MOTION OF MULTIPLE INTERVENORS, THE CITY OF JAMESTOWN BOARD OF PUBLIC UTILITIES AND THE NEW YORK STATE CONSUMER PROTECTION BOARD IN OPPOSITION TO APPEAL OF LONG ISLAND POWER AUTHORITY AND LIPA OF MANAGEMENT COMMITTEE'S ACTIONS ON A WORKING CAPITAL AND BAD DEBT LOSSES ALLOCATION METHODOLOGY

Multiple Intervenors, the City of Jamestown Board of Public Utilities and the New York State Consumer Protection Board (collectively "Joint Movants") urge the Board of Directors to reject the extraordinary relief requested by the Long Island Power Authority and LIPA ("LIPA"), in LIPA's March 6, 2003 Appeal ("LIPA's Appeal"), to revert to a methodology that allocates 100% of bad debt losses and working capital contributions to loads. The Board of Directors should deny LIPA's appeal of the Management Committee's February 20, 2003 decision to finally approve, after over two years of effort, a new comprehensive Financial Assurance Policy (Motion No. 3), including: (1) Credit Requirements, (2) a Bad Debt Loss Allocation Methodology, and (3) a Working Capital Contribution Allocation Methodology. Further, the Board should reject LIPA's attempt to substitute its preferred methodology for the Bad Debt Loss and Working Capital Contribution allocation, which was rejected by the Management Committee.

Joint Movants request that the Board of Directors direct the NYISO Staff to amend the currently pending Section 206 submittal at the Federal Energy Regulatory Commission ("FERC") of only the Credit Requirements component of the Financial Assurance Policy and convert it into a Section 205 filing of the three-part comprehensive Financial Assurance Policy.

I. BACKGROUND

On June 13, 2002, the Management Committee approved, with over 80 percent of the vote, a compromise package that included the framework of a new Credit Requirements policy and a specific formula for allocating bad debt losses incurred by the NYISO, along with the other elements not at issue here. The bad debt loss formula uses a customer's total dollar volume of transactions (other than virtual transactions) to allocate bad debt losses declared by the NYISO. The Management Committee directed that detailed Credit Requirements be developed by the Credit Policy Working Group, according to the framework approved by the Committee, and that the package be returned for final Committee approval.

In the fall of 2002, the Credit Policy Working Group returned with the new comprehensive Financial Assurance Policy, including: (1) a detailed Credit Requirements policy, (2) a Bad Debt Loss Allocation Methodology which utilizes the bad debt losses formula approved in the June 13 decision, and (3) a Working Capital Contribution Allocation Methodology that utilizes the same formula. The new comprehensive Financial Assurance Policy had the support of the NYISO staff.

In the fall, other methods for allocating bad debt losses were discussed at meetings of the Scheduling and Pricing Working Group. These methods generally used a MWH allocation (instead of dollar volume), and applied a ratio of the parties' share of the total MWH injected into the grid and withdrawn from the grid (in other words, both methods allocate credit risk to generators as well as loads). However, these proposals did not gather a consensus in the Scheduling and Pricing Working Group, and the Credit

Policy Working Group expressly declared its preference for the original dollar volume allocation methodology.

The comprehensive Financial Assurance Policy was approved at the December 13, 2002 Business Issues Committee meeting, with an affirmative vote in excess of 60 percent. A special meeting of the Management Committee, held by conference call, was convened on December 16, 2002. At that meeting, the comprehensive Financial Assurance Policy failed, with "only" 57.09 percent of the affirmative vote.

At the January, 2003 Liaison Committee meeting, representatives of the Board announced the Board's intention to file at FERC only the Credit Requirements component of the Financial Assurance Policy as a Section 206 filing. The Board representatives stated that they had rejected a request to defer action until after the February 20, 2003 Management Committee meeting, when there would be a re-vote of the comprehensive Financial Assurance Policy. However, they also urged the parties to reach a consensus at that meeting, and stated their intention to convert the Section 206 filing into a Section 205 filing if a consensus was reached.

At the February 20, 2003 Management Committee meeting, the three-part comprehensive Financial Assurance Policy (Motion #3), using the original dollar volume allocation methodology, was approved with over 60 percent of the affirmative vote. At the same meeting, a motion to amend sponsored by LIPA (Motion #3a), substituting a complicated MWH method for allocating bad debt losses, was defeated while receiving only 30 percent of the affirmative vote.

Therefore, since consensus was reached at the February 20 meeting, Joint Movants respectfully request that the Board reject the LIPA appeal in its entirety and

expeditiously file to convert the pending Section 206 submittal of the Credit Requirements policy into a Section 205 filing of the comprehensive Financial Assurance Policy.

II. ADOPTION OF LIPA's BAD DEBT LOSS ALLOCATION METHOD WOULD NOT BE FAIR TO LOADS

LIPA's primary relief requested in its Appeal is the extraordinary request that the allocation methodology for bad debt losses and working capital contributions should be performed on a load ratio share charged on a MWH basis, assessed only to loads (LIPA Appeal at 2). LIPA states that this is the current allocation methodology. However, under the interim policy adopted by the FERC, [1] bad debt losses are collected pursuant to Rate Schedule 1. Since June 1, 2002, Rate Schedule 1 charges are to be allocated 85/15 to loads and generators. What LIPA in fact seeks is a return to the former 100% allocation of bad debt losses and working capital contributions to loads. LIPA's request is untimely and manifestly unfair to loads.

While LIPA may have a vested self-interest in attempting to reinstate a methodology whereby the risk of bad debt losses is assessed solely to loads, no serious proposal to do so has been discussed at any working group or committee level since work on the new credit policy began over two years ago. For LIPA now to advocate a return to this approach that allocates all the risk for bad debt losses and working capital contributions to consumers, including LIPA's own customers, is untimely and unsupportable.

LIPA's request is the latest in a series of attempts to undermine the June 13 Management Committee decision. LIPA, and others, would like to have the new Credit

Requirements imposed on certain market participants, while other market participants escape any new obligations under the Bad Debt Loss and Working Capital Allocation Methodology approved as part of the package. However, LIPA's proposal is manifestly unfair to loads.

LIPA argues that the NYISO should reinstate an allocation methodology which allocates 100% of the risk of bad debt losses and working capital contributions to loads because it "allocates costs to the ultimate beneficiaries of the market stability created" (LIPA at 2). The NYISO's coverage of bad debt losses and maintaining working capital requirements ensures that generators and other suppliers will be paid. Therefore, to argue that loads are the sole beneficiaries of the NYISO's bad debt and working capital policies is preposterous. To the contrary, a good argument could be made that working capital contributions and bad debt loss allocations should be attributed 100 percent to generators, since these mechanisms function as insurance that the generators will be paid by the NYISO. In light of the conflicting perspectives, in the Comprehensive Financial Assurance Policy, the market participants achieved consensus on the dollar volume methodology that allocates the costs on a 50/50 basis. This consensus should be upheld by the Board.

Furthermore, LIPA's request is inconsistent with FERC's January Order approving the Interim Bad Debt Loss Policy. FERC approved the policy on an interim basis, over the objections of load serving entities, on the basis that the interim policy was only a stopgap until the comprehensive Financial Assurance Policy could be filed. Thus, adopting LIPA's position would not be consistent with the FERC's expectations.

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[1] Docket No. ER03-180-000 - New York Independent System Operator, Inc., 102 FERC ¶ 61,021, Order Conditionally Accepting Tariff Revisions, issued January 10, 2003.

III. LIPA's ALTERNATIVE APPEAL TO SUBSTITUTE MOTION 3a FOR MOTION 3 MUST ALSO BE DENIED, SINCE THE MANAGEMENT COMMITTEE CORRECTLY CONSIDERED AND REJECTED LIPA's ARGUMENTS

In achieving a consensus on Motion 3, and approving, at long last, a comprehensive Financial Assurance Policy, the Management Committee considered and correctly rejected LIPA's arguments in support of a MWH allocation methodology when it approved Motion 3, and rejected Motion 3a, at the February 20th meeting.[2] First, the dollar volume allocation methodology correctly aligns the volume of a party's transactions with the NYISO with its credit risk and with the bad debt loss exposure as compared to other market participants. On the other hand, the MWH allocation methodology distorts the bad debt loss exposure of market participants, because it ignores the true measure of that risk.

Further, LIPA's request that it be allowed to 'net' its purchases with its sales was carefully considered by the Credit Policy Working Group. The netting approach was not accepted because, using LIPA's own numbers, LIPA would bear a share of a bad debt loss of less than two tenths of a percent, while its volume of transactions was 16 percent. Other market participants would be subsidizing LIPA.

In addition, the dollar volume approach does not discriminate against parties to bilateral transactions. LIPA has it backwards on the bias between bilateral and LBMP transactions. Parties to bilateral transactions already bear the costs of credit risk within their bilateral transactions. The dollar volume allocation correctly reflects that the only credit exposure of the NYISO to bilateral transactions is for Rate Schedule 1 and other

[2] LIPA makes several factual allegations, *e.g.*, on page 3 of its appeal, that are accepted here only for the sake of argument. Despite opportunities at numerous working group meetings, LIPA declined to discuss the specifics of its situation, and it failed to substantiate its factual allegations.

ancillary services (since the credit risk of the energy is covered by bilateral contract). The MWH allocation method inappropriately allocates the costs of credit risk for the NYISO spot market energy transactions to parties that are not participating in the market and have already covered their exposure in their bilateral contracts. Thus, contrary to LIPA's assertion, the MWH allocation does ***not*** "remove the bias towards bilateral transactions," it creates the bias against bilateral transactions.[3]

Finally, the Board of Directors should recognize the recommendation of the Credit Policy Working Group, which was that the pooled approach to credit risk offered by the NYISO LBMP markets is a tremendous advantage over bilateral transactions, since the risk is spread over many diverse parties. For a party to threaten to pull out of the LBMP market because it claims to fear bad debt losses, ignores the advantages it receives by participating in the pooled market. LIPA has not demonstrated, either in its appeal or in the working group process, that the risks of costs outweighs the benefits of participation in the LBMP market.

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[3] *See* LIPA Appeal at 8 ("both bilaterals and transactions that participate in the NYISO market would be treated equally.") This is in error because the bilateral has already covered its energy risk in the bilateral contract. The MWH allocation is not just and reasonable in using bilateral transactions to subsidize the NYISO markets.

IV. CONCLUSION

For the above reasons, Joint Movants urge the Board of Directors to deny LIPA's appeals and request that the NYISO expeditiously convert its Section 206 submittal of the Credit Requirements into a Section 205 filing of the comprehensive Financial Assurance Policy.

Respectfully submitted,

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