

Bilateral Netting

Concept of Operation

MIWG 6/25/07

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Business Case - Background

- Definition: “Bilateral Netting” makes use of new bilateral transaction features whereby energy may be sourced from internal locations other than a generation source and delivered (sunked) at an internal zonal hub. Transactions may then be sourced at the zonal hub to deliver the same energy or portions thereof to other delivery points or to the same zonal hub but to a different MP effectively transferring title and financial responsibility for the energy to that counterparty.

Business Case - Background

- Proposed several years ago
- Failed to gain traction through the governance process
- FERC action resulted in a 2006 order to proceed with COO development

Business Case - Background

- **FERC compliance:** the results of a dispute resolution process requires the NYISO to develop the COO for a Bilateral Netting function for possible implementation if approved and funded by the NYISO through the governance process. The agreed upon schedule of activity is:
- March 2007 – Begin meeting with potential users, initial draft COO ready for review and discussion
- May 31 2007 – Draft COO complete with input from selected users
- June 2007 – Present COO to MIWG for review and comment
- June – November Present final COO to BIC, BPWG, MC, BOD for funding and, if funded, scheduling of implementation.

Business Case – Concept overview

- The current NYISO market model requires one to source any internal bilateral transaction at a physical energy source (generator bus requiring the approval of the generator owner/operator) and sink any such transaction at a designated zonal sink.

Business Case – Concept overview

- The requested function requires the addition of the Bilateral Netting feature which allows energy to be delivered from locations other than a generation source bus and to be delivered to a zonal hub (a virtual trading location).
- Transactions may then be sourced at the hub to deliver energy to other delivery points or to the same delivery point but to a different MP effectively transferring title and financial responsibility for the energy to that counterparty

Business Case – Concept overview

- The concept presented here is to expand the NYISO's current concept of virtual trading buses assigned to MPs qualified to conduct virtual trading and allow qualified MPs to sink and source internal bilateral transactions at designated virtual bilateral trading locations where the responsible MP will balance its net transaction positions at the spot price of the applicable market (DAM or RT).

Business Case – Business Impact

- Bilateral Netting applies only to **internal** bilateral transactions and has no affect on external transaction management.
- Bilateral Netting will be applicable to both the DAM and the RTM. Each transaction will settle in the market in which it is scheduled.

Business Case – Business Impact

- Settlement and MIS software will be the major subsystems impacted by the netting function. Design will likely utilize an enhanced version of the virtual trading models.
- A third area to be impacted will be credit monitoring and the interface between credit and settlements subsystems.
- All aspects of this function should be automated at initial implementation. The NYISO cannot support early implementation through manual processes as they would be required in scheduling, settlements, dispatch operations, and credit tracking.

Business Case – Risk/Cost

- MIS and Settlements design and development are expected to extend current bilateral transaction scheduling functionality.
- Automated credit monitoring will be required. Existing credit rule modifications and guidelines to accommodate this new function will also need to be developed. MM5
- Implementation cost estimate – TBD

Business Case – Benefit

- Netting is intended to facilitate trading by providing additional flexibility for marketers and LSEs in carrying out their physical trades.
- Netting may support a means whereby retailers or small LSEs could make better use of the creditworthiness of larger marketing institutions.

Business Case – Benefit

- This function is consistent with the PSC and FERC emphasis on support for development and expansion of retail choice.
- This functional concept development was ordered by FERC as a potential means to reduce the cost of credit in the NYISO that they feel may represent a barrier to entry of smaller LSEs.

Software Functions Required

- Modification of **virtual bus models to allow the netting of an energy position at a Virtual Netting Location** for a given market for each hour for each qualified participating MP.
 - Sell Mw from sink designated transactions into the respective market at LBMP for that location (Zonal Energy Price) and buy Mw for source designated transactions at LBMP for that location (Zonal LBMP).
 - NYISO Bilateral Netting transactions will be conducted in Mw increments as are all other energy transaction bids and offers.

Software Functions Required

- Modification (as needed) to **bid formats, upload download software, and other MIS processing** software to accommodate:
 - Sourcing internal bilateral transactions at a virtual netting location in addition to a generator bus.
 - Sinking internal bilateral transactions at a virtual netting location in addition to a current zonal sink bus.
 - Modification to SCUC data input and output processing to maintain tracking of the above changes for transactions present at DAM and RT market closing time.
 - Bilateral netting may or may not require changes to the contract definitions.

Software Functions Required

- Modification to **settlement software** to properly account for transaction activity at the virtual netting locations
- Development of an **interface between settlements and credit analysis software** to provide appropriate data needed to support credit tracking software functions specific to Bilateral Netting.
- Development of **credit tracking functions consistent with credit requirements** to be established for MPs qualified to participate in Bilateral Netting.

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User Characteristics (ISO internal)

- **Credit Management:** Monitoring and managing the credit exposure of MPs. Specifically: changes in individual Customer exposure resulting from transfers of financial responsibility, sales, and purchases of spot energy at virtual netting locations.
- **Customer Settlements:** Responsible for ensuring that accurate settlement information is produced and issued to the market. Specifically: incorporation of new settlement rules associated with incorporation of trading at virtual netting locations.
- **MIS product management :** Responsible for upload download software will need to support MP user testing of new protocol features for qualified MP Bilateral Netting users.

User Characteristics (ISO internal)

- **Data Warehouse:** Changes and additions will be required to support the storage and access to data associated with the bilateral netting function

User Characteristics (external)

- **Marketers and traders:**
 - These users will utilize the additional flexibility to physically carry out forward contracts for energy as well as to clear forward positions in the DAM and RTM.
 - The additional flexibility provided by this function will make it possible for larger marketers to more efficiently package deals including transmission and credit costs.
- **LSEs:**
 - this feature can simplify the task of acquiring supply contracts and in some cases may reduce the overall cost of doing business in the NYISO for retailers.

Next Steps

- Feedback from Market Participants on the concept:
 - potential benefit
 - questions
 - clarifications needed and
 - recommendations.
- ISO staff to develop a cost model based on the concept presented and will integrate feedback into the model.