UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

New York Independent System Operator, Inc.	Docket Nos. ER03-552-004 ER03-552-005 ER03-984-002 ER03-984-003

ORDER GRANTING CLARIFICATION AND CONDITIONALLY ACCEPTING COMPLIANCE FILING

(Issued December 23, 2003)

I. Introduction

1. In this order, the Commission grants clarification of its order conditionally accepting 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).[1] This order also conditionally accepts a compliance filing required by the September 22 Order, which instructed NYISO to make several changes to its creditworthiness and working capital provisions that are part of its comprehensive financial assurance policy. These actions will benefit customers because they will clarify the Commission's intent and require compliance with the Commission's directives in the September 22 Order.

II. Background

2. In Docket No. ER03-552-000, the NYISO filed revisions to its Tariffs to specify the creditworthiness requirements for customers participating in the NYISO-administered

[1] New York Independent System Operator, Inc., 104 FERC ¶ 61,311 (2003) (September 22 Order).

markets. It stated that the proposed creditworthiness requirements protected against losses from non-payment by a NYISO customer without creating barriers to entry or unduly burdening customers in these markets. The NYISO stated that the customers who would be subject to the requirements were also those for whose benefit the requirements had been designed, since they ultimately had to cover the bad debts of other customers. The NYISO provided a detailed description of its creditworthiness requirements, as had been previously required by the Commission.[2] The NYISO also filed, on June 26, 2003 in Docket No. ER03-984-000, proposed revisions that would enhance its rules governing the allocation of new working capital contributions and bad debt losses among NYISO customers.

3. On September 22, 2003, the Commission conditionally accepted NYISO's proposed revisions to its Tariffs. However, the Commission found that the NYISO did not provide adequate justification for certain aspects of its filing. The Commission stated that it must balance the goal of allowing the ISOs and RTOs to reduce their risk of exposure in the event of default with the goal of ensuring that the credit or collateral requirements are not so stringent that they unnecessarily inhibit access to the marketplace. The Commission found that the NYISO had not adequately justified its proposed prohibition against customers netting their positions if they operate in more than one of the NYISO-administered markets.[3] The Commission directed NYISO to file revised tariff sheets to allow for netting across its markets in determining Operating Requirements. The order also required the NYISO to extend the pay-down agreement option to all, rather than only Investment Grade, customers,[4] permit surety bonds with a "pay now, fight later" provision, and provide that all working capital contribution adjustments (rather than only adjustments related to new working capital contributions)[5] use the new dollar volume methodology.

---

[2] See New York Independent System Operator, Inc., et al., 98 FERC ¶ 61,282 at 62,217 (2002).

[3] Netting allows customers to use current obligations owed by the NYISO to the customer to reduce collateral requirements.

[4] In lieu of providing collateral, this option allows a customer to pay down the amount by which its Operating Requirement exceeds the amount of its Unsecured Credit and any existing collateral.

[5] Working capital contributions are used to offset temporary imbalances in cash flow. The working capital fund contributes to the liquidity, stability, and efficiency of NYISO's markets.

III. Notice of Filing, Interventions and Protests

4. Notice of the NYISO's compliance filing was published in the Federal Register, 68 Fed. Reg. 62,573 (2003), with motions to intervene and protests due on or before November 13, 2003. The New York Transmission Owners[6] (NY Transmission Owners) filed a timely motion to intervene that raises no substantive issues.[7] The National Energy Marketers Association (NEM) filed timely comments with concerns, and NYISO subsequently filed an answer. NEM later responded to NYISO's filing.

5. Rule 213(a) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a) (2003), prohibits an answer to a protest and/or answer unless otherwise ordered by the decisional authority. We will accept NYISO's and NEM's answers because they have provided information that assisted us in our decision-making process.

IV. Requests for Clarification

6. On October 22, 2003 in Docket Nos. ER03-552-004 and ER03-984-002, the NYISO and the NY Transmission Owners requested clarification of the requirement that the NYISO allow netting within the NYISO markets. Both pleadings state that if the clarification requests are denied, they request rehearing of the September 22 Order.

7. Both entities request that the Commission clarify that the netting requirement does not require the NYISO to reduce the collateral the customer must provide by amounts that the customer may earn in the NYISO-administered markets at some time in the future. The NYISO states that these projected future earnings are speculative and are not meaningful security for the customer's obligations. For example, the potential return of a customer's Transmission Congestion Contracts (TCCs) suggests that those contracts will produce revenue in the future. If so, those TCCs may be a valuable source of future income for the customer. However, the returns on TCCs are speculative in nature and subject to change. A change in transmission system conditions can render a TCC substantially less valuable or even cause the TCC to yield negative congestion rents, thus requiring payments by the holder to the NYISO. As a result, the NYISO states it should not be required to allow a customer to net the potential value of such a contract against the amount of collateral that the customer would otherwise be required to provide.

---

[6] The New York Transmission Owners include Central Hudson Gas & Electric Corp., Consolidated Edison Company of New York, Inc., Long Island Power Authority, New York Power Authority, New York State Electric & Gas Corp., Orange and Rockland Utilities, Inc., Rochester Gas and Electric Corp., and Niagara Mohawk Power Corp.

[7] NY Transmission Owners were already parties to this proceeding by virtue of their timely intervention in Docket Nos. ER03-552-000 and ER03-984-000.

8. The NYISO also seeks clarification that the netting requirement of the September 22 Order is satisfied by NYISO's compliance filing. Essentially, the Netting Provision allows a customer to use current amounts due to the customer, and not potential future amounts, to reduce its collateral requirement.

V. Discussion of Clarification

9. We will grant the NYISO's and the NY Transmission Owner's requests for clarification regarding netting in NYISO's markets.

10. It was never the Commission's intent to permit netting of amounts that a customer may earn in the future in the NYISO-administered markets. We agree with both pleadings that the use of possible future earnings in the netting calculation could lead to a situation in which the NYISO is under-collateralized with respect to a customer's obligations to the NYISO. Moreover, current amounts due are reasonable security, since they are obligations that the NYISO knows for certain it owes the customers. As discussed below, we also agree that the NYISO's proposed Netting Provision in its October 23, 2003 filing will satisfy the Commission's September 22 Order.

11. Because the above clarifications address NYISO's and NY Transmission Owners' concerns, we dismiss as moot their requests for rehearing.

VI. Compliance Filing

12. On October 23, 2003 in Docket Nos. ER03-552-005 and ER03-984-003, the NYISO submitted proposed revisions to comply with the Commission's September 22 Order.[8] Specifically, the NYISO proposes to reduce the Energy Component of non-investment and unrated customers' Operating Requirements[9] to reflect 50 days of obligations. The NYISO also proposes to make conforming changes to the Operating Requirement for customers that have executed a prepayment agreement. The conforming changes were necessary since a prepayment agreement reduces the amount of collateral a customer must provide by half, so a customer with a prepayment agreement only needs to supply 25 days of security.

---

[8] On October 23, 2003, the NYISO also submitted a request to file its compliance filing one day out-of-time. The Commission will grant this request.

[9] The Operating Requirement reflects the nonpayment exposure attributable to each customer based on the customer's activity in each of the NYISO's markets; there is an Energy and Ancillary Services component, a UCAP component, a Transmission Congestion Charge component, and a Bid component.

13. The NYISO proposes to revise its Tariffs to allow all customers participating in the NYISO-administered markets to enter into a pay-down agreement. The NYISO also proposes the Netting Provision it describes in its request for clarification. It further proposes to revise its Tariffs to permit customers to use a surety bond with a "pay now, fight later" provision as collateral.

14. The proposed revisions provide that the revised methodology for calculating working capital contributions shall apply to both existing working capital contributions as well as those made after the effective date of the filing. Finally, the NYISO proposes various other minor changes required by the September 22 Order.

15. The NYISO requests that the revisions in Docket No. ER03-552-000 become effective on December 21, 2003, which is the effective date established in the September 22 Order. The NYISO proposes that the revisions in Docket No. ER03-984-000 become effective January 1, 2004, which is also the effective date established in the September 22 Order.

VII. Analysis of Compliance Filing

16. The NYISO's proposed revisions to its tariffs generally comply with the September 22 Order, and we will conditionally accept the revisions for filing, subject to the discussion below.

17. The Netting Provision will allow a customer to reduce the amount of collateral that it would otherwise be required to provide by a reasonable estimate of the amount that the NYISO will owe to the customer. Moreover, the Netting Provision limits netting to a customer's positive position in a market that can be offset by obligations that the NYISO already owes to that customer. We believe that the Netting Provision achieves the Commission's goal of striking a balance between reducing the NYISO's risk of exposure in the event of default while at the same time ensuring that the credit or collateral requirements are not so stringent that they unnecessarily inhibit access to the marketplace.[10]

18. NYISO's proposed Prepayment Agreement provisions would allow a transmission customer that has executed a prepayment agreement with the NYISO to reduce the Energy Component of its collateral by half, so that it would only need to supply 25 days of security. According to the NYISO, a Prepayment Agreement requires the customer to make weekly prepayments in amounts to be determined by NYISO for all purchases of

---

[10] The Commission notes that no one protested this aspect of the compliance filing.

Energy and Ancillary Services.[11] NYISO states that the prepayment amount will be the amount of the charges that the NYISO determines the customer is likely to incur in the coming week for purchases of Energy and Ancillary services.

19. NEM argues that requiring customers to prepay 25 days of energy charges as security is unfair and substantially increases the cost of doing business. NEM urges the Commission to reduce the NYISO's proposed collateral requirements for customers with a prepayment agreement from 25 days to ten days, since NEM customers can make payments within this time frame.

20. In our September 22 Order, we stated that it is necessary to require only enough collateral to protect NYISO from the risk of non-payment by its customers. Although not entirely clear, it appears from NYISO's answer that NYISO has minimal exposure in the energy market, since the estimated charges for customers with a prepayment agreement are collected before the service is even provided. It seems that NYISO's only risk of exposure would arise from underestimating the amount of prepayment owed each week; it is not clear how NYISO intends to handle any such discrepancies. We therefore direct the NYISO to either eliminate or modify the Energy Component of the Operating Requirement for customers with prepayment agreements to reflect only NYISO's actual risk of non-payment. Further, due to the ambiguity of the prepayment provisions, NYISO is directed to revise its tariff to clearly describe the terms and conditions of a Prepayment Agreement, and to adopt a pro forma Prepayment Agreement.

21. Regarding NEM's wish for a shorter payment cycle, we stated in the September 22 Order that shortening the payment cycle could be a way of decreasing up front collateral requirements. We directed NYISO to explore through its stakeholder process whether changes should be made to the settlement or credit procedures and to file a report on the results of those discussions. We expect NEM's ideas to be entertained in the course of that process.

22. NEM also objects to NYISO requiring a minimum "A" rating from a surety as not being competitively neutral and unnecessarily hard on smaller entities, since an affiliated guarantor is required to only be investment grade, which is a rating of "BBB-" or higher. NEM states the difference between an affiliated guarantor being rated "BBB-" or better and a surety being rated "A" or better creates an undue preference for larger energy marketers with parent affiliates. NEM also suggests that customers should be permitted to obtain guarantees from non-affiliated guarantors that meet the NYISO's credit requirements.

[11] NYISO Answer at pp. 2-3.

23. We disagree with NEM regarding the use of public ratings for surety bonds. As noted by NYISO, it is important that a third party guarantor clearly has adequate financial strength to secure the obligation of the NYISO customer. NYISO determines the financial strength of parent affiliates not only by requiring a minimum public rating of BBB-, but also by subjecting them to its own credit assessment (which may result in an adjustment in the amount of unsecured credit to be granted). Although NYISO and its stakeholders have adopted a different method of determining the financial strength of banks issuing letters of credit and of sureties (i.e., a minimum "A" public rating), it is not at all clear that this is a more stringent assessment criterion. Even if it were more stringent, however, the difference may be justified by the fact that companies with investment grade parent affiliates, whether large or small, are able to provide the NYISO with more financial security than a surety bond, which has been shown to be a less reliable form of collateral.[12] Moreover, we fail to see how the lower rating for an affiliated guarantor is prejudicial, since the smaller entities that NEM represents can also have investment grade affiliates themselves.

24. NEM's comments about allowing non-affiliated guarantors are beyond the scope of this compliance proceeding, as NYISO did not propose and the Commission did not require any revisions to the affiliate guarantee provisions of NYISO's Tariffs. NEM may pursue any desired changes to NYISO's policies through the NYISO stakeholder process.

25. Finally, the Commission notes that NYISO neglected to make a conforming revision to First Revised Sheet No. 499 in its Services Tariff (Original Volume No. 2). Under Section C of that sheet, which deals with Prepayment Agreements, NYISO did not replace "Non-Investment Grade Customer or an Unrated Customer" with "Customer," which would be consistent with the Commission-ordered changes to First Revised Sheet No. 727 of its OATT (Original Volume No. 1). Therefore, we direct the NYISO to make the above revision in a compliance filing within 15 days of the date of this order.

The Commission orders:

(A) The NYISO's and the NY Transmission Owners' requests for clarification are hereby granted, as discussed in the body of this order.

(B) The requests for rehearing are hereby dismissed as moot, as discussed in the body of this order.

(C) Subject to Ordering Paragraph (D), the NYISO's compliance filing is hereby conditionally accepted as discussed in the body of this order, to become effective on December 21, 2003 or January 1, 2004, as requested.

---

[12] See September 22 Order at P 57-58.

(D) The NYISO is hereby ordered to submit a compliance filing within 15 days of the date of this order reflecting the modification discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.