

**NYISO MARKETS**

**CREDIT ISSUES AND WORKING CAPITAL REQUIREMENTS**

**After a year of operations, and in light of recent events, it is time for the NYISO to reevaluate its credit and working capital policies.**

In order to maintain the liquidity, integrity and confidence in the New York markets, the NYISO must have a clear and comprehensive credit and collections program that also includes contingency cash planning in the event of default or non-payment by a market participant. The basis of the NYISO program is analagous to a four legged stool: (1) effective collection and market participant credit policies, including appropriate levels of market participant collateral, (2) credit insurance, (3) working capital and (4) bank relationships. Each of these legs is essential to a maintaining a strong, balanced, and liquid market. Following is a brief description of each leg and the related issues that need to be reviewed:

**Collection Policies:** These policies should be enforced consistent with the language of both the Open Access Transmission and Market Services Tariffs.

**Action:** NYISO staff is requesting Management Committee support for the proposal, included in the attached presentation, related to the expeditious recovery of late and/or default payments through Rate Schedule 1.

**Creditworthiness Policies:** The tariff prescribes the creditworthiness criteria that an applicant must meet in order to participate in the NYISO market. If the prescribed corporate debt ratings and/or payment history criteria are not met, then the applicant must provide credit support in the form of cash, a letter of credit, a parental guarantee or a surety bond in order to participate in the market.

The recent willful payment withholding by NYSEG has highlighted an inherent weakness in the creditworthiness criteria prescribed in the tariff. This weakness must be reevaluated. Approximately 10% of the market participants representing 90% of the dollar volume transacted each month (approximately \$350 million) are not required to provide any specific credit support. Additionally, other than instituting termination proceedings at FERC (a process that may not be practical) the NYISO has no direct recourse to a delinquent market participant that provides no credit support nor does the NYISO have the authority to impose specific sanctions or penalties.

As suggested by the Management Committee at its December meeting, NYISO staff will work with the BSPS Committee to develop appropriate revisions to the creditworthiness criteria in the tariff.

**Credit Insurance:** In the event of a financial default on the part of a market participant who has not been required to provide credit support, the other market participants will bear the financial burden of paying the suppliers in-full through a surcharge to Rate Schedule One. This exposure can be greater than \$100 million for a default by the single largest market participant in any given month. The Management Committee concurred with NYISO staff's recommendation to procure \$50 million of credit insurance, and this insurance has been procured with an effective date of January 1, 2001.

\$50 million is the total annual insurance proceeds payable by the insurance carrier. In light of average monthly receivables on the order of \$350million (almost \$5 billion annually) the NYISO staff will be reviewing, with the BSPS Committee, the appropriateness of increasing this level of coverage. The issue to be addressed is "how much risk is appropriate and how much is the market willing to self-insure"

**Working Capital and Banking Relationships:** Working capital and banking relationships go hand-in-hand with respect to providing short-term contingency support for the market. Short-term contingency support means being able to sustain paying the market in-full for a month or two while attempting to resolve the inevitable payment issues that will arise in a \$5 billion dollar annual market. The liquidity, integrity and confidence in the New York markets can be best served by paying the market's suppliers on-time and in-full each month. To date, the NYISO has a perfect record in this regard; a record made possible through the prudent use of accumulated working capital and the revolving credit facility. Without these two facilities, the NYISO would not have been able to achieve its perfect payment history.

Currently, the NYISO has accumulated approximately \$5 million of working capital and has a \$50 million revolving credit agreement with its banks. Although both of these agreements ostensibly provide immediate access to the indicated levels of cash, the only truly unrestricted cash is the working capital fund.

The immediate question to be answered is how much total contingency funding is appropriate. NYISO staff's position is that the establishment of a \$100 million dollar contingency fund to be provided by accumulating \$50 million of working capital combined with the \$50 million revolving credit facility, would be appropriate. This level would be sufficient to cover one month of the average receivable of any given market participant in 2000, with the exception of the single largest market participant.

**Action:** NYISO staff is requesting Management Committee support for a proposal to this effect; see the attached presentation for the specific proposal.

*Richardson*

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- FRONT SECTION
- MARKETPLACE
- MONEY & INVESTING
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- SPORTS
- PERSONAL JOURNAL
  - NEWS
  - FAVORITES
  - PORTFOLIO



December 14, 2000

# California Electricity Deregulation Is in Chaos; Energy Secretary Steps In

By **REBECCA SMITH**  
Staff Reporter of THE WALL STREET JOURNAL

California's four-year-old experiment in electricity deregulation lurched from crisis to chaos as a group of generators demanded extraordinary credit guarantees in order to continue selling power and the state's No. 2 utility demanded an immediate return to traditional regulation.

The moves -- and the threat of blackouts throughout the world's sixth-largest economy -- prompted Energy Secretary Bill Richardson to invoke an emergency federal provision to force generators to stay in the market. "Our objective is to keep the lights on," he said, adding that he would "not allow generators to unjustly profit from the unstable situation."

Mr. Richardson's intervention comes as wholesale electricity prices in the Western U.S. have soared to record levels as a result of booming demand, chronic supply shortages and a spike in the price of natural gas, used by most generators to power their plants. The high wholesale prices, in turn, are threatening the solvency of California utilities that must buy most of their power from outside generators and currently aren't allowed to pass along higher prices to consumers.

The troubling state of affairs in California, and the clear difficulty regulators and lawmakers are facing in coming up with a politically palatable solution to the crisis, is likely to cast a pall on electricity deregulation initiatives across the U.S. Currently, 24 states have either deregulated their markets or are in the process of doing so.

The situation Wednesday came to a head during a Washington meeting attended by California Gov. Gray Davis, U.S. Sen. Dianne Feinstein, Federal Energy Regulatory Commission Chairman Jim Hoecker and Mr. Richardson. As they debated how to fix California's

**▶ Energy Price Volatility May Hurt Utilities' Credit (Dec. 13)**


In this Section:  
World-Wide

- Asia
- Europe
- The Americas
- Economy
- Earnings Focus
- Politics & Policy

Editorial Page  
Leisure & Arts  
Voices

Weekend Journal

WSJ.com Audio:  
Business Update  
Markets Recap  
WSJ on Audible  
Learn More

Journal Atlas:  
Table of Contents  
Headlines  
Business Index  
Search   
News Search  
Past Editions  
Briefing Books  
Quotes

Resources:

Article  
Quote  
Compa

Join the  
Gerald S  
discussi  
aftermat  
presider  
Thursda

Sp  
▶ Amer  
The Wa  
Journal/  
finds m  
support  
overhau  
procedu

GET  
TE  
E-M  
▶ sign

Ad

D  
&

Social A  
Pri

- [Help](#)
- [New Features](#)
- [E-mail Center](#)
- [Your Account](#)
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...RICHARDSON AND MR. FEINSTEIN. AS THEY DEBATED HOW TO FIX CALIFORNIA'S broken market, they were notified by officials from the grid-operating California Independent System Operator, or ISO, they would have to begin rolling blackouts for the first time and faced an apparent mutiny by 13 generators and traders. Soon after, Mr. Richardson asserted his emergency powers under the Federal Power Act to make sure suppliers don't abandon the market.

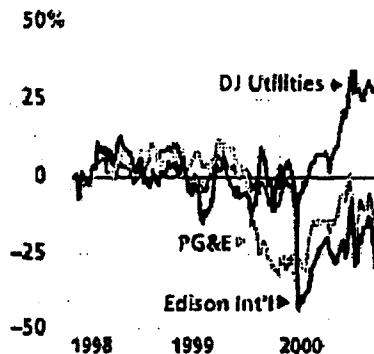
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While Mr. Richardson's move buys some time, it didn't address the underlying financial problem that threatens to engulf not only the utilities but, eventually, consumers throughout the West. California's three investor-owned utilities, which supply power to customers at frozen rates ranging between \$54 and \$65 per megawatt hour, are paying as much as \$1,200 per megawatt hour for their juice.

Since June, they have amassed a deficit of more than \$7 billion. Prior to deregulation, California spent \$23 billion a year on electricity. Recently, it has been spending as much as \$850 million a day.

**ELECTRIC SHOCK**

Percent change since Dec. 26, 1997, in weekly closes of the Dow Jones U.S. Utilities Index and Edison International and PG&E.



Sources: [TradeLine.com](#); [Dow Jones Indexes](#)

Over the course of the last week, the credit ratings of both Southern California Edison and Pacific Gas & Electric Co., the state's other big utility, have been cut. Wednesday, Standard & Poor's joined in the chorus, putting the two utilities on negative credit watch.

To keep the situation from getting any further out of control, Mr. Davis and Ms. Feinstein Wednesday called on the FERC to impose a low, uniform price cap on what generators can charge throughout the region. They also want the commission to order

generators to enter into long-term contracts with the state's utilities at reasonable price levels.

John Bryson, chairman of [Edison International](#), parent of California's second-largest utility, wants to go further than that. "The new market structure is broken and must be discarded," he said.

Mr. Bryson, formerly a leading proponent of deregulation, said the utility would "soon be compelled to take drastic measures" to serve its customers, including rationing. "It is time to break decisively from this failed policy," he added. "We need to reform, and, where necessary, reregulate California's electrical system."

In an interview, Mr. Bryson said Edison has in recent days faced

difficulty in securing a \$1 billion credit line from a consortium led by Chase Manhattan Bank owing to fears that it will never get paid. "There's no question we need this money," Mr. Bryson said. "It is a serious credit crunch."

Indeed, generators say they are worried that the financial drain on the utilities is nudging them toward default. One of them, though, says that as a group they have never threatened to cut off supplies.

"All we said was, you either need to give us a letter of credit, or the state needs to step forward," said Steve Bergstrom, president of Dynegy Inc. of Houston, operator of 16% of California's fossil-fuel generating capacity. "All the governor has to do is prove he's not going to let the utilities go under, that's he's going to allow them to pass along their costs to consumers."

That's clearly the rub. Mr. Davis and Ms. Feinstein, neither of them eager to foist the enormous cost of the troubled deregulation policy on consumers, Wednesday accused the generators of price gouging.

The governor even went so far as to release a list of 13 generating companies, including Dynegy and power giant Enron Corp., that "are unwilling to sell power into the California markets." Mr. Davis added that he hoped Mr. Richardson's emergency actions would "stop market abuses" and bring temporary relief.

Write to Rebecca Smith at [rebecca.smith@wsj.com](mailto:rebecca.smith@wsj.com)

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**Introducing**

[Return to top of page](#) | [Format for printing](#)

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## **NYISO Markets**

**Credit Issues and Working Capital  
Requirements**

**The New York Markets After One Year**

**\$5 Billion!**



## Credit Issues and Working Capital Requirements

### ➤ Issue:

- *Maintaining Market Liquidity*
- *Integrity*
- *Confidence*

### ➤ Objective:

- *Pay the Market on-time and in-full*
- *To date, the NYISO has a Perfect Record*

### ➤ Concerns:

- *NYSEG withholding*
- *Late payments by others*

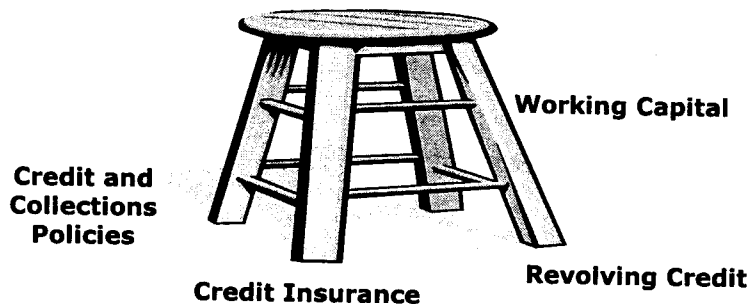
### ➤ Resolution:

- *Appropriate Credit and Collections Policies*
- *Contingency Planning - Working Capital/Bank Relations*



## Liquidity of the NYISO Markets

### Four-Legged Stool



**It's Time for a Comprehensive Review**  
**One Year of History**

➤ **Leg One**

- *Credit Policy*
- *BSPS Committee*
- *Collection Policy*
- *Staff Proposal Today*

➤ **Leg Two**

- *Credit Insurance*
- *BSPS Committee*

➤ **Leg Three**

- *Revolving Credit Line*
- *\$50 Million/ expires  
October 2005*

➤ **Leg Four**

- *Working Capital*
- *Staff Proposal Today*



**NYISO must have a Firm and Consistent Policy for**  
**Dealing with Late Payments and/or Defaults**

- **Tariff provides for recovery of late payments and defaults through Rate Schedule One.**
- **Banks have extended unsecured revolving credit line on basis of above tariff provision.**
- **NYISO must maintain Bank's confidence in ability to enforce Tariff.**
- **NYISO's Market Participants must honor their obligations.**
- **NYISO must enforce the Tariff consistently and diligently.**



## The NYISO must have a Firm and Consistent Policy for dealing with Late Payments and/or Defaults

### Proposal:

The Management Committee accepts the NYISO staff position to recommend to the NYISO Board that late payments and/or defaults will be expeditiously recovered through Rate Schedule One. In the event of a late payment or default, the NYISO staff will immediately notify the Market Participant of its payment obligations under the Tariff, and request that the Market Participant forward the payment due immediately. If deemed appropriate by the NYISO staff, the Market Participant will be declared in default and a notice will be filed with FERC, in accordance with the provisions of the Tariff. Any late payments or defaults which are not paid before the next Market Billing Date (generally 30 days) will be recovered through Rate Schedule One as deemed appropriate by NYISO staff. The NYISO will post, as promptly as possible, the name of the entity and amount of the late payment or default, and the associated impact on Rate Schedule One. It is further resolved that the NYISO staff will work with the BSPS Committee to determine an appropriate sanction to be applied to late payments and defaults, and to make the requisite filing with FERC to revise the Tariff accordingly.



## Working Capital Proposal.

### Proposal:

The Management Committee accepts the NYISO staff's position to recommend to the NYISO Board accumulation and maintenance a Working Capital Fund of approximately \$50 million. The \$50 million will be gradually accumulated, throughout 2001, by adding approximately \$.40 per megawatt-hour to the monthly Rate Schedule One charge beginning in February 2001. This \$.40 per megawatt-hour, when added to the \$.60 per megawatt-hour necessary to fund the NYISO's 2001 operating budget of \$101.8 million, will bring the targeted Rate Schedule One charge for 2001 to \$1.00 per megawatt-hour. NYISO staff will make every effort to stabilize the Rate Schedule One charge at \$1.00 per megawatt-hour in 2001, through the use of accumulated working capital and the available revolving credit line.

