



*FERC Order 741-A:
Credit Reforms in Organized
Wholesale Electric Markets
Update*

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Summary

- ◆ In November 2010, NYISO sought rehearing of Order No. 741 on one credit reform (ability to offset market obligations).
- ◆ On February 17, 2011, FERC issued Order No. 741-A denying all requests for rehearing on the ability to offset market obligations issue.
- ◆ FERC has extended the deadline for making a compliance filing with respect to the ability to offset market obligations to September 30, 2011, with tariff revisions to take effect January 1, 2012.

Ability to Offset Market Obligations

Summary of FERC Order

- ◆ FERC directs each ISO/RTO to submit a compliance filing that includes tariff revisions to include one of the following options:
 - *Establish a central counterparty.*
 - *Require market participants to provide a security interest in their transactions in order to establish collateral requirements based on net exposure.*
 - *Propose another alternative, which provides the same degree of protection as the two above-mentioned methods.*
 - *Choose none of the three above alternatives, and instead establish credit requirements for market participants based on their gross obligations (¶ 117, pages 55-56).*

Summary of Options

<u>Option</u>	<u>Points of Consideration</u>
1. Central Counterparty	<ul style="list-style-type: none"> • Of the four options provided by FERC, Market Participants appear to support this option. • NYISO researching implications on accounting treatment, debt covenants, insurance, taxes & others (see next slide). • Potential tax exposure is currently largest concern. • The CFTC has expressed a preference for this option.
2. Obtain Security Interest in MP Receivables	<ul style="list-style-type: none"> • Many Market Participants are prohibited from providing such a security interest (either by law or existing financing arrangements). • Some additional NYISO administrative and legal costs.
3. Develop Another Option	<ul style="list-style-type: none"> • To date, NYISO and Market Participants have not identified another viable option that meets FERC Order 741.
4. Collateralize Based on Gross Obligations	<ul style="list-style-type: none"> • Some Market Participants could incur potentially significant increases in creditworthiness requirements.

Establish a Central Counterparty

- ◆ *What is a Central Counterparty?*
 - *Acts as the counterparty to all participants in the market.*
 - Explicitly taking title to transactions further supports a finding of mutuality in those transactions, thereby permitting setoff in a bankruptcy proceeding.

- ◆ *Implementation Requirements:*
 - *Amendments to NYISO tariffs noting that NYISO is a counterparty to all Market Participant transactions.*
 - *No software development or process changes are anticipated.*

Establish a Central Counterparty

◆ Risks and Implications

■ *Accounting Treatment*

- NYISO's independent auditors have agreed that the NYISO's financial statements can continue to be recorded on a net basis.
- NYISO's independent auditors are continuing to review the NYISO's financials for purposes of tax treatment.

■ *Debt Covenants*

- NYISO's legal counsel indicates there are no prohibitions to becoming a central counterparty.

■ *Insurance*

- NYISO's insurance broker confirms there are no impacts to NYISO's insurance policies / coverage / etc.

Establish a Central Counterparty

◆ Risks and Implications

■ *Tax Concerns*

- The NYISO is a 501(c)(3) and New York not-for-profit entity.
- Legal counsel does not believe that becoming a central counterparty to market transactions changes the substance of NYISO's operations, and therefore, should not alter NYISO's tax-exempt status.
- Legal counsel has advised that the NYISO should notify the IRS and NYS of this potential change and obtain confirmation of the continuation of NYISO's existing tax treatment.
- NYISO would not likely obtain advisory opinions from the IRS or NYS prior to September 30, the due date of the compliance filing for Order 741-A.

Next Steps

- ◆ NYISO staff is pursuing the Central Counterparty option to comply with FERC Orders 741/741-A.
 - *Recommendation is dependent on the results of the tax discussions with the IRS and NYS.*
 - *NYISO and certain other ISOs/RTOs have initiated discussions with FERC to obtain additional time to comply with Order 741-A.*
 - *A motion seeking the extension will be filed in July/August.*
 - *In June, NYISO and certain other ISOs met with the Internal Revenue Service regarding this topic and are currently preparing requests for private letter rulings by the IRS.*
 - *NYISO is also planning to initiate discussions with New York State during July/August.*

Next Steps

- ◆ NYISO staff is pursuing the Central Counterparty option to comply with FERC Orders 741/741-A.
 - *NYISO staff will provide regular updates to Market Participants and appropriate regulators, as needed.*
 - *In the event tax discussions reveal that becoming a central counterparty is not in the best interest of NYISO and its Market Participants, the NYISO will need to revisit remaining options.*



The New York Independent System Operator (NYISO) is a not-for-profit corporation that began operations in 1999. The NYISO operates New York's bulk electricity grid, administers the state's wholesale electricity markets, and provides comprehensive reliability planning for the state's bulk electricity system.

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