

November 30, 2004

The Honorable Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, NE
Washington, DC 20426

New York Independent System Operator, Inc.'s
Report in Docket Nos. ER03-552-000 and ER03-984-000 et al.
Regarding NYISO Settlement and Customer Credit Policies

Dear Ms. Salas,

In its September 22, 2003, *Order Conditionally Accepting Tariff Revisions*¹ (“September 22 Order”), the Commission conditionally accepted revisions to the New York Independent System Operator, Inc.’s (“NYISO’s”) Open Access Transmission Tariff (“OATT”) and Market Administration and Control Area Services Tariff (“Services Tariff”) regarding customer credit requirements. In the September 22 Order, the Commission directed the NYISO to explore through its stakeholder process whether further changes to the NYISO’s settlement or credit procedures should be made and either to submit a report on the results of that stakeholder process or to file revised tariff provisions within 180 days of the September 22 Order.² The NYISO submitted a report as required by the Commission on March 29, 2004³ (“March 29 Report”). In its June 2, 2004, *Order Conditionally Accepting Compliance Filings*⁴ (“June 2 Order”), the Commission accepted the March 29 Report, but ordered the NYISO to submit within 180 days of the June 2 Order a subsequent status report on its work with stakeholders to consider the NYISO’s creditworthiness standards and settlement policies. The NYISO respectfully submits this report as directed by the Commission in the June 2 Order.

The NYISO continues to believe that its overall approach to addressing customer credit risk is sound and that its policies appropriately protect the NYISO and its customers against credit risk without creating undue barriers to entry into the markets it administers. However, the NYISO remains committed to exploring ways to further refine and improve its policies to minimize the burden of those requirements on customers while still appropriately protecting the market from financial losses. Accordingly, the NYISO continues to work with stakeholders to

¹ 104 FERC ¶ 61,311 (Sept. 22, 2003).

² *Id.*

³ *New York Independent System Operator, Inc.’s Report in Docket Nos. ER03-552-000 and ER03-984-000 et al. Regarding Potential Settlement and Customer Credit Enhancements* (March 29, 2004).

⁴ 107 FERC ¶ 51,243 (June 2, 2004).

examine possible means by which the NYISO's settlement systems and customer credit requirements can be better tailored to balance the credit risk faced by the NYISO and its customers against the credit requirements imposed on its customers. Furthermore, the NYISO has begun examining its credit and settlement policies in light of the Commission's November 18, 2004, policy statement encouraging ISOs to examine and revise their credit and settlement policies.⁵

This report outlines the NYISO's activities since the issuance of the June 2 Order to: (i) engage stakeholders regarding credit issues, (ii) continue pursuing the implementation of policies previously reported in the March 29 Report, and (iii) examine new methods to further enhance NYISO credit and settlement policies.

A. Involvement of Stakeholders

In response to the June 2 Order requiring the NYISO to fully use its stakeholder process to examine creditworthiness issues, the NYISO has worked diligently to engage its stakeholders as described more fully below. Toward that end and since the March 29 Report, the NYISO has utilized its governance process to meet with stakeholders on five occasions to discuss creditworthiness issues and solicit stakeholder input with regard to possible additional enhancements to the NYISO's credit requirements.⁶

B. Progress on Items Reported in March 29 Report

1. Enhanced Settlement System. In the March 29 Report, the NYISO reported that it had hired an outside consultant to examine means by which the NYISO might shorten its settlement system so as to reduce the amount of collateral necessary to protect the NYISO from the risk of default by a market participant. Since that time, the NYISO's consultant has provided the NYISO with a report on its findings. The NYISO has released this report to its stakeholders⁷ and actively sought feedback from them. This matter is currently being reviewed by a stakeholder working group, namely the Billing and Accounting Working Group ("BAWG"). The BAWG has developed a list of action items and goals that Market Participants agree must be accomplished as a prerequisite to shortening the settlement cycle. The action items and goals relate to the improvement of settlement system accuracy. The NYISO is currently working with stakeholders to accomplish these action items and goals.

⁵ Policy Statement on Credit-Related Issues for Electric OATT Transmission Providers, Independent System Operators and Regional Transmission Organizations, 109 FERC ¶ 61,186 (November 19, 2004).

⁶ The dates of these meetings are as follows: (i) the June 9 meeting of the Credit Policy Task Force; (ii) the June 17 meeting of the Credit Policy Task Force; (iii) the July 8 meeting of the Credit Policy Task Force; (iv) the October 18 meeting of the Scheduling and Pricing Working Group; and (v) the November 23 meeting of the Scheduling and Pricing Working Group.

⁷ A copy of this report is available at http://mdex.nyiso.com/publish/Document/1e5d61_ffdb9d0b55_-7f420a03015d?action=download&_property=Attachment

Though the NYISO has not yet shortened the settlement cycle applicable to customers generally, the NYISO has successfully implemented a weekly prepayment program that allows a market participant to effectively shorten its settlement cycle by entering into a prepayment agreement with the NYISO, as approved by the Commission in the June 2 Order. By entering into a prepayment agreement, a NYISO customer agrees to prepay for its expected purchases in the energy and ancillary services market each week, effectively reducing the customer's settlement cycle from one month to one week. This significantly reduces the amount of collateral that the market participant is required to provide. So far, the NYISO has entered into such agreements with several of its customers, thereby reducing their combined collateral requirements by approximately 3.7 million dollars.

In addition, the NYISO has continued to investigate how third party clearing organizations might enhance its settlement process. Accordingly, the NYISO has continued discussions with the New York Mercantile Exchange, as mentioned in the March 29 Report, as well as North American Credit and Clearing and Depository Trust and Clearing Corporation.

2. Changes in Bilateral Scheduling. In the March 29 Report, the NYISO stated that it was beginning to explore a stakeholder proposal that would allow customers to schedule bilateral contracts without identifying a specific generation source. This proposal purportedly would reduce the need for customers engaging in certain transactions to provide collateral to the NYISO to cover market energy purchases while also providing collateral to counterparties to cover contracts for differences. Since the March 29 Report, the Project Prioritization Team, composed of stakeholders and NYISO staff, has examined the bilateral scheduling proposal and placed it in the project development queue for further consideration in 2005 if resources become available.

3. Aggregated Treatment of Municipals. In the March 29 Report, the NYISO reported that it was using its stakeholder process to propose an amendment to the NYISO tariffs that would allow municipal electric systems in New York to aggregate their unsecured credit since as a single joint action agency, the New York Municipal Power Agency, handles all of the bidding, scheduling, and settlement for its member municipal systems. Since the report was filed, the NYISO has obtained full stakeholder approval for such an amendment.. The Commission approved the proposed tariff changes in its July 30, 2004, *Order Re: Filing of Revised Tariff Sheets that Update Creditworthiness Requirements* ("July 30 Order").

C. Other Credit and Settlement Policy Enhancements

1. Collateral for Wholesale TSC. In some cases, refining the balance between protecting against the risk of default and minimizing customer collateral requirements mandates an *increase* in customer collateral requirements to address a previously unrecognized risk of loss. Since the March 29 Report, the NYISO has worked with stakeholders to mitigate a potential

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exposure transmission owners faced in the collection of wholesale transmission service charges due to them pursuant to the OATT. This risk arose because market participant obligations to pay these transmission charges were unsecured. Working through its stakeholder process, the NYISO developed an addition to its collateral requirements to provide security for this obligation. The Commission approved the NYISO's proposed tariff changes in the July 30 Order.

2. Virtual Transactions Collateral. The NYISO has worked with stakeholders to examine the methodology pursuant to which the NYISO determines customers' collateral requirements for engaging in virtual transactions. In response to a stakeholder proposal, the NYISO is developing a proposed tariff amendment designed to reduce collateral requirements for virtual transactions.

3. Successful Implementation of Paydown Option. Since the March 29 Filing and pursuant to the paydown authority established in the NYISO's OATT and Services Tariff, the NYISO has developed a standard paydown agreement for use by market participants. A paydown agreement provides that, in exchange for a customer obligation to pay down amounts owed to the NYISO upon demand, the NYISO shall determine the customer's collateral requirements based upon an estimate of projected purchases in the forthcoming month, rather than upon a historical basis. As a result of the NYISO's successful implementation of this paydown option, the NYISO has reduced the combined collateral requirement of those parties entering into paydown agreements by approximately 143 million dollars.

Respectfully submitted,

/s/ Andrew S. Antinori
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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in the above-captioned proceeding in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure 18 C.F.R. § 2010 (2004).

Dated at Albany, NY this 30th day of November 2004.

/s/ Andrew S. Antinori
Andrew S. Antinori
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290 Washington Ave. Ext.
Albany, NY 12203

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

New York Independent System Operator, Inc.)

**Docket No. ER03-552
ER03-984**

NOTICE OF FILING

Take notice that on November 30, 2004, the New York Independent System Operator, Inc. (“NYISO”) submitted a report regarding the NYISO settlement and customer credit policies.

Any person desiring to be heard or to protest this filing should file a motion to intervene or protest with the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426, in accordance with Rules 211 and 214 of the Commission’s Rules of Practice and Procedure (18 CFR §§ 385.211 and 385.214). Protests will be considered by the Commission to determine the appropriate action to be taken, but will not serve to make protestants parties to the proceeding. Any person wishing to become a party must file a motion to intervene. All such motions or protests should be filed on or before the comment date, and, to the extent applicable, must be served on the applicant and on any other person designed on the official service list. This filing is available for review at the Commission or may be viewed on the Commission’s website at www.ferc.gov, using the FERRIS link. Enter the docket number excluding the last three digits in the docket number filed to access the document. For assistance, call (202) 502-8222 or TTY, (202) 208-1659. Protests and interventions may be filed electronically via the Internet in lieu of paper. *See*, 18 CFR 385.2001(a)(1)(iii) and the instructions on the Commission’s website under the “e-filing” link. The Commission strongly encourages electronic filings.

Comment Date:

Magalie R. Salas, Esq.
Secretary