

**WORKING CAPITAL  
POLICY AND PROCEDURE**

I. Working Capital Information and History

In order to maintain the liquidity and stability of its markets and to accommodate its internal cash flow and working capital requirements, the New York Independent System Operator, Inc. (“NYISO”) has established the following:

- a. Sound creditworthiness criteria for Market Participants;
- b. Appropriate levels of credit insurance;
- c. A line of credit of \$50 million; and,
- d. A working capital fund targeted at \$50 million.

The purpose of this document is to outline the policies and procedures surrounding the working capital fund.

Rate Schedule 1 of the Open Access Transmission Tariff (“OATT”) permits the NYISO to collect “working capital and carrying costs on ISO assets, capital requirements and debts” from Market Participants. NYISO manages its cash flow by maintaining a prudent level of working capital as a supplement to the funds available under the NYISO’s established line of credit. These two sources afford the NYISO the flexibility to settle with the suppliers in the New York energy markets on time and in full each month while resolving inevitable billing and payment issues that will arise when administering a complex \$5 billion annual energy market.

Anticipating the need to balance cash flows and cover temporary imbalances between collections from purchasers and payments to suppliers, NYISO’s Board of Directors originally authorized a targeted level of \$50 million for working capital, and NYISO included the recovery of a working capital component in Rate Schedule 1 through December 2001.

II. Accumulation of the Working Capital Fund

The working capital fund has been accumulated in two segments. Prior to October 2000, the variable component of Rate Schedule 1 was collected from Market Participants one month in arrears. Projecting cash flow on a monthly basis, however, was difficult and the Rate Schedule 1 rate per MWH varied from (\$0.90) to \$1.94. The unpredictability of the variable component of Rate Schedule 1 absorbed most of what could have otherwise been available for working capital purposes. Since October 2000, the variable portion of Rate Schedule 1 has been settled during the actual billing month, which has resulted in a more predictable accumulation of working capital. As such, NYISO is no longer required to forecast the funds needed to settle variable Rate Schedule 1 charges.

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By early 2001, the net result of (a) including certain amounts in Rate Schedule 1 for working capital, and, (b) funding the variable portion of Rate Schedule 1, was an accumulation of approximately \$4 million toward working capital. At that time, the NYISO Board authorized NYISO to increase the working capital fund to approximately \$50 million. Accordingly, NYISO included a \$0.30 per MWH charge in Rate Schedule 1 from March through December 2001. After the settlement of December 2001 invoices in January 2002, NYISO had collected approximately \$46 million of the \$50 million target.

III. Working Capital Reconciliations

NYISO has agreed to monitor working capital fund activity both in total and according to each Market Participant’s respective share. An explanation will be included at the bottom of each Market Participant’s consolidated invoice summary page that will list current month working capital activity as follows:

|                             |                     |
|-----------------------------|---------------------|
| Opening Balance             | \$\$\$\$\$\$        |
| Current Month Contributions | \$\$\$\$\$\$        |
| Current Month Interest      | \$\$\$\$\$\$        |
| Other Adjustments           | <u>(\$\$\$\$\$)</u> |
| Ending Balance              | <u>\$\$\$\$\$\$</u> |

In addition, NYISO plans to include a separate Working Capital Transaction page in csv format within the consolidated invoice issued each month that can be reworked for a Market Participant’s use. The Working Capital Transaction page will detail a complete history of all transactions in the Market Participant’s working capital account.

An example of the Working Capital Transaction page is listed below:

| <u>Transaction Type</u> | <u>Transaction Date</u> | <u>Description</u> | <u>Amount</u> |
|-------------------------|-------------------------|--------------------|---------------|
| 10                      | 02/28/2001              | Opening Balance    | \$5,000       |
| 20                      | 03/01/2001              | Interest           | 250           |
| 30                      | 03/01/2001              | Contribution       | 750           |
| 20                      | 04/01/2001              | Interest           | 300           |
| 30                      | 04/01/2001              | Contribution       | 775           |
| 40                      | 04/15/2001              | Other Adjustment   | (1,000)       |

The specific treatment of contributions, interest, and other adjustments is detailed below in this policy.

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IV. Contributions to Working Capital

The \$4 million of working capital accumulated from November 1999 through February 2001 represents the net result of numerous invoices, making the respective contributions of each Market Participant difficult to determine. This initial working capital accumulation, therefore, will be allocated to Market Participants based on their load-ratio shares during this time period. The amounts determined under this allocation will represent the initial “opening balance” for each Market Participant’s Working Capital Transaction page.

Contributions made to working capital since March 2001 will be tracked and listed monthly on the each Market Participant’s Working Capital Transaction page. For example, for the period March through December 2001, a Market Participant’s contribution will reflect the rate for working capital contributions (i.e. \$0.30/MWH) times that Participant’s actual load consumed during that billing month.

Future working capital contributions are not expected to be assessed to generators under the proposed “85/15” methodology for sharing NYISO operating costs.

V. Interest on Working Capital

Interest allocated to Market Participants represents the actual interest earned on the funds in NYISO’s working capital bank account when invested in overnight short-term investments. Each Participant will be allocated a pro rata share of interest earnings by multiplying the gross monthly interest earned by each Participant’s percentage share of the balance in the working capital fund. For example, a Participant with a 5% share in the total working capital balance would be allocated \$5 of the total interest earned if the NYISO were to earn \$100 in monthly interest on the working capital fund.

NYISO may distribute accrued interest earned on the working capital fund to Market Participants periodically. This distribution of interest, however, will be at the discretion of the NYISO Board of Directors. Such distributions will be made as an adjustment to each Market Participant’s invoice, which would either increase a net payable from NYISO or decrease a net receivable due to NYISO (depending on the Market Participant’s balance).

NYISO’s external auditors advise that if interest is accrued and credited to a Market Participant’s account and is available for withdrawal, an IRS Form 1099-INT must be issued whether or not a cash disbursement is made. Based on NYISO policy that the interest is not available for Market Participant withdrawal until the NYISO Board of Directors has given its approval, therefore, a Form 1099-INT will only be issued if an

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actual disbursement of cash has been made.

Allocation of interest will first be reflected with the contribution made on the March 2001 invoices.

VI. Other Adjustments to Working Capital

Examples of other adjustments to working capital and the proposed treatments are as follows:

A. Distribution to Market Participant that exits NYISO's markets:

When a Market Participant exits the NYISO's markets, NYISO will refund the Participant's working capital balance.

This refund will not occur, however, until the Market Participant has paid all final settlement adjustment invoices, and the challenge period for all final invoices has expired. NYISO may be willing to refund the working capital balance prior to the end of the challenge period if the Market Participant signs a release accepting all final settlement invoices as accurate and waiving all rights to challenge their final settlement invoices. Upon leaving the NYISO markets, the Market Participant must notify NYISO where to send any future distributions of working capital.

Distributions of the working capital fund would be replenished at the discretion of the NYISO Board of Directors. The Board's decision would be based on the remaining balance of the working capital fund following any distributions and its assessment of the NYISO's working capital needs. If the Board elects to replenish the working capital fund, Rate Schedule 1 would be increased. The NYISO would notify Market Participants of a decision to replenish the working capital fund in the monthly posting of Rate Schedule 1.

B. Charge for Market Participant Defaults (i.e. Bad Debt Losses):

If all balances due to NYISO on settlement invoices are not received on the dates specified in the tariff, NYISO will need to utilize funds accumulated in the working capital fund to make payments in full to suppliers. In these situations, the defaulting Market Participant's balance in the working capital fund and available collateral may be applied toward the outstanding receivable balance and against any future obligations from that Participant for settlement adjustments. If a balance remains in working capital after all settlement adjustments are completed, that balance will be returned to the Market Participant after the final bill challenge period has ended.

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Once a bad debt loss is declared, NYISO will recover the amount of the loss through Rate Schedule 1 from Market Participants in NYISO's markets during the month of the loss. The recovered amount will be returned to the working capital fund. (See additional details on the treatment of bad debt losses in the NYISO's Bad Debt Losses Policy.)

Attachment 1 to this policy contains an example to illustrate how bad debt losses would be prorated among working capital balances, and then recovered through Rate Schedule 1.

C. Temporary Draw on Working Capital due to Load Forecasting Shortfalls:

If the actual load in a given month is lower than forecasted load, this may cause a shortfall in the amount NYISO needs to recover for monthly operating budget. To date, NYISO has recovered its full monthly budget by drawing the shortfall amount from the working capital fund. Going forward, NYISO will apply only the amount actually recovered in a given month toward the operating budget. If the load is consistently lower than forecasted, NYISO may either borrow funds from working capital or increase Rate Schedule 1 to compensate for amounts needed to fully fund the approved operating budget.

D. NYISO Share of Working Capital:

Certain transactions occurring within the working capital fund are not specific to individual market participants (or their shares of the working capital fund), and will be considered to represent NYISO's share of the working capital fund. Examples of such transactions include monthly transactions with other ISO's, payments/recoveries of DAC adjustments, timing of past due receivables, and temporary draws on working capital due to load forecasting shortfalls. When a draw on working capital is required for situations as described in B and C above, the adjustment to working capital will be made according to the following order:

- i) first, to a defaulting market participant (if any)
- ii) second, to NYISO's share of working capital (to the extent available), and
- iii) finally, on a pro-rata share to market participant shares of working capital.

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VII. New Market Participants joining NYISO

An initial contribution to working capital will not be required from new Market Participants (i.e. “an entry fee”). As discussed above, however, the new Market Participant would be subject to any potential future replenishments of the working capital fund necessitated by defaults of Market Participants.

VIII. Working Capital Not Considered Collateral

Market Participant contributions to the working capital fund are not a substitute for, and do not represent an acceptable form of, collateral, as required under the NYISO’s tariffs and its Financial Assurance Policy. As noted above, however, if a Market Participant is declared in default, the NYISO may, at its discretion, utilize that Participant’s working capital balance to offset any outstanding receivable balance when other forms of collateral are deemed insufficient to cover a defaulted payment obligation.

IX. Working Capital Treatment under proposed Northeast RTO

The specific treatment of the working capital fund as well as the overall credit/collateral/financial assurances for Market Participants in a Northeast RTO (NERTO) would be addressed during any transition to an NERTO. The NYISO will ensure, however, that any NERTO-related agreements include language providing that contributions to the NYISO’s working capital fund will be returned to NYISO market participants upon the transition to the NERTO or, at a Market Participant’s request, credited towards any working capital contribution requirement that may accrue to them as a Market Participant in the NERTO.