⁴ The NYISO now plans to automate the credit requirements for its Virtual Transaction market with the deployment of CMS-Phase 2 in June. The automation of the

¹ 16 U.S.C. § 824d (2008).

² Capitalized terms that are not otherwise defined herein shall have the meanings specified in Article 1.0 of the OATT and Article 2 of the Services Tariff.

³ See *New York Independent System Operator, Inc.'s Filing of Proposed Revisions to the Transmission Congestion Contract Creditworthiness Provisions*, Docket No. ER09-378-000 (Dec. 5, 2008) ("December 5 Filing") accepted by the Commission on January 7, 2009.

⁴ See December 5 Filing.



Kimberly D. Bose, Secretary
April 17, 2009
Page 2

credit requirements for Virtual Transactions will enable the NYISO to implement the credit enhancements proposed in this filing letter and described in detail in Section V below.

I. List of Documents Submitted

The NYISO submits the following documents:

1. This filing letter;
2. A clean version of the proposed revisions to the OATT and to the Services Tariff (Attachment I); and
3. A blacklined version of the proposed revisions to the OATT and to the Services Tariff (Attachment II).

II. Copies of Correspondence

Copies of correspondence concerning this filing should be served on:

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⁵ The NYISO respectfully requests waiver of 18 C.F.R. § 385.203(b)(3) (2008) to permit service on counsel for the NYISO in both Washington, D.C. and Richmond, VA.

Kimberly D. Bose, Secretary
April 17, 2009
Page 3

III. Service List

The NYISO will electronically send a link to this filing to the official representative of each of its customers, to each participant on its stakeholder committees, to the New York Public Service Commission, and the New Jersey Board of Public Utilities, and send a copy of this filing by first class mail to the Pennsylvania Public Utilities Commission. In addition, the complete filing will be posted on the NYISO's website at www.nyiso.com. The NYISO will also make a paper copy available to any interested party that requests one. To the extent necessary, the NYISO requests waiver of the requirements of Section 35.2(d) of the Commission's Regulations (18 C.F.R. § 35.2(d) (2008)) to permit it to provide service in this manner.

IV. Background

In connection with the planned implementation of CMS-Phase 2, the NYISO reassessed the appropriateness of its Virtual Transaction credit requirements by reviewing the riskiness of hypothetical virtual trading positions over the three year time period from April 1, 2005, through March 31, 2008.⁶ The NYISO based its analysis on publicly available Day-Ahead and Real-Time Market Energy price data. This analysis resulted in a number of key findings, including the following:

- the variability of virtual supply losses during peak hours was two to three times greater than for virtual load losses;
- there was considerably more variability in virtual supply losses versus virtual load losses during off-peak hours in the eastern zones, especially in Zones J and K;
- the variability of virtual load losses during peak hours was similar across zones;
- the differences between the dispersion of virtual supply losses and virtual load losses was most extreme during the summer months;
- the potential for virtual supply losses was greatest during peak hours during the summer months in the eastern zones; and

⁶ On February 1, 2005, the NYISO implemented the SMD2 (Standard Market Design) computer platform. The NYISO limited the scope of its analysis of the Virtual Transaction credit requirements to include only data from the SMD2 time period because software design changes and other factors affecting the determination of Energy prices in the Real-Time Market prior to the implementation of SMD2 could make price differential data from pre-SMD2 time periods less reliable as an indicator of prospective price dispersion.

Kimberly D. Bose, Secretary

April 17, 2009

Page 4

- the potential for virtual load losses was greatest during peak hours, during the summer months in Zones G–I and K, and during the winter months in Zones A–F.⁷

Under the NYISO's current Virtual Transaction credit requirements, a customer's credit requirement is calculated based on the highest amount of credit support required per MWh for any zone in which the customer is authorized to bid on Virtual Transactions, the number of MWhs of requested bidding authorization, and a multiplier of two. The NYISO establishes the amount of credit support required per MWh for a particular zone by calculating the price differential, at the 97th percentile,⁸ between the Energy prices in the Day-Ahead and Real-Time Markets, during the same two-month interval for each of the prior two years and selecting the higher of the two price differentials. While this methodology adjusts for seasonality it does not take into account the type of transaction (i.e., virtual supply or virtual load), the time-of-day, and other factors that the NYISO's recent analysis demonstrates could have a significant impact on a customer's risk of loss in the Virtual Transaction market. As a result, under the current credit requirements, the NYISO might over-collateralize for some Virtual Transaction positions (e.g., virtual load in the summer months) and under-collateralize for others (e.g., virtual supply during peak hours).

The analysis also revealed that not all differences in virtual trading positions are sufficient to justify distinct credit requirements. The results of the analysis led the NYISO and its stakeholders to conclude that the NYISO should revise its credit requirements for Virtual Transactions, as set forth in the proposed tariff sheets, to (i) distinguish between virtual load and virtual supply, (ii) group months with similar risk characteristics together, then take into account the differences in riskiness in the seasonal groupings, (iii) group zones with similar risk characteristics together, then take into account the differences in riskiness in the zonal groupings, and (iv) group times-of-day with similar risk characteristics together, then take into account the differences in riskiness in the time-of-day groupings.

If the credit enhancements proposed in this filing letter had been in effect in August 2008, then the credit requirements for virtual load transactions would have decreased in all hours, and the credit requirements for virtual supply transactions would have decreased in most hours. The credit requirements for virtual supply transactions would have increased substantially, however,

⁷ Additional materials regarding the Virtual Transaction analysis and recommendations are available at http://www.nyiso.com/public/committees/documents.jsp?com=bic_miwg.

⁸ In other words, the price differential calculated by the NYISO is greater than or equal to 97% of the price differentials observed during the relevant time period.

Kimberly D. Bose, Secretary

April 17, 2009

Page 5

for transactions during the weekday hours beginning (“HB”) 11:00 a.m. through 6:00 p.m., in particular in Zones F-K. Yet, the majority of the increase in the credit requirements for these virtual supply positions would have been offset by the decrease in the credit requirements for other virtual supply positions.

V. Description of Proposed Revisions

With this filing, the NYISO proposes to revise Section III.B.(v) of Attachment W to the OATT, and Section III.B.(v) of Attachment K to the Services Tariff,⁹ to replace the current procedure and methodology for determining the credit requirements for Virtual Transactions with a revised procedure and refined methodology that establishes credit requirements for Virtual Transactions that are better aligned with transaction risk. The refined methodology would continue to base the credit requirements on the price differential between Energy prices in the DAM and RTM, which methodology the Commission has previously found to be just and reasonable, but would identify more targeted price differentials based upon further differentiation of Virtual Transaction characteristics.

Under the proposed tariff revisions, the NYISO would determine the credit requirements for virtual supply and virtual load transactions separately. For each virtual supply bid, the amount of credit support required per MWh would equal the virtual supply price differential between the Energy prices in the DAM and RTM, at the 97th percentile, for the period of time from April 1, 2005, through the end of the prior calendar month, for the same season, zone, and time-of-day based upon the following groupings:

1. Seasons

Summer (May–Aug.)

Winter (Dec.–Feb.)

Rest-of-Year (March, April, and Sept.–Nov.)

2. Zones

A–F

G–I

J

K

⁹ The proposed revisions to the OATT and the Services Tariff are identical. As such, only one description is necessary to explain the revisions to both tariffs.



Kimberly D. Bose, Secretary

April 17, 2009

Page 6

3. Times-of-Day

Peak Hours (Monday–Friday)

HB 07:00–10:00

HB 11:00–14:00

HB 15:00–18:00

HB 19:00–22:00

Night Hours (All days)

HB 23:00–06:00

Weekend/Holiday Hours

HB 07:00–22:00

This methodology is designed to result in a 97% probability that the credit requirement for a virtual supply position would equal or exceed any payment due to the NYISO as a result of a loss on the Virtual Transaction.

For each virtual load bid, the amount of credit support required per MWh would equal the virtual load price differential between the Energy prices in the DAM and RTM, at the 97th percentile, for the period of time from April 1, 2005, through the end of the prior calendar month, for the same season, zone, and time-of day based upon the groupings indicated in the revised tariff sheets, which groupings are similar to the virtual supply groupings set forth above. This methodology is designed to result in a 97% probability that the credit requirement for a virtual load position would equal or exceed any payment due to the NYISO as a result of a loss on the Virtual Transaction.

On or about the third day of each month, CMS will automatically add the Energy price data from the prior month to the existing data set, and then recalculate and update the virtual supply and virtual load price differentials and the Virtual Transaction credit requirements. Once a Customer's Virtual Transaction bids for a given day are settled, based upon the difference between the Energy prices in the DAM and the RTM, then the Customer's credit requirement for those bids will default to zero; however, the Customer's total Virtual Transaction credit requirement will include the net amount owed to the NYISO for settled Virtual Transactions.

After the NYISO has accumulated six years of Energy price data, beginning with data from April 1, 2005, the NYISO will reevaluate the statistical validity of the proposed groupings, and determine the appropriate number of months of Energy price data to include in the price differential data sets for the purpose of recalculating and updating the price differentials.

Kimberly D. Bose, Secretary

April 17, 2009

Page 7

VI. Effective Date

The NYISO respectfully requests that this filing become effective on June 17, 2009, which date is the targeted deployment date for CMS-Phase 2. In the event the deployment date for CMS-Phase 2 is delayed, the NYISO also respectfully requests permission to delay the effective date of the proposed tariff revisions, by up to 45 days, upon the filing of a notice and amended tariff sheets with the Commission by June 17, 2009 that indicate the revised effective date.

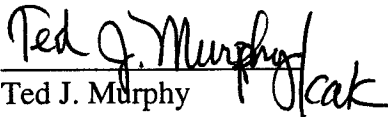
VII. Requisite Stakeholder Approval

The tariff revisions proposed in this filing are the product of extensive analysis and discussion with the NYISO's Market Issues Working Group. The NYISO's Business Issues Committee unanimously approved these revisions by a show of hands at its meeting on October 22, 2008, and the NYISO's Management Committee also unanimously approved these revisions by a show of hands at its meeting on October 29, 2008. On November 17, 2008, the NYISO's Board of Directors approved a motion directing the NYISO to file the proposed tariff revisions approved by the Management Committee.

VIII. Conclusion

WHEREFORE, for the foregoing reasons, the New York Independent System Operator, Inc. respectfully requests that the Commission accept the proposed tariff changes identified in this filing.

Respectfully submitted,


Ted J. Murphy

Counsel for

New York Independent System Operator, Inc.

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