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March 7, 2006

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

Re: California Independent System Operator Corporation
Docket No. ER06-____- 000
March 2006 Credit Policy Amendments to the Tariff of the California Independent System Operator Corporation

Dear Secretary Salas:

Pursuant to Section 205 of the Federal Power Act ("FPA"), 16 U.S.C. § 824d, and Section 35.13 of the regulations of the Federal Energy Regulatory Commission ("Commission"), 18 C.F.R. § 35.13, the California Independent System Operator Corporation ("CAISO") respectfully submits for filing an original and five copies of an amendment (containing the "March 2006 Credit Policy Amendments") to the CAISO's Simplified and Reorganized ("S&R") Tariff, which was filed and approved in Docket No. ER05-1501.[1] The March 2006 Credit Policy Amendments revise the S&R Tariff to modify the credit requirements and procedures contained therein.

Two extra copies of this filing are also enclosed. Please stamp these copies with the date and time filed and return them to the messenger.

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1 The Commission has accepted the S&R Tariff effective as of March 1, 2006. *See California Independent System Operator Corp.*, 114 FERC ¶ 61,199 (2006). The S&R Tariff as accepted by that order (*see id.* at Ordering Paragraph (A)) is referred to in the instant filing as the "current S&R Tariff". Capitalized terms not otherwise defined herein are used in the sense given in the Master Definitions Supplement, Appendix A to the S&R Tariff.

I. BACKGROUND

From the time the CAISO began operations, it has employed provisions in its Tariff that require Market Participants[2] that submit Schedules or transact in the CAISO's markets to satisfy creditworthiness requirements or else post financial security, in order to provide assurance that the Market Participants can meet their present and future financial obligations in the CAISO's settlement process. These credit provisions are now contained in Section 12 of the S&R Tariff.[3] Section 12 describes the creditworthiness requirements and the requirements for posting financial security, the circumstances in which a Market Participant fails to satisfy those requirements, and certain steps that the CAISO can take if a Market Participant fails to satisfy the requirements. Further implementation details regarding the credit provisions in Section 12 are found in the CAISO Credit Policy & Procedures Guide ("Guide"), which is available on the ISO Home Page at <http://www.caiso.com/docs/2005/06/14/200506141656326466.html>.[4]

Ever since the California energy crisis of 2000-2001, the CAISO has periodically been evaluating whether changes should be made to its credit policies, as provided in the Tariff and the Guide, in order to better ensure that Market Participants satisfy creditworthiness standards or post financial security sufficient to cover all of their financial obligations in the CAISO settlement process and to discourage defaults in the CAISO's markets. This is an issue of concern not only to the CAISO and Market Participants but also to the Commission, as evidenced by the Commission's *Policy Statement on Electric Creditworthiness*. As the Commission stated in its *Policy Statement*:

> [T]he Commission [has] explained that . . . credit downgrades have raised the level of concern regarding credit-related risks. . . . In addition, the Commission [has] stated that it believes that there are ways for ISOs/RTOs to reduce credit/default exposure and, in turn,

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2 Specifically, prior to the filing of these March 2006 Credit Policy Amendments, the credit provisions of Section 12 of the S&R Tariff applied only to Scheduling Coordinators ("SCs"), Utility Distribution Companies ("UDCs"), and Metered Subsystems ("MSSs"). SCs, UDCs, and MSSs are all types of "Market Participants," as that term is defined in the S&R Tariff, and the Tariff revisions proposed in the instant filing use the term "Market Participants" when referring to credit requirements applicable to SCs, UDCs, and MSSs. As described below, in the instant filing the CAISO also proposes to apply the revised credit provisions in Section 12 to bidders for Firm Transmission Rights ("FTRs").

3 The S&R Tariff simplified and reorganized the CAISO's tariff and, among other things, gathered the credit-related tariff provisions that were in several different sections and placed them in a new Section 12.

4 In its *Policy Statement on Electric Creditworthiness*, 109 FERC ¶ 61,186 (2004) ("*Policy Statement*"), the Commission stated that it expected ISOs and RTOs to post their credit policies and practices either in their tariffs or on their websites. *Id.* at PP 8-12.

> to minimize the mutualized default risk in their markets. . . . ISOs/RTOs are typically non-profit entities that administer the market on behalf of market participants. In such markets, credit is collectively extended by market participants to each individual market participant. As a result, if one market participant defaults, it falls upon the remaining participants to make up the shortfall (i.e., the default risk is mutualized).[5]

The CAISO evaluated potential changes to its credit policies by benchmarking the practices of other ISOs and RTOs, obtaining internal and stakeholder feedback, and using that information and discussion to develop recommendations that would ultimately be presented to the CAISO's Board of Governors. The CAISO conducted stakeholder meetings on November 13, 2003,[6] November 30, 2004 and April 26, 2005, to discuss possible changes to its credit policies. By the CAISO's count, a total of 26 entities and 33 individuals participated in the stakeholder meetings. The stakeholders were generally supportive of the proposals the CAISO put forth at the meetings, though they also raised a number of questions and suggestions. After those meetings, the CAISO solicited written comments and questions from stakeholders. The CAISO received comments and questions in writing from nine stakeholders and verbally from several others. The CAISO posted the comments and questions, as well as written responses that the CAISO provided to each of them, on the ISO Home Page (at <http://www.caiso.com/docs/2003/04/21/2003042117001924814.html>).

On May 6, 2005, CAISO Management provided to the Finance Committee of the CAISO's Board of Governors proposed revisions to its credit policies. As described in the June 8, 2005 memorandum to the Finance Committee that is provided in Attachment C to the instant filing ("June 8 Memorandum"), the CAISO divided the proposed changes into three categories: (1) changes that did not need to be included in a tariff amendment, and that the CAISO had already

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5 *Policy Statement*, 109 FERC ¶ 61,186, at PP 4-5. In the *Policy Statement*, the Commission also requested that ISOs and RTOs submit reports addressing their progress toward implementing any measures that might serve to reduce the mutualized default risk in their markets (or their reasons for not yet adopting such measures) and addressing any future plans that the ISOs and RTOs had for reducing the mutualized default risk. *Id.* at P 33. In response, the CAISO filed a report that included discussion of the following: the transparency of the CAISO's current credit policies; the CAISO's current tools for determining creditworthiness; the CAISO's efforts to improve the accuracy of those tools; the CAISO's processes for communicating with Market Participants concerning creditworthiness; and the CAISO's current measures and future plans for reducing risk in the CAISO's markets. *See* Report of the CAISO, Docket No. PL05-3-000 (Feb. 17, 2005).

6 See topics discussed at Market Issues Forum discussion available on the ISO Home Page at <http://www.caiso.com/docs/2000/06/12/200006121229457917.html>.

implemented; (2) changes to be included in "Phase 1" of the credit policy revisions, some of which would require a tariff amendment to implement; and (3) changes to be included in "Phase 2" of the CAISO's credit policy revisions, some of which may require a later tariff amendment to implement (to be filed subsequent to the instant filing).[7] The June 8 Memorandum requested authorization to proceed with preparing and filing the tariff language for the Phase 1 changes and to develop procedures for implementing each of the Phase 1 changes. Pursuant to that request, on June 15, 2005, the CAISO's Board of Governors unanimously approved the Phase 1 changes to the CAISO's credit policies and directed Management to proceed with developing tariff language (as necessary) and revising its business practices to implement the changes. The Board of Governors' motion approving those actions is provided in Attachment D to the instant filing.

As described in Section II, below, the March 2006 Credit Policy Amendments include proposed tariff provisions to implement Phase 1 changes described in the June 8 Memorandum, include proposed revisions to Section 12 to better ensure that Market Participants provide credit or post financial security sufficient to cover all of their financial obligations and to discourage market defaults, and add definitions to Appendix A to the S&R Tariff to reflect those revisions. The instant filing also contains conforming revisions to other sections of the S&R Tariff, and reflects additional efforts to simplify and reorganize the S&R Tariff by eliminating needless duplication. In addition, the provisions contained in the instant filing are consistent with the CAISO's vision of achieving a user-friendly, well organized Tariff with supporting implementation detail in manuals and guides such as the CAISO Credit Policy & Procedures Guide. The CAISO deferred submitting the instant filing until after the Commission made the S&R Tariff effective, in order to take advantage of the new organizational format of Section 12 (see footnote 3, above) to present the revisions contained in this filing in a more clear and straightforward manner.

II. PROPOSED CHANGES

In the instant filing, Section 12.1 has been revised to state that the CAISO's credit requirements apply not only the CAISO's acceptance of schedules and all transactions in the CAISO markets, but also the payment of charges pursuant to the S&R Tariff (including the Grid Management Charge). This is essentially a restatement of the provisions previously included in Section 12.3 of the S&R Tariff that clarify that financial securities required under the Tariff are intended to cover an entity's outstanding and estimated liability for the Grid Management Charge and/or other charges assessed pursuant to the S&R Tariff.

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[7] Many of the Phase 2 issues still under consideration require further definition and review with stakeholders or may require CAISO computer system changes that are only expected to be available in 2007 (*e.g.*, the new Settlements and Market Clearing system).

A number of the proposed changes are intended to clarify that the CAISO will apply the credit provisions of Section 12 to all entities subject to credit requirements under the S&R Tariff. Bidders in the CAISO's FTR auctions (or "FTR Bidders," a term defined in Appendix A to the S&R Tariff) are already subject to certain credit requirements pursuant to Section 36.2.6 of the S&R Tariff. Section 12.1 has been revised to clarify that the CAISO's credit requirements apply to FTR Bidders. In addition, as discussed in footnote 2 above, Section 12.1 has been revised to state that it applies to Market Participants instead of referring solely to SCs, UDCs, and MSSs. The term Market Participant is defined in Appendix A to the S&R Tariff and includes SCs, UDCs, and MSSs.

Under the current S&R Tariff, SCs, UDCs, and MSSs that have an Approved Credit Rating (as defined in the S&R Tariff) generally obtain unlimited unsecured credit in the CAISO markets.[8] The instant filing replaces the right of Market Participants to satisfy the CAISO's credit requirements by maintaining an Approved Credit Rating with a process by which the CAISO determines entity-specific Unsecured Credit Limits.

Revised Section 12.1 of the S&R Tariff states that a Market Participant's or FTR Bidder's financial transactions with the CAISO (including participation in any auction of FTRs), must be secured by maintaining an "Unsecured Credit Limit" and/or by posting "Financial Security," the level of which constitutes the Market Participant's or FTR Bidder's "Financial Security Amount." The sum of a Market Participant's or FTR Bidder's Unsecured Credit Limit and Financial Security Amount will represent its "Aggregate Credit Limit." Each Market Participant is required to maintain an Aggregate Credit Limit that is at least equal to its "Estimated Aggregate Liability." An FTR Bidder's Aggregate Credit Limit in excess of its Estimated Aggregate Liability may be used to establish the limit on the amount an FTR Bidder may bid in any auction of FTRs.

The CAISO believes that the proposed approach of determining unsecured credit limits is an improvement on the current designation of entities that meet certain criteria as having an Approved Credit Rating permitting them an unlimited amount of unsecured credit. The replacement of an unlimited amount of unsecured credit with an entity-specific, CAISO-specified amount of unsecured credit will provide greater assurance that each Market Participant and FTR Bidder can satisfy its financial obligations and not present undue credit risk to CAISO market creditors.

This proposed approach to establishing unsecured credit limits is comparable to that used by other ISOs and RTOs. The CAISO reviewed and

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8 *See* S&R Tariff, § 12.1; S&R Tariff, Appendix A (definition of "Approved Credit Rating").

used elements of the credit policies of its peer ISOs and RTOs in developing its approach.[9] The proposed approach also accords with the guidance provided by the Commission's *Policy Statement*, as the CAISO will consider qualitative and quantitative factors in setting the unsecured credit limits for rated entities, and will not deny unsecured credit to financially strong entities merely because they do not maintain an agency credit rating.[10]

An Unsecured Credit Limit is defined in the proposed Tariff revisions as the level of credit established for a Market Participant or FTR Bidder that is not secured by any form of Financial Security, as provided for in the S&R Tariff. Financial Security is defined as any of the types of financial instruments listed in Section 12 of the S&R Tariff. A Financial Security Amount is defined (in an adaptation of the current defined term "ISO Security Amount") as the level of Financial Security posted in accordance with the S&R Tariff. An Aggregate Credit Limit is defined as the sum of a Market Participant's or FTR Bidder's Unsecured Credit Limit and its Financial Security Amount, as provided for in Section 12 of the S&R Tariff. An Estimated Aggregate Liability is defined as the sum of a Market Participant's or FTR Bidder's known and reasonably estimated potential liabilities for a specified time period arising from charges described in the S&R Tariff, as provided for in Section 12 of the S&R Tariff. The defined term Approved Credit Rating has been deleted, and the use of that term has been eliminated throughout the S&R Tariff.

New Section 12.1.1 contains provisions concerning the CAISO's determination of Unsecured Credit Limits. Each Market Participant or FTR Bidder requesting an Unsecured Credit Limit must submit a credit application to the CAISO and periodically provide other financial information. The CAISO will determine whether the Market Participant or FTR Bidder will receive an Unsecured Credit Limit, and if so, what that Unsecured Credit Limit will be, in accordance with the procedures described in the Guide posted on the ISO Home Page. The process used will be transparent and the factors used in the determination of the limit will be available to the applicant. Any individual limit established through the entity-specific process for setting Unsecured Credit Limits will also be subject to a ceiling: the maximum Unsecured Credit Limit for a Market Participant or FTR Bidder will be $250 million (or a lesser amount determined by the CAISO's Board of Governors, in its discretion, and posted on the ISO Home Page). The CAISO believes that $250 million is an ample cap on Unsecured Credit Limits, and the CAISO's Board of Governors might in the future determine that a lesser Unsecured Credit Limit is more prudent, particularly after

9 See the CAISO document entitled "SC Credit Policy Appendix A – Credit Limit Caps," which is posted on the ISO Home Page at <http://www.caiso.com/docs/09003a6080/35/8a/09003a6080358a90ex.html>.

10 *See Policy Statement*, 109 FERC ¶ 61,186, at PP 13-14.

the planned reduction in the number of days outstanding in the CAISO payment cycle in 2008 upon the CAISO's implementation of "Accelerated Payments".

New Section 12.1.1.1 contains provisions describing how the CAISO will determine Unsecured Credit Limits for Affiliates. New Section 12.1.1.2 contains provisions requiring a Market Participant or FTR Bidder to provide the CAISO with notification of a "Material Change in Financial Condition." The new term "Material Change in Financial Condition" is defined as a change in or potential threat to the financial condition of a Market Participant or FTR Bidder that increases the risk that it will be unlikely to meet some or all of its financial obligations to the CAISO. It is important that the CAISO be notified of such Material Changes in Financial Condition, because such a change may signal an alteration in the creditworthiness of a Market Participant or FTR Bidder. New Section 12.1.1.3 contains provisions concerning the transition from the current credit regime, under which a Market Participant or FTR Bidder may maintain an Approved Credit Rating, to the credit regime proposed in the instant filing, under which a Market Participant or FTR Bidder may obtain an Unsecured Credit Limit.

Section 12.1.2 of the proposed new provisions in the Tariff addresses "Financial Security" and the "Financial Security Amount."[11] The section lists the acceptable types of Financial Security, including letters of credit, surety bonds, guarantees, and escrow accounts. It states that the CAISO requires the use of the CAISO's standardized forms for the various types of acceptable Financial Security to the greatest extent possible. New Section 12.1.2.1 states that a Market Participant or FTR Bidder may seek the ISO's permission to use a form for Financial Security other than a standardized form, and the CAISO will determine whether the proposed non-standardized form should be approved as reasonably acceptable. The CAISO anticipates that the standardized forms, which are the easiest to administer, will cover the vast majority of Market Participants and FTR Bidders.

New Section 12.1.2.2 provides that the CAISO may treat financial instruments that do not have automatic renewal provisions and that are not renewed or replaced within 30 days of their dates of expiration as being out of compliance with the standards for Financial Security under the S&R Tariff and may deem the value of those instruments to be zero, and may draw upon such Financial Security prior to its stated expiration if deemed necessary by the ISO. The CAISO has learned from experience that some Market Participants do not renew their financial instruments until very shortly before expiration, and that practice could put the CAISO in the position of being unsecured if the instrument should expire before being drawn. Section 12.1.2.2 will encourage the timely

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[11] The term "Financial Security Amount" replaces the term "ISO Security Amount" in the current S&R Tariff.

renewal of financial instruments and will reduce the likelihood of under-secured Market Participants exposing other CAISO participants to credit default risk.

New Section 12.1.2.3 clarifies that the risk of loss of a Financial Security Amount held and invested by the CAISO on behalf of a Market Participant or FTR Bidder will be borne by the Market Participant or FTR Bidder that provided the Financial Security Amount. As the section indicates, and as discussed in June 8 Memorandum provided as Attachment C to this filing, the CAISO will invest these funds in relatively conservative investments (the CAISO will invest only in bank accounts, high quality money market accounts, or U.S. Treasury/Agency securities in accordance with the CAISO's investment policy), unless a Market Participant or FTR Bidder makes a written request to have the CAISO invest a Financial Security Amount in a different type of investment and the CAISO agrees in writing. Thus, although a Market Participant or FTR Bidder will bear the risk of loss as provided in the section, that risk of loss will be minimized due to the relative safety of the investment by the CAISO, unless the Market Participant or FTR Bidder will have expressly directed the CAISO to invest the security in an alternative form of investment (which in any event must also be an authorized investment under the CAISO's conservative investment policy), and the CAISO consents in writing.[12]

New Section 12.1.4 states that an FTR Bidder may elect to allocate a portion of its Aggregate Credit Limit toward satisfying the credit requirements for participating in auctions of FTRs, as set forth in Section 36.2.6 of the S&R Tariff. This provision therefore links the general credit requirements set forth in Section 12 to the specific requirements for FTR Bidders in Section 36 of the S&R Tariff.

New Section 12.1.5 contains provisions concerning Estimated Aggregate Liability. The section states that the CAISO will periodically calculate an Estimated Aggregate Liability for each Market Participant and FTR Bidder based on all charges and settlement amounts for which the Market Participant or FTR Bidder is liable or reasonably anticipated by the CAISO to be liable for pursuant to the S&R Tariff. The Estimated Aggregate Liability will be determined and applied by the CAISO consistent with the procedures set forth in the Guide posted on the ISO Home Page. The CAISO will upon request provide each Market Participant and FTR Bidder with information concerning the basis for the CAISO's determination of its Estimated Aggregate Liability, and this determination may be contested in accordance with the procedures set forth in the Guide. The ISO will compare each Market Participant's and FTR Bidder's

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12 See the CAISO investment policy posted on the ISO Home Page at <http://www.caiso.com/docs/09003a6080/36/1a/09003a6080361ad8.pdf>. The CAISO must be reasonably satisfied that the alternative investment will maintain the value of the Financial Security Amount.

Estimated Aggregate Liability against its Aggregate Credit Limit on a periodic basis.

Section 12.2 has been revised to modify the provisions concerning the CAISO's review of creditworthiness, in order to reflect the new defined terms described above.

Section 12.3 has been revised to modify the provisions concerning posting and releases of financial security. The revisions include new procedures for a Market Participant or FTR Bidder to request that its Financial Security Amount be reduced or released. The CAISO will evaluate all such requests and may decline to reduce or release a Financial Security Amount for any of the reasons listed in Section 12.3. These revisions are intended to increase the likelihood that a Market Participant or FTR Bidder will have a sufficient Financial Security Amount at all times.

New Section 12.4 revises current Section 12.3 with regard to the calculation of ongoing financial security requirements. Section 12.4 states that, following the date on which a Market Participant commences trading, if the Market Participant's Estimated Aggregate Liability, as calculated by the CAISO, at any time exceeds its Aggregate Credit Limit, the CAISO will direct the Market Participant to post an additional Financial Security Amount within five Business Days that is sufficient to ensure that the Market Participant's Aggregate Credit Limit is at least equal to its Estimated Aggregate Liability. As is the case under the current S&R Tariff, the CAISO will notify a Market Participant if at any time its Estimated Aggregate Liability exceeds 90% of its Aggregate Credit Limit.

New Section 12.5 concerns ISO enforcement actions regarding under-secured Market Participants. The section states that if a Market Participant's Estimated Aggregate Liability exceeds its Aggregate Credit Limit, the CAISO may take any or all of the following actions:

- The CAISO may withhold a pending payment distribution. This action is authorized by Section 11.12.4 of the S&R Tariff, which states that the CAISO is "authorized to recoup, set off and apply any amount to which any defaulting ISO Debtor is or will be entitled, in or towards the satisfaction of any of that ISO Debtor's debts arising under the CAISO's Settlement and billing process."[13]

- The CAISO may limit trading, which may include rejection of Schedules and/or limiting other CAISO Market activity. In such case, the CAISO will

[13] An ISO Debtor is "[a] Scheduling Coordinator, Participating TO, or other Market Participant that is required to make a payment under the terms of the ISO Tariff." S&R Tariff, Appendix A (definition of "ISO Debtor").

notify the Market Participant of its action and the Market Participant will not be entitled to submit further Schedules to the CAISO and may not otherwise participate in the CAISO's markets until the Market Participant posts an additional Financial Security Amount to ensure that the Market Participant's Aggregate Credit Limit is at least equal to its Estimated Aggregate Liability. The CAISO's authority for this action is found in the current versions of S&R Tariff Sections 12.3 and 12.3.1, which limit trading and authorize the rejection of Schedules.[14] This authority is further confirmed by Commission orders on CAISO creditworthiness.[15]

- The CAISO may require the Market Participant to post an additional Financial Security Amount in lieu of an Unsecured Credit Limit for a period of time. The CAISO is authorized to take this action by the provisions in current Section 12.2, which permits the ISO to require a Market Participant to provide credit support in the form of Financial Security if the Market Participant "delays or defaults in making payments due under the S&R Tariff."

- The ISO may restrict, suspend, or terminate a Market Participant's Service Agreement. The termination of a Scheduling Coordinator's Service Agreement is authorized by the current version of Section 4.5.4.4 of the S&R Tariff, and the ability to terminate the Service Agreement encompasses the ability to restrict or suspend it.

- In addition, the CAISO may restrict or suspend a Market Participant's right to Schedule or require the Market Participant to increase its Financial Security Amount if at any time such Market Participant's potential additional liability for Imbalance Energy and other ISO charges is determined by the ISO to be excessive by comparison with the Energy scheduled by the Market Participant. This provision reflects the CAISO's authority as stated in the current version of Section 12.3.2 (which the CAISO now proposes to delete because its provisions are captured in the language described above).

The CAISO has made changes to portions of the S&R Tariff other than Section 12 and Appendix A to conform those portions of the S&R Tariff with the modifications to Section 12 and Appendix A contained in the instant filing (*e.g.*,

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[14] The ISO proposes to delete the current version of Section 12.3.1 in the instant filing, because its provisions are captured in the language described in the bullet point above.

[15] See California Independent System Operator Corp., 95 FERC ¶ 61,026, at 61,080-81 (2001); California Independent System Operator Corp., 95 FERC ¶ 61,391, at 62,457-58 (2001); California Independent System Operator Corp., 97 FERC ¶ 61,151, at 61,658-59 (2001); California Independent System Operator Corp., 98 FERC ¶ 61,335, at 62,425-26, 62,430 (2002).

by modifying the Scheduling Coordinator Application contained in Appendix T to the S&R Tariff to reflect the use of the Unsecured Credit Limit and Financial Security described above).

III. EFFECTIVE DATE

The CAISO requests that the Commission make all of the revisions contained in these March 2006 Credit Policy Amendments effective sixty days after submittal of the instant filing, *i.e.*, on May 7, 2006.

IV. COMMUNICATIONS

Communications regarding this filing should be addressed to the following individuals, whose names should be placed on the official service list established by the Secretary with respect to this submittal:

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V. SERVICE

The CAISO has served copies of this transmittal letter, and all attachments, on the California Public Utilities Commission, the California Energy Commission, the California Electricity Oversight Board, and all parties with effective Scheduling Coordinator Service Agreements under the S&R Tariff. In addition, the CAISO is posting this transmittal letter and all attachments on the ISO Home Page.

VI. ATTACHMENTS

The following documents, in addition to this transmittal letter, support the instant filing:

Attachment A	Revised S&R Tariff sheets that incorporate the proposed changes described above
Attachment B	The proposed changes to the S&R Tariff shown in black-line format
Attachment C	The June 8 Memorandum
Attachment D	The CAISO Governing Board's June 15, 2005 motion

VII. CONCLUSION

For all the foregoing reasons, the Commission should accept these March 2006 Credit Policy Amendments to become effective May 7, 2006. Please feel free to contact the undersigned if you have any questions concerning this matter.

Respectfully submitted,

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ATTACHMENT A

4.5.1.1.1 Scheduling Coordinator Applicant makes a Request.

To become a Scheduling Coordinator, a Scheduling Coordinator Applicant must submit a written application to the ISO by mail, fax, e-mail or in person. A Scheduling Coordinator Applicant may retrieve the application and necessary information from the ISO Home Page.

4.5.1.1.2 ISO Information.

The ISO will provide the following information, in its most current form, on the ISO Home Page. Upon a request by a Scheduling Coordinator Applicant, the ISO will send the following information by mail:

(a) the Scheduling Coordinator Application Form (including the ISO Application File Template, which is Appendix T);

(b) the ISO Tariff and ISO Protocols;

(c) Interim Black Start Agreement;

(d) historical ISO charges (Note: prior to January 2, 1998, estimated ISO charges) including, but not limited to, charges for purchased Ancillary Services, ISO Grid Management Charge, ISO Grid Operations Charge, Imbalance Energy market charges, and Usage Charges to assist the Scheduling Coordinator Applicant in determining the Financial Security Amount the Scheduling Coordinator Applicant must provide; and

(e) a pro forma letter of understanding for payment for Scheduling Coordinator Applicants with Unsecured Credit Limits, guaranty, letter of credit and escrow agreement for the Financial Security Amount, all of which will be in a form acceptable to the ISO.

4.5.1.1.3 Duplicate Information.

If two or more Scheduling Coordinators apply simultaneously to register with the ISO for a single meter or Meter Point for an ISO Metered Entity or if an Scheduling Coordinator applies to register with the ISO for a meter or Meter Point for an ISO Metered Entity for which an Scheduling Coordinator has already registered, the ISO will return the application with an explanation that only one Scheduling Coordinator may register with the ISO for the meter or Meter Point in question and that an Scheduling Coordinator has

4.5.1.1.8.1 Approval or Rejection Letter.

(a) If the ISO approves the application, it will send an approval letter with a signed Scheduling Coordinator Agreement for the Scheduling Coordinator Applicant's signature and any required software licensing agreement.

(b) If the ISO rejects the application, the ISO will send a rejection letter stating one or more of the following grounds:

i. incomplete information;

ii. non-compliance with security requirements;

iii. non-compliance with third party contractual obligations;

iv. non-compliance with technical requirements; or

v. non-compliance with any other ISO Tariff requirements.

Upon request, the ISO will provide guidance as to how the Scheduling Coordinator Applicant can cure the grounds for the rejection.

4.5.1.1.8.2 Time for Processing Application.

The ISO will make a decision whether to accept or reject the application within 14 days of receipt of the application. If more information is requested, the ISO will make a final decision within 14 days of the receipt of all outstanding or additional information requested.

4.5.1.1.9 Scheduling Coordinator Applicant's Response.

4.5.1.1.9.1 Scheduling Coordinator Applicant's Acceptance.

If the ISO accepts the application, the Scheduling Coordinator Applicant must return an executed Scheduling Coordinator Agreement, Meter Service Agreements, Interim Black Start Agreements and letter of credit, guaranty or escrow agreement for the Financial Security Amount, as applicable.

4.5.1.1.9.2 Scheduling Coordinator Applicant's Rejection.

4.5.1.1.11 Final Certification of Scheduling Coordinator Applicant.

The Scheduling Coordinator Applicant will become a Scheduling Coordinator when:

(a) its application has been accepted;

(b) it has entered into an Scheduling Coordinator Agreement, Meter Service Agreements and Interim Black Start Agreements, if applicable, with the ISO;

(c) the Scheduling Coordinator Applicant has met the financial requirements of ISO Tariff Section 12.1; and

(d) the Scheduling Coordinator Applicant has fulfilled all technical/operational requirements of ISO Tariff Section 4.5.4.1, Section 4.5.1.1.10.1, and the ISO Application File Template.

The ISO will not certify a Scheduling Coordinator Applicant as a Scheduling Coordinator until the Scheduling Coordinator Applicant has completed all the above referenced requirements to the ISO's satisfaction, at least 14 days before the commencement of service.

4.5.1.2 Scheduling Coordinator's Ongoing Obligations After Certification.

4.5.1.2.1 Scheduling Coordinator's Obligation to Report Changes.

4.5.1.2.1.1 Obligation to Report a Change in Filed Information.

Each Scheduling Coordinator has an ongoing obligation to inform the ISO of any changes to any of the information submitted by it to the ISO as part of the application process, including any changes to the additional information requested by the ISO and including but not limited to changes in its Credit Rating. Appendix T sets forth the procedures for changing the Scheduling Coordinator's information and timing of notifying the ISO of such changes.

4.5.1.2.1.2 Obligation to Report a Change in Credit Rating.

The Scheduling Coordinator has an ongoing obligation to inform the ISO within 3 Business Days of any change to its Credit Rating.

4.5.1.2.2 ISO's Response for Failure to Inform.

11.2.10 Payments Under Section 40.3.1Contracts.

The ISO shall calculate and levy charges for the recovery of costs incurred under contracts entered into by the ISO under the authority granted in Section 40.3.1 in accordance with Section 40.3.1.8 of this ISO Tariff.

11.2.11 Obligation for FERC Annual Charges.

11.2.11.1 Each Scheduling Coordinator shall be obligated to pay for the FERC Annual Charges for its use of the ISO Controlled Grid to transmit electricity, including any use of the ISO Controlled Grid through Existing Contracts scheduled by the Scheduling Coordinator. Any FERC Annual Charges to be assessed by FERC against the ISO for such use of the ISO Controlled Grid shall be assessed against Scheduling Coordinators at the FERC Annual Charge Recovery Rate, as determined in accordance with this Section 11.2.11. Such assessment shall be levied monthly against all Scheduling Coordinators based upon each Scheduling Coordinator's metered Demand and exports.

11.2.11.2 Scheduling Coordinators may elect, each year, to pay the FERC Annual Charges assessed against them by the ISO either on a monthly basis or an annual basis. Scheduling Coordinators that elect to pay FERC Annual Charges on a monthly basis shall make payment for such charges within five (5) Business Days after issuance of the monthly invoice. The FERC Annual Charges will be issued to Market Participants once a month, on the first business day after the final market and Grid Management Charge invoices are issued for the trade month. Once the final FERC Annual Charge Recovery Rate is received from FERC in the Spring/Summer of the following year, a supplemental invoice will be issued. Scheduling Coordinators that elect to pay FERC Annual Charges on an annual basis shall make payment for such charges within five (5) Business Days after the ISO issues such supplemental invoice. Scheduling Coordinators that elect to pay FERC Annual Charges on an annual basis shall maintain either an Unsecured Credit Limit or shall maintain Financial Security in accordance with Section 12.1.

If the ISO Reserve Account is drawn upon, the ISO shall as soon as possible thereafter take any necessary steps against the defaulting Scheduling Coordinator, including making any calculations or taking any other appropriate action, to replenish the ISO Reserve Account including drawing on any credit support provided by the defaulting Scheduling Coordinator pursuant to Section 12.1 of this ISO Tariff or serving demands on any defaulting Scheduling Coordinators with an Unsecured Credit Limit.

The proceeds of drawings under any line of credit or other credit facility of the ISO Reserve Account shall be held on trust for ISO Creditors. If the Reserve Account is replenished as provided for in 11.8.5.2.1, any credits shall be held on trust for all ISO Creditors.

11.8.5.2.1 Replenishing the ISO Reserve Account Following Payment Default.

If the ISO has debited the ISO Reserve Account then:

(a) If, after the ISO has debited the ISO Reserve Account on a Payment Date, the ISO Bank receives a remittance from an ISO Debtor which has not been (but should have been, if it had been received on a timely basis) credited to the ISO Clearing Account by 10:00 am on the Payment Date and which required the debiting of the ISO Reserve Account, such remittance shall be credited to the ISO Reserve Account.

(b) The proceeds of any enforcement of Security and/or amounts recovered under proceedings shall be credited to the ISO Reserve Account.

(c) If after taking reasonable action the ISO determines that the Default Amount (or any part) and/or Interest cannot be recovered, such amounts shall be deemed to be owing by those Market Participants who were ISO Creditors on the relevant Payment Date pro rata to the net payments they received on that Payment Date and shall be accounted for by way of a charge in the next Settlement Statements of those ISO Creditors. Such charge shall be credited to the Reserve Account.

12 CREDITWORTHINESS.

12.1 Credit Requirements.

The creditworthiness requirements in this section apply to the ISO's acceptance of Schedules, to all transactions in an ISO Market, to the payment of charges pursuant to the ISO Tariff (including the Grid Management Charge), and to establish credit limits for participation in any ISO auction of FTRs. Each Market Participant (including each Scheduling Coordinator, UDC, or MSS) or FTR Bidder shall secure its financial transactions with the ISO (including its participation in any auction of FTRs) by maintaining an Unsecured Credit Limit and/or by posting Financial Security, the level of which constitutes the Market Participant's or FTR Bidder's Financial Security Amount. For each Market Participant or FTR Bidder, the sum of its Unsecured Credit Limit and its Financial Security Amount shall represent its Aggregate Credit Limit. Each Market Participant or FTR Bidder shall have the responsibility to maintain an Aggregate Credit Limit that is at least equal to its Estimated Aggregate Liability.

12.1.1 Unsecured Credit Limit.

Each Market Participant or FTR Bidder requesting an Unsecured Credit Limit shall submit an application to the ISO in the form specified on the ISO Home Page. The ISO shall determine the Unsecured Credit Limit for each Market Participant or FTR Bidder in accordance with the procedures set forth in the ISO Credit Policy & Procedures Guide posted on the ISO Home Page. The maximum Unsecured Credit Limit for any Market Participant or FTR Bidder shall be $250 million, or a lesser maximum Unsecured Credit Limit determined by the ISO Governing Board, in its discretion, and posted on the ISO Home Page. In accordance with the procedures described in the ISO Credit Policy & Procedures Guide, each Market Participant or FTR Bidder requesting or maintaining an Unsecured Credit Limit is required to submit to the ISO or its agent financial statements and other information related to its overall financial health as directed by the ISO. Each Market Participant or FTR Bidder is responsible for the timely submission of its latest financial statements as well as other information that may be reasonably necessary for the ISO to conduct its evaluation. As part of the credit evaluation process, the ISO may also rely on Nationally Recognized Statistical Rating Organizations as defined by the U.S. Securities and Exchange

Commission, other third-party credit assessment tools and services, and the general and/or financial press. As a result of the credit evaluation, a Market Participant or FTR Bidder may be given an Unsecured Credit Limit by the ISO or denied an Unsecured Credit Limit with the ISO.

12.1.1.1 Determination of Unsecured Credit Limits for Affiliates.

If any Market Participant or FTR Bidder requesting or maintaining an Unsecured Credit Limit is affiliated with one or more other entities subject to the credit requirements of this Section 12, the ISO may consider the overall creditworthiness and financial condition of such Affiliates when determining the applicable Unsecured Credit Limit. The ISO may determine that the maximum Unsecured Credit Limit specified in Section 12.1.1 applies to the combined activity of such Affiliates.

12.1.1.2 Notification of Material Change in Financial Condition.

Each Market Participant or FTR Bidder shall notify the ISO in writing of a Material Change in Financial Condition, within five (5) Business Days of when the Material change in Financial Condition is known or reasonably should be known by the Market Participant or FTR Bidder. The provision to the ISO of a copy of a Form 10-K, 10-Q, or Form 8-K filed with the U.S. Securities and Exchange Commission shall satisfy the requirement of notifiying the ISO of such Material Change in Financial Condition.

12.1.1.3 Transition from Credit Provisions that Were in Effect Prior to the Effective Date of this Section 12.1.1, *et seq.*

Each Market Participant or FTR Bidder that, prior to the effective date of this Section 12.1.1, *et seq.*, maintained an "Approved Credit Rating" with respect to market and/or Grid Management Charge obligations, shall be assigned a maximum Unsecured Credit Limit of $250 million for a period not to exceed thirty (30) days. Such thirty-day period shall start on the date the ISO issues a market notice stating that FERC has issued an order making Section 12.1.1, *et seq.* effective. Prior to or during such thirty-day period, each Market Participant or FTR Bidder maintaining an "Approved Credit Rating" as described herein shall submit to the ISO the information that is required for the ISO to make a credit evaluation regarding the Market Participant or FTR Bidder as described in Section 12.1.1. If the Market Participant or FTR Bidder does not submit the required information within the thirty-day period described herein, the ISO shall assign an Unsecured Credit Limit of $0 to the Market Participant or FTR Bidder until the required information has been submitted.

Each Market Participant or FTR Bidder that, prior to the effective date of this Section 12.1.1, *et seq.*, did *not maintain an* "Approved Credit Rating" *with respect to market and/or* Grid Management Charge obligations, shall be assigned an Unsecured Credit Limit of $0 until the Market Participant or FTR Bidder submits to the ISO the information that is required for the ISO to make a credit evaluation regarding the Market Participant or FTR Bidder as described in Section 12.1.1.

12.1.2 Financial Security and Financial Security Amount.

A Market Participant or FTR Bidder that does not have an Unsecured Credit Limit, or that has an Unsecured Credit Limit that is less than its Estimated Aggregate Liability, shall post Financial Security that is acceptable to the ISO and that is sufficient to ensure that its Aggregate Credit Limit (*i.e.*, the sum of its Unsecured Credit Limit and Financial Security Amount) is equal to or greater than its Estimated Aggregate Liability. The Financial Security posted by a Market Participant or FTR Bidder may be any combination of the following types of Finanical Security provided in favor of the ISO and notified to the ISO under Section 12.3:

(a) an irrevocable and unconditional letter of credit issued by a bank or financial institution that is reasonably acceptable to the ISO;

(b) an irrevocable and unconditional surety bond issued by an insurance company that is reasonably acceptable to the ISO;

(c) an unconditional and irrevocable guaranty issued by a company that is reasonably acceptable to the ISO;

(d) a cash deposit standing to the credit of the ISO in an interest-bearing escrow account maintained at a bank or financial institution that is reasonably acceptable to the ISO;

(e) a certificate of deposit in the name of the ISO issued by a bank or financial institution that is reasonably acceptable to the ISO;

(f) a payment bond certificate in the name of the ISO issued by a bank or financial institution that is reasonably acceptable to the ISO; or

(g) a prepayment to the ISO.

Financial Security instruments as listed above shall be in such form as the ISO may reasonably require from time to time by notice to Market Participants or FTR Bidders, or in such other form as has been evaluated and approved as reasonably acceptable by the ISO. The ISO shall publish and maintain standardized forms related to the types of Financial Security listed above on the ISO Home Page. The ISO shall require the use of standardized forms of Financial Security to the greatest extent possible.

12.1.2.1 Process for Evaluating Requests to Use Non-Standardized Forms of Financial Security.

A Market Participant or FTR Bidder that seeks permission to use a form for Financial Security other than one or more of the standardized forms posted on the ISO Home Page shall seek such permission in a written request to the ISO that explains the basis for the use of such non-standardized form. The ISO shall have ten (10) Business Days from receipt of such request to evaluate it and determine whether it will be approved as reasonably acceptable. If the ISO does not respond to such request within the ten (10) Business Day period, the request shall be deemed to have been denied. Until and unless the ISO approves the use of a non-standardized form for Financial Security, the Market Participant or FTR Bidder that submitted such request shall be required to use one of the standardized forms for Financial Security described in this Section 12.1.2.

12.1.2.2 Expiration of Financial Security.

Each Market Participant or FTR Bidder shall ensure that the financial instruments it uses for the purpose of providing Financial Security will not expire and thereby cause the Market Participant's or FTR Bidder's Aggregate Credit Limit to fall below the Market Participant's or FTR Bidder's Estimated Aggregate Liability. The ISO may treat a financial instrument that does not have an automatic renewal provision and that is not renewed or replaced within thirty (30) days of its date of expiration as being out of compliance with the standards for Financial Security contained in this Section 12 and may deem the value of such financial instrument to be zero, and may draw upon such Financial Security prior to its stated expiration if deemed necessary by the ISO.

12.1.2.3 Risk of Loss of Financial Security Amounts Held and Invested by the ISO.

In accordance with the ISO's investment policy, the ISO will invest each Financial Security Amount of a Market Participant or FTR Bidder only in bank accounts, high-quality money market accounts, and/or U.S. Treasury/Agency securities unless a specific written request is received from the Market Participant or FTR Bidder for a different type of investment and the ISO provides its written consent to such alternative investment. A Market Participant or FTR Bidder that provides a Financial Security Amount that is held and invested by the ISO on behalf of the Market Participant or FTR Bidder will bear all risks that such Financial Security Amount will incur a loss of principal and/or interest as a result of the ISO's investment of such Financial Security Amount.

12.1.3 Self-Supply of UDC Demand.

Notwithstanding anything to the contrary in the ISO Tariff, a Scheduling Coordinator or UDC that is an Original Participating Transmission Owner or is a Scheduling Coordinator for an Original Participating Transmission Owner shall not be precluded by Section 12.3 from scheduling transactions that serve a UDC's Demand from –

(1) a resource that the UDC owns; and

(2) a resource that the UDC has under contract to serve its Demand.

12.1.4 Allocation of Aggregate Credit Limit for FTR Auction Participation.

An FTR Bidder may elect to allocate a portion of its Aggregate Credit Limit toward satisfying the credit requirements for participating in auctions of FTRs, as set forth in Section 36.2.6.

12.1.5 Estimated Aggregate Liability.

The ISO will periodically calculate the Estimated Aggregate Liability of each Market Participant and FTR Bidder, based on all charges and settlement amounts for which such Market Participant or FTR Bidder is liable or reasonably anticipated by the ISO to be liable for pursuant to the ISO Tariff. The Estimated Aggregate Liability for each Market Participant or FTR Bidder shall be determined and applied by the ISO consistent with the procedures set forth in the ISO Credit Policy & Procedures Guide posted on the ISO Home Page. The ISO shall upon request provide each Market Participant or FTR Bidder with information concerning the basis for the ISO's determination of its Estimated Aggregate Liability, and the ISO's determination may be disputed in accordance with the procedures set forth in the ISO Credit Policy & Procedures Guide. The ISO shall compare each Market Participant's or FTR Bidder's Estimated Aggregate Liability against its Aggregate Credit Limit on a periodic basis.

12.2 Review of Creditworthiness.

The ISO may review the creditworthiness of any Market Participant or FTR Bidder which delays or defaults in making payments due under the ISO Tariff and, as a consequence of that review, may require such Market Participant or FTR Bidder, whether or not it has an Unsecured Credit Limit, to provide credit support in the form of any of the following types of Financial Security:

(a) an irrevocable and unconditional letter of credit by a bank or financial institution reasonably acceptable to the ISO;

(b) a cash deposit standing to the credit of an interest-bearing escrow account maintained at a bank or financial institution designated by the ISO;

(c) an irrevocable and unconditional surety bond posted by an insurance company reasonably acceptable to the ISO;

(d) a payment bond certificate in the name of the ISO from a financial institution designated by the ISO; or

(e) a prepayment to the ISO.

The ISO may require the Market Participant or FTR Bidder to maintain such Financial Security for at least one (1) year from the date of such delay or default.

12.3 Posting and Release of Financial Security.

Each Market Participant or FTR Bidder required to provide a Financial Security Amount under Section 12.1.2 shall notify the ISO of the initial Financial Security Amount that it wishes to provide at least fifteen (15) days in advance and shall ensure that the ISO has received such

Financial Security Amount prior to the date the Market Participant commences activity through the ISO, or the date the FTR Bidder participates in the applicable auction of FTRs. A Market Participant or FTR Bidder may at any time increase its Financial Security Amount by providing additional Financial Security in accordance with Section 12.1.2. A Market Participant or FTR Bidder may request that its Financial Security Amount be reduced or released by making its request not fewer than fifteen (15) days prior to the date on which the reduction or release is requested to occur. The ISO shall evaluate the request and inform the Market Participant or FTR Bidder within ten (10) Business Days either that a reduction or release of the Financial Security Amount is permissible, that a reduction or release of the Financial Security Amount is impermissible, or that the ISO requires more information from the Market Participant or FTR Bidder in order to make its determination. The ISO may decline to reduce or release a Financial Security Amount or may release a lesser amount for any of the following reasons:

(a) The Estimated Aggregate Liability for the Market Participant or FTR Bidder cannot be accurately determined due to a lack of supporting settlement charge information.

(b) The most recent liabilities of the Market Participant or FTR Bidder are volatile to a significant degree and a reduction or release of the Financial Security Amount would present a high likelihood that, after the Financial Security Amount was reduced or released, the Estimated Aggregate Liability for the Market Participant or FTR Bidder, as calculated by the ISO, would exceed its Aggregate Credit Limit.

(c) The Market Participant has provided notice or otherwise demonstrated that it is terminating or significantly reducing its participation in the ISO markets. The ISO may retain a portion of the Financial Security Amount to ensure that the Market Participant is adequately secured with respect to pending liabilities that relate to settlement re-runs or other liabilities for which the Market Participant may be responsible under this ISO Tariff.

12.4 Calculation of Ongoing Financial Security Requirements.

Following the date on which a Market Participant commences trading, if the Market Participant's Estimated Aggregate Liability, as calculated by the ISO, at any time exceeds its Aggregate Credit Limit, the ISO shall direct the Market Participant to post an additional Financial Security Amount within five (5) Business Days that is sufficient to ensure that the Market Participant's Aggregate Credit Limit is at least equal to its Estimated Aggregate Liability. The ISO shall also notify a Market Participant if at any time its Estimated Aggregate Liability exceeds 90% of its Aggregate Credit Limit. For the purposes of calculating the Market Participant's Estimated Aggregate Liability, the ISO shall include (1) outstanding charges for Trading Days for which Settlement data is available, and (2) an estimate of charges for Trading Days for which Settlement data is not yet available. To estimate charges for Trading Days for which Settlement data is not yet available, the ISO will consider available historical Settlement data, and other available operational and market data as described in the ISO Credit Policy & Procedures Guide posted on the ISO Home Page.

12.5 ISO Enforcement Actions Regarding Under-Secured Market Participants.

Following the date on which a Market Participant commences trading, if a Market Participant's Estimated Aggregate Liability, as calculated by the ISO, at any time exceeds its Aggregate Credit Limit, the ISO may take any or all of the following actions:

(a) The ISO may withhold a pending payment distribution.

(b) The ISO may limit trading, which may include rejection of Schedules and/or limiting other ISO market activity. In such case, the ISO shall notify the Market Participant of its action and the Market Participant shall not be entitled to submit further Schedules to the ISO until the Market Participant posts an additional Financial Security Amount that is sufficient to ensure that the Market Participant's Aggregate Credit Limit is at least equal to its Estimated Aggregate Liability.

(c) The ISO may require the Market Participant to post an additional Financial Security Amount in lieu of an Unsecured Credit Limit for a period of time.

(d) The ISO may restrict, suspend, or terminate a Market Participant's Service Agreement.

In addition, the ISO may restrict or suspend a Market Participant's right to schedule or require the Market Participant to increase its Financial Security Amount if at any time such Market Participant's potential additional liability for Imbalance Energy and other ISO charges is determined by the ISO to be excessive by comparison with the likely cost of the amount of Energy scheduled by the Market Participant.

Protocol) for submission of Schedules. However, a Scheduling Coordinator can also initiate the stage two validation at any time prior to that deadline, as described in more detail in the Scheduling Protocol. If the Scheduling Coordinator adds a new Schedule or modifies an existing Schedule, that Schedule must be re-validated. Scheduling Coordinators must comply with the ISO Data Templates and Validation Rules document, which contains the validation criteria for Balanced Schedules.

30.4.1.1 Stage One Validation.

During stage one validation, each incoming Schedule will be validated to verify proper content, format and syntax. The ISO will check that the Scheduling Coordinator had not exceeded its Aggregate Credit Limit and verify that the Scheduling Coordinator is certified in accordance with the ISO Tariff. The ISO will further verify that the Scheduling Coordinator has inputted valid Generating Unit and Demand location identification. Scheduled Reliability Must-Run Generation will be verified against the contract reference numbers in the ISO's Scheduling Coordinator database. A technical validation will be performed verifying that a scheduled Generating Unit's output is not beyond it's declared capacity and/or operating limits. If there is an error found during stage one validation, the Scheduling Coordinator will be notified immediately through WEnet. The Scheduling Coordinator can then look at the notification messages to review the detailed list of errors, make changes, and resubmit the Schedule if it is still within the ISO's timing requirements. Additionally, if the ISO detects an invalid contract usage (of either Existing Contract rights or Firm Transmission Rights), the ISO will issue an error message in similar manner to the Scheduling Coordinator and allow the Scheduling Coordinator to view the message(s), to make changes, and to resubmit the contract usage template(s) if it is still within the ISO's timing requirements. The Scheduling Coordinator is also notified of successful validation via WEnet.

30.4.1.2 Stage Two Validation.

During stage two validation, Schedules will be checked to determine whether each Scheduling Coordinator's aggregate Generation and external imports (adjusted for Transmission Losses) and Inter-Scheduling Coordinator Energy Trades (whether purchases or sales) equals the Scheduling Coordinator's aggregate Demand Forecast, including external exports. The Scheduling Coordinator must take into account the applicable Generation Meter Multipliers (GMMs). The Scheduling Coordinator will

Administrative Price	The price set by the ISO in place of a Market Clearing Price when, by reason of a System Emergency, the ISO determines that it no longer has the ability to maintain reliable operation of the ISO Controlled Grid relying solely on the economic Dispatch of Generation. This price will remain in effect until the ISO considers that the System Emergency has been contained and corrected.
Adverse System Impact	The negative effects due to technical or operational limits on conductors or equipment being exceeded that may compromise the safety and reliability of the electric system.
Affected System	An electric system other than the ISO Controlled Grid that may be affected by the proposed interconnection, including the Participating TOs' electric systems that are not part of the ISO Controlled Grid.
Affected System Operator	The entity that operates an Affected System.
Affiliate	An entity, company or person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with the subject entity, company, or person.
AGC (Automatic Generation Control)	Generation equipment that automatically responds to signals from the ISO's EMS control in real time to control the power output of electric generators within a prescribed area in response to a change in system frequency, tie-line loading, or the relation of these to each other, so as to maintain the target system frequency and/or the established interchange with other areas within the predetermined limits.
Aggregate Credit Limit	The sum of a Market Participant's or FTR Bidder's Unsecured Credit Limit and its Financial Security Amount, as provided for in Section 12 of the ISO Tariff.
Alert Notice	A Notice issued by the ISO when the operating requirements of the ISO Controlled Grid are marginal because of Demand exceeding forecast, loss of major Generation, or loss of transmission capacity that has curtailed imports into the ISO Control Area, or if the Hour-Ahead Market is short on scheduled Energy and Ancillary Services for the ISO Control Area.

Ancillary Services Regulation, Spinning Reserve, Non-Spinning Reserve, Replacement Reserve, Voltage Support and Black Start together with such other interconnected operation services as the ISO may develop in cooperation with Market Participants to support the transmission of Energy from Generation resources to Loads while maintaining

	reliable operation of the ISO Controlled Grid in accordance with Good Utility Practice.
Ancillary Service Provider	A Participating Generator or Participating Load who is eligible to provide an Ancillary Services.
Annual Peak Demand Forecast	A Demand Forecast of the highest Hourly Demand in any hour in a calendar year, in MW.
Applicable Reliability Criteria	The reliability standards established by NERC, WECC, and Local Reliability Criteria as amended from time to time, including any requirements of the NRC.
Applicants	Pacific Gas and Electric Company, San Diego Gas & Electric Company, and Southern California Edison Company and any others as applicable.

Approved Load Profile	Local Regulatory Authority approved Load profiles applied to cumulative End-Use Meter Data in order to allocate consumption of Energy to Settlement Periods.
Approved Maintenance Outage	A Maintenance Outage which has been approved by the ISO through the ISO Outage Coordination Office.
"Area Control Error (ACE)"	The sum of the instantaneous difference between the actual net interchange and the scheduled net interchange between the ISO Control Area and all adjacent Control Areas and the ISO Control Area's frequency correction and time error correction obligations.
Authorized Users	A person or an entity identified as an authorized user in a meter service agreement between the ISO and an ISO Metered Entity or a meter service agreement between the ISO and a SC.
Automatic Mitigation Procedure (AMP)	The market power mitigation procedure described in Attachment A to Appendix P.
Available Transfer Capacity	For a given transmission path, the capacity rating in MW of the path established consistent with ISO and WECC transmission capacity

Energy Export	For purposes of calculating the Grid Management Charge, Energy included in an interchange Schedule submitted to the ISO, or dispatched by the ISO, to serve a Load located outside the ISO's Control Area, whether the Energy is produced by a Generator in the ISO Control Area or a resource located outside the ISO's Control Area.
Entitlements	The right of a Participating TO obtained through contract or other means to use another entity's transmission facilities for the transmission of Energy.
Environmental Dispatch	Dispatch designed to meet the requirements of air quality and other environmental legislation and environmental agencies having authority or jurisdiction over the ISO.
Estimated Aggregate Liability	The sum of a Market Participant's or FTR Bidder's known and reasonably estimated potential liabilities for a specified time period arising from charges described in the ISO Tariff, as provided for in Section 12 of the ISO Tariff.
Ex Post GMM	GMM that is calculated utilizing the real-time Power Flow Model in accordance with Section 27.2.1.2.1.2.
Ex Post Price	The Hourly Ex Post Price, the Dispatch Interval Ex Post Price, the Resource-Specific Settlement Interval Ex Post Price, or the Zonal Settlement Interval Ex Post Price.
Ex Post Transmission Loss	Transmission Loss that is calculated based on Ex Post GMM.
Existing Contracts	The contracts which grant transmission service rights in existence on the ISO Operations Date (including any contracts entered into pursuant to such contracts) as may be amended in accordance with their terms or by agreement between the parties thereto from time to time.
Existing High Voltage Facility	A High Voltage Transmission Facility of a Participating TO that was placed in service on or before the Transition Date defined in Section 4.2 of Schedule 3 of Appendix F.
Existing Rights	Those transmission service rights defined in Section 16.2.1.1 of the ISO Tariff.

Facility Owner	An entity owning transmission, Generation, or distribution facilities connected to the ISO Controlled Grid.
Facility Study	An engineering study conducted by a Participating TO to determine required modifications to the Participating TO's transmission system, including the cost and scheduled completion date for such

	modifications that will be required to provide needed services.
Facility Study Agreement	An agreement between a Participating TO and either a Market Participant, Project Sponsor, or identified principal beneficiaries pursuant to which the Market Participants, Project Sponsor, and identified principal beneficiaries agree to reimburse the Participating TO for the cost of a Facility Study.
Fed-Wire	The Federal Reserve Transfer System for electronic funds transfer.
FERC	The Federal Energy Regulatory Commission or its successor.
FERC Annual Charges	Those charges assessed against a public utility by the FERC pursuant to 18 C.F.R. § 382.201 and any related statutes or regulations, as they may be amended from time to time.
FERC Annual Charge Recovery Rate	The rate to be paid by Scheduling Coordinators for recovery of FERC Annual Charges assessed against the ISO for transactions on the ISO Controlled Grid.
FERC Annual Charge Trust Account	An account to be established by the ISO for the purpose of maintaining funds collected from Scheduling Coordinators for FERC Annual Charges and disbursing such funds to the FERC.
Final Approval	A statement of consent by the ISO Control Center to initiate a scheduled Outage.
Final Day-Ahead Schedule	The Day-Ahead Schedule which has been approved as feasible and consistent with all other Schedules by the ISO based upon the ISO's Day-Ahead Congestion Management procedures.
Final Hour-Ahead Schedule	The Hour-Ahead Schedule of Generation and Demand that has been approved by the ISO as feasible and consistent with all other Schedules based on the ISO's Hour-Ahead Congestion Management procedures.
Final Invoice	The invoice due from a RMR Owner to the ISO at termination of the RMR Contract.
Final Schedule	A Schedule developed by the ISO following receipt of a Revised Schedule from a Scheduling Coordinator.
Final Settlement Statement	The restatement or recalculation of the Preliminary Settlement Statement by the ISO following the issue of that Preliminary Settlement Statement.

Financial Security	Any of the types of financial instruments listed in Section 12 of the ISO Tariff that are posted by a Market Participant or FTR Bidder.
Financial Security Amount	The level of Financial Security posted in accordance with Section 12 of the ISO Tariff by a Market Participant or FTR Bidder.
Forbidden Operating	The operating region of a resource wherein the resource cannot

	separately, in relation to its meters at points of connection of its Service Area with the systems of other utilities.
ISO Metered Entity Meter Service Agreements	The meter service agreements between the ISO and ISO Metered Entities.
ISO Operations Date	The date on which the ISO first assumes Operational Control of the ISO Controlled Grid.
ISO Outage Coordination Office	The office established by the ISO to coordinate Maintenance Outages in accordance with Section 9.3 of the ISO Tariff.
ISO Payments Calendar	A calendar published by the ISO showing the dates on which Settlement Statements will be published by the ISO and the Payment Dates by which invoices issued under the ISO Tariff must be paid.
ISO Protocols	The rules, protocols, procedures and standards promulgated by the ISO (as amended from time to time) to be complied with by the ISO Scheduling Coordinators, Participating TOs and all other Market Participants in relation to the operation of the ISO Controlled Grid and the participation in the markets for Energy and Ancillary Services in accordance with the ISO Tariff.
ISO Register	The register of all the transmission lines, associated facilities and other necessary components that are at the relevant time being subject to the ISO's Operational Control.
ISO Reserve Account	The account established for the purpose of holding cash deposits which may be used in or towards clearing the ISO Clearing Account.
ISO Surplus Account	The account established by the ISO pursuant to Section 11.8.5.3.
ISO Tariff	The California Independent System Operator Corporation Operating Agreement and Tariff, dated March 31, 1997, as it may be modified from time to time.

Master File	A file containing information regarding Generating Units, Loads and other resources.
Material Change in Financial Condition	A change in or potential threat to the financial condition of a Market Participant or FTR Bidder that increases the risk that the Market Participant or FTR Bidder will be unlikely to meet some or all of its financial obligations. The types of Material Change in Financial Condition include but are not limited to the following: (a) a credit agency downgrade; (b) being placed on a credit watch list by a major rating agency; (c) a bankruptcy filing; (d) involvency; (e) the filing of a material lawsuit that could significantly and adversely affect past, current, or future financial results; or (f) any change in the financial condition of the Market Participant or FTR Bidder which exceeds a five percent reduction in the Market Participant's or FTR Bidder's tangible net worth for the Market Participant or FTR Bidder's preceding fiscal year, calculated in accordance with generally accepted accounting practices.
Material Modification	Those modifications that have a material impact on the cost or timing of any Interconnection Request or any other valid interconnection request with a later queue priority date.
MDAS	The ISO's revenue meter data acquisition and processing system.
Meter Data	Energy usage data collected by a metering device or as may be otherwise derived by the use of Approved Load Profiles.
Meter Points	Locations on the ISO Controlled Grid at which the ISO requires the collection of Meter Data by a metering device.

Metered Control Area Load	For purposes of calculating and billing the Grid Management Charge, Metered Control Area Load is: (a) all metered Demand for Energy of Scheduling Coordinators for the supply of Loads in the ISO's Control Area, plus (b) all Energy for exports by Scheduling Coordinators from the ISO Control Area; less (c) Energy associated with the Load of a retail customer of a Scheduling Coordinator, UDC, or MSS that is served by a Generating Unit that: (i) is located on the same site as the customer's Load or provides service to the customer's Load through arrangements as authorized by Section 218 of the California Public Utilities Code; (ii) is a qualifying small power production facility or qualifying cogeneration facility, as those terms are defined in FERC's regulations implementing Section 201 of the Public Utility Regulatory Policies Act of 1978; and (iii) the customer secures Standby Service from a Participating TO under terms approved by a Local Regulatory Authority or FERC, as applicable, or the customer's Load can be curtailed concurrently with an outage of the Generating Unit.
Meter Data Exchange Format	The format for submitting Meter Data to the ISO which will be published by the ISO on the ISO Home Page or available on request to the Meter and Data Acquisition Manager, ISO Client Service Department.

Uninstructed Deviation	A deviation from the resources' Dispatch Operating Point.
Uninstructed Deviation Penalty	The penalty as set forth in Section 11.2.4.1.2 of this ISO Tariff.
Uninstructed Imbalance Energy	The real-time change in Generation or Demand other than that instructed by the ISO or which the ISO Tariff provides will be paid at the price for Uninstructed Imbalance Energy.
Unit Commitment	The process of determining which Generating Units will be committed (started) to meet Demand and provide Ancillary Services in the near future (e.g., the next Trading Day).
Unsecured Credit Limit	The level of credit established for a Market Participant or FTR Bidder that is not secured by any form of Financial Security, as provided for in Section 12 of the ISO Tariff.
Usage Charge	The amount of money, per 1 kW of scheduled flow, that the ISO charges a Scheduling Coordinator for use of a specific Congested Inter-Zonal Interface during a given hour.
Validation, Estimation and Editing (VEE)	Applies to Meter Data directly acquired by the ISO. Validation is the process of checking the data to ensure that it is contiguous, within pre-defined limits and has not been flagged by the meter. Estimation and Editing is the process of replacing or making complete Meter Data by using data from redundant meters, schedules, PMS or, if necessary, statistical estimation.
Value Added Network (VAN)	A data communications service provider that provides, stores and forwards electronic data delivery services within its network and to subscribers on other VANs. The data is mostly EDI type messages.
Voltage Limits	For all substation busses, the normal and post-contingency Voltage Limits (kV). The bandwidth for normal Voltage Limits must fall within the bandwidth of the post-contingency Voltage Limits. Special voltage limitations for abnormal operating conditions such as heavy or light Demand may be specified.
Voltage Support	Services provided by Generating Units or other equipment such as shunt capacitors, static var compensators, or synchronous condensers that are required to maintain established grid voltage criteria. This service is required under normal or System Emergency conditions.

Waiver Denial Period	The period determined in accordance with Section 40.1.6.
Warning Notice	A Notice issued by the ISO when the operating requirements for the ISO Controlled Grid are not met in the Hour-Ahead Market, or the quantity of Regulation, Spinning Reserve, Non-Spinning Reserve,

The information provided for this application will be treated as confidential information

PART A

SCHEDULING COORDINATOR APPLICATION FORM

This application is for approval as a Scheduling Coordinator ("SC") by the California Independent System Operator Corporation ("ISO") in accordance with the ISO Tariff.

I. Administrative Requirements

SC Applicant's Legal Name:

____

Address of principal place of business:

____

____

____

Authorized Representative: ____

Address: ______________________________________

____

Phone: ______________________________________

Fax: ______________________________________

E-mail: ______________________________________

Type of entity: ____

(Municipal utility, power marketer, investor owned utility, federal or state entity or other)

State of Incorporation or Partnership: ______________________

Proposed commencement date for service: __________________

II. Scheduling Coordinator Customer Information

2.1 The information required under Part C, the ISO Application File Template, must be provided for represented Scheduling Coordinator Metered Entities, which are Generators. The Scheduling Coordinator Applicant must submit all requested information prior to final certification, which must occur fourteen (14) days before the commencement of service.

2.2 Information for Scheduling Coordinator Metered Entities, which are End Users or Eligible Customers, must be kept in a standard business format based on generally accepted accounting principals. The ISO shall have the right to inspect and audit a Scheduling Coordinator's accounts and files relating to its Scheduling Coordinator Metered Entities after giving two Business Days notice in writing.

2.3 The Scheduling Coordinator Applicant must submit a list of all ISO Metered Entities, which it will represent.

III. Security Requirement

3.1 The Scheduling Coordinator Applicant will submit a completed credit application to receive an Unsecured Credit Limit as set forth in the ISO Tariff and the ISO Credit Policy & Procedures Guide: (yes/no).

The Scheduling Coordinator Applicant has submitted a completed credit application to receive an Unsecured Credit Limit as set forth in the ISO Tariff and the ISO Credit Policy & Procedures Guide: (yes/no). OR

3.2 The Scheduling Coordinator Applicant will provide Financial Security in a form listed in Section 12.1.2 of the ISO Tariff: (yes/no).

Acceptable forms of Financial Security include:

(a) an irrevocable and unconditional letter of credit issued by a bank or financial institution that is reasonably acceptable to the ISO;

(b) an irrevocable and unconditional surety bond issued by an insurance company that is reasonably acceptable to the ISO;

(c) an unconditional and irrevocable guaranty issued by a company that is reasonably acceptable to the ISO;

(d) a cash deposit standing to the credit of the ISO in an interest-bearing escrow account maintained at a bank or financial institution that is reasonably acceptable to the ISO;

(e) a certificate of deposit in the name of the ISO issued by a bank or financial institution that is reasonably acceptable to the ISO;

(f) a payment bond certificate in the name of the ISO issued by a bank or financial institution that is reasonably acceptable to the ISO; or

(g) any other form of security that has been evaluated and approved as reasonably acceptable by the ISO.

AND

3.3 The Scheduling Coordinator Applicant must provide its bank account information before final certification. The Scheduling Coordinator Applicant's bank must be capable of performing Fed-Wire System transfers.

IV. <u>Technical Requirements</u>

4.1 Does the Scheduling Coordinator Applicant have the computer hardware, software and communication capabilities for interface compatibility with the ISO system for data transmission, for electronic data interchange (EDI) and for Fed-Wire System transfer accounts? (yes / no) If no, please submit a proposed completion date to be fully operational so that an ISO staff site visit can be arranged.

4.2 For Loads and Generating Units located within the ISO Controlled Grid, does the Scheduling Coordinator Applicant have any scheduling restrictions imposed by the parties they represent? (yes / no) If yes, provide full details on a separate sheet of paper.

4.3 Does the Scheduling Coordinator Applicant have adequate staffing to operate a Scheduling Coordinator's operational facility twenty-four (24) hours a day for 365 days a year? (yes / no). If no, please submit a proposed completion date to be fully operational so that an ISO staff site visit can be arranged.

V. Third Party Contractual Requirements

5.1 The Scheduling Coordinator Applicant confirms that all of its Scheduling Coordinator Customers which are located within the ISO Controlled Grid and which should execute agreements with the ISO have entered into or will enter into, prior to the certification of the Scheduling Coordinator Applicant, all required agreements with the ISO to enable them to meet the requirements of the ISO Tariff: (yes / no).

(a) Represented Generators have signed Participating Generator Agreements: (yes / no).

(b) Represented UDCs have signed UDC Operating Agreements and Meter Service Agreements: (yes / no).

(c) Represented ISO Metered Entities have signed Meter Service Agreements: (yes / no).

(d) Wholesale Customers it will represent have warranted to the Scheduling Coordinato Applicant that they are eligible for wholesale transmission service pursuant to the provisions of the FPA Section 212(h): (yes / no).

(e) Each End-Use Customer it will represent which requests Direct Access service has warranted to the Scheduling Coordinator Applicant that the End-Use Customer is eligible for such service: (yes / no).

5.2 The SCHEDULING COORDINATORApplicant confirms that all of the parties which it represents as Scheduling Coordinator Customers have granted it all necessary agency authority, whether actual, implied or inherent, to enable the Scheduling Coordinator to perform all of its obligations under the ISO Tariff: (yes / no).

5.3 Notwithstanding 5.2, the Scheduling Coordinator confirms that it will have the primary responsibility, as the principal, for all Scheduling Coordinator payment obligations under the ISO Tariff : (yes / no).

VI. Additional Information and Obligations

6.1 The Scheduling Coordinator Applicant agrees to provide such further information to the ISO as the ISO may deem necessary to process the application and certify the Scheduling Coordinator Applicant as a Scheduling Coordinator now and on a continuing basis.

6.2 Subject to the ISO Tariff, the Scheduling Coordinator Applicant agrees to promptly report to the ISO within seven (7) Business Days or earlier any changes regarding the information provided by it referred to in the ISO Tariff and in the application with the exception of the security requirement data referred to in Part III of Part A in this Appendix which must be updated within three (3) Business Days. The Scheduling Coordinator shall be responsible if a failure to submit revised technical data more promptly extends the period during which schedules are rejected by the ISO.

6.3 The Scheduling Coordinator Applicant agrees to enclose herein the non-refundable application fee of $500 to cover the application processing costs, site visit and costs of providing ISO Tariff.

Please make check payable to:

The California Independent System Operator Corporation

6.4 Scheduling Coordinator Applicant agrees to promptly execute and return the Scheduling Coordinator Agreement, Meter Service Agreements, Interim Black Start Agreements, software licensing agreement, letter of understanding, letter of credit, guaranty, escrow agreement, as applicable, and Fed-Wire System bank account number, after receiving its application approval letter from the ISO.

6.5 Final certification is contingent upon Scheduling Coordinator Applicant fulfilling all financial and technical requirements as referenced in the ISO Tariff (including Part C of this Appendix, the ISO Application File Template).

Scheduling Coordinator Applicant certifies by its signature on this Application Form that:

ATTACHMENT B

4.5.1.1.2 ISO Information.

The ISO will provide the following information, in its most current form, on the ISO Home Page. Upon a request by a Scheduling Coordinator Applicant, the ISO will send the following information by mail:

(a) the Scheduling Coordinator Application Form (including the ISO Application File Template, which is Appendix T);

(b) the ISO Tariff and ISO Protocols;

(c) Interim Black Start Agreement;

(d) historical ISO charges (Note: prior to January 2, 1998, estimated ISO charges) including, but not limited to, charges for purchased Ancillary Services, ISO Grid Management Charge, ISO Grid Operations Charge, Imbalance Energy market charges, and Usage Charges to assist the Scheduling Coordinator Applicant in determining the ~~ISO~~Financial Security Amount the Scheduling Coordinator Applicant must provide; and

(e) a pro forma letter of understanding for payment for Scheduling Coordinator Applicants with ~~Approved~~Unsecured Credit Limits~~Ratings~~, guarant~~ee~~y, letter of credit and escrow agreement for the ~~ISO~~Financial Security Amount, all of which will be in a form acceptable to the ISO.

* * *

4.5.1.1.9 Scheduling Coordinator Applicant's Response.

4.5.1.1.9.1 Scheduling Coordinator Applicant's Acceptance.

If the ISO accepts the application, the Scheduling Coordinator Applicant must return an executed Scheduling Coordinator Agreement, Meter Service Agreements, Interim Black Start Agreements and letter of credit, guarant~~ee~~y or escrow agreement for the ~~ISO~~Financial Security Amount, as applicable.

* * *

4.5.1.2 Scheduling Coordinator's Ongoing Obligations After Certification.

4.5.1.2.1 Scheduling Coordinator's Obligation to Report Changes.

4.5.1.2.1.1 Obligation to Report a Change in Filed Information.

Each Scheduling Coordinator has an ongoing obligation to inform the ISO of any changes to any of the information submitted by it to the ISO as part of the application process, including any changes to the additional information requested by the ISO and including but not limited to changes in its Credit Rating. Appendix T sets forth the procedures for changing the Scheduling Coordinator's information and timing of notifying the ISO of such changes.

4.5.1.2.1.2 Obligation to Report a Change in Credit Rating.

The SC has an ongoing obligation to inform the ISO within 3 Business Days ~~if~~of any change to its ~~Approved~~ Credit Rating ~~has been reduced below the ISO requirements~~.

* * *

11.2.11.2 Scheduling Coordinators may elect, each year, to pay the FERC Annual Charges assessed against them by the ISO either on a monthly basis or an annual basis. Scheduling Coordinators that elect to pay FERC Annual Charges on a monthly basis shall make payment for such charges within five (5) Business Days after issuance of the monthly invoice. The FERC Annual Charges will be issued to Market Participants once a month, on the first business day after the final market and Grid Management Charge invoices are issued for the trade month. Once the final FERC Annual Charge Recovery Rate is received from FERC in the Spring/Summer of the following year, a supplemental invoice will be issued. Scheduling Coordinators that elect to pay FERC Annual Charges on an annual basis shall make payment for such charges within five (5) Business Days after the ISO issues such supplemental invoice. Scheduling Coordinators that elect to pay FERC Annual Charges on an annual basis shall maintain either an ~~Approved~~Unsecured Credit Limit~~Rating, as defined with respect to either payment of the Grid Management Charge, or payment of other charges,~~ or shall maintain Financial ~~s~~Security in accordance with Section 12.1.

* * *

11.8.5.2 Reserve Account.

The ISO Reserve Account shall be available to the ISO for the purpose of providing funds to clear the ISO Clearing Account in the event that there are insufficient funds in the ISO Clearing Account to pay ISO Creditors. If there are insufficient funds in the ISO Clearing Account to pay ISO Creditors and clear the account on any Payment Date, due to payment default by one or more ISO Debtors, the ISO shall transfer funds from the ISO Reserve Account to the ISO Clearing Account to clear it by close of banking business on that Payment Date pursuant to Section 11.12.2.2.

If the ISO Reserve Account is drawn upon, the ISO shall as soon as possible thereafter take any necessary steps against the defaulting Scheduling Coordinator, including making any calculations or taking any other appropriate action, to replenish the ISO Reserve Account including drawing on any credit support provided by the defaulting Scheduling Coordinator pursuant to Section 12.1 of this ISO Tariff or serving demands on any defaulting Scheduling Coordinators with an ~~Approved~~Unsecured Credit Limit~~Rating~~.

The proceeds of drawings under any line of credit or other credit facility of the ISO Reserve Account shall be held on trust for ISO Creditors. If the Reserve Account is replenished as provided for in 11.8.5.2.1, any credits shall be held on trust for all ISO Creditors.

* * *

12 CREDITWORTHINESS.

12.1 Credit Requirements.

The creditworthiness requirements in this section apply to the ISO's acceptance of Schedules, ~~and~~ to all transactions in an ISO Market, to the payment of charges pursuant to the ISO Tariff (including the Grid Management Charge), and to establish credit limits for participation in any ISO auction of FTRs. Each Market Participant (including each Scheduling Coordinator, UDC, or MSS) or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~ shall secure its financial transactions with the ISO (including its participation in any auction of FTRs)~~either~~ by maintaining an ~~Approved~~Unsecured Credit Limit~~Rating (which may differ for different types of transactions with the ISO)~~ and/or by posting Financial Security, the level of which constitutes the Market Participant's or FTR Bidder's Financial Security Amount. For each Market Participant or FTR Bidder, the sum of its Unsecured Credit Limit and its Financial Security Amount shall represent its Aggregate Credit Limit. Each Market Participant or FTR Bidder shall have the responsibility to maintain an Aggregate Credit Limit that is at least equal to its Estimated Aggregate Liability.

12.1.1 Unsecured Credit Limit.

Each Market Participant or FTR Bidder requesting an Unsecured Credit Limit shall submit an application to the ISO in the form specified on the ISO Home Page. The ISO shall determine the Unsecured Credit Limit for each Market Participant or FTR Bidder in accordance with the procedures set forth in the ISO Credit Policy & Procedures Guide posted on the ISO Home Page. The maximum Unsecured Credit Limit for any Market Participant or FTR Bidder shall be $250 million, or a lesser maximum Unsecured Credit Limit determined by the ISO Governing Board, in its discretion, and posted on the ISO Home Page. In accordance with the procedures described in the ISO Credit Policy & Procedures Guide, each Market Participant or FTR Bidder requesting or maintaining an Unsecured Credit Limit is required to submit to the ISO or its agent financial statements and other information related to its overall financial health as directed by the ISO. Each Market Participant or FTR Bidder is responsible for the timely submission of its latest financial statements as well as other information that may be reasonably necessary for the ISO to conduct its evaluation. As part of the credit evaluation process, the ISO may also rely on Nationally Recognized Statistical Rating Organizations as defined by the U.S. Securities and Exchange

Commission, other third-party credit assessment tools and services, and the general and/or financial press. As a result of the credit evaluation, a Market Participant or FTR Bidder may be given an Unsecured Credit Limit by the ISO or denied an Unsecured Credit Limit with the ISO.

12.1.1.1 Determination of Unsecured Credit Limits for Affiliates.

If any Market Participant or FTR Bidder requesting or maintaining an Unsecured Credit Limit is affiliated with one or more other entities subject to the credit requirements of this Section 12, the ISO may consider the overall creditworthiness and financial condition of such Affiliates when determining the applicable Unsecured Credit Limit. The ISO may determine that the maximum Unsecured Credit Limit specified in Section 12.1.1 applies to the combined activity of such Affiliates.

12.1.1.2 Notification of Material Change in Financial Condition.

Each Market Participant or FTR Bidder shall notify the ISO in writing of a Material Change in Financial Condition, within five (5) Business Days of when the Material Change in Financial Condition is known or reasonably should be known by the Market Participant or FTR Bidder. The provision to the ISO of a copy of a Form 10-K, 10-Q, or Form 8-K filed with the U.S. Securities and Exchange Commission shall satisfy the requirement of notifiying the ISO of such Material Change in Financial Condition.

12.1.1.3 Transition from Credit Provisions that Were in Effect Prior to the Effective Date of this Section 12.1.1, *et seq.*

Each Market Participant or FTR Bidder that, prior to the effective date of this Section 12.1.1, *et seq.*, maintained an "Approved Credit Rating" with respect to market and/or Grid Management Charge obligations, shall be assigned a maximum Unsecured Credit Limit of $250 million for a period not to exceed thirty (30) days. Such thirty-day period shall start on the date the ISO issues a market notice stating that FERC has issued an order making Section 12.1.1, *et seq.* effective. Prior to or during such thirty-day period, each Market Participant or FTR Bidder maintaining an "Approved Credit Rating" as described herein shall submit to the ISO the information that is required for the ISO to make a credit evaluation regarding the Market Participant or FTR Bidder as described in Section 12.1.1. If the Market Participant or FTR Bidder does not submit the required information within the thirty-day period described herein, the ISO shall assign an Unsecured Credit Limit of $0 to the Market Participant or FTR Bidder until the required information has been submitted.

Each Market Participant or FTR Bidder that, prior to the effective date of this Section 12.1.1, *et seq.*, did not maintain an "Approved Credit Rating" with respect to market and/or Grid Management Charge obligations, shall be assigned an Unsecured Credit Limit of $0 until the Market Participant or FTR Bidder submits to the ISO the information that is required for the ISO to make a credit evaluation regarding the Market Participant or FTR Bidder as described in Section 12.1.1.

12.1.2 Financial Security and Financial Security Amount.

A Market Participant or FTR Bidder that does not have an Unsecured Credit Limit, or that has an Unsecured Credit Limit that is less than its Estimated Aggregate Liability, shall post Financial Security that is acceptable to the ISO and that is sufficient to ensure that its Aggregate Credit Limit (*i.e.*, the sum of its Unsecured Credit Limit and Financial Security Amount) is equal to or greater than its Estimated Aggregate Liability. The Financial Security posted by a Market Participant or FTR Bidder may be any combination~~provide in favor of the ISO one~~ of the following ~~forms~~ types of Financial ~~s~~Security provided in favor of the ISO ~~for an amount to be determined by the Scheduling Coordinator, UDC or MSS~~ and notified to the ISO under Section 12.3:

(a) an irrevocable and unconditional letter of credit ~~confirm~~issued by a bank or financial institution that is reasonably acceptable to the ISO;

(b) an irrevocable and unconditional surety bond ~~post~~issued by an insurance company that is reasonably acceptable to the ISO;

(c) an unconditional and irrevocable guarant~~ee~~y issued by a company that is reasonably acceptable to the ISO~~which has and maintains an Approved Credit Rating~~;

(d) a cash deposit standing to the credit of the ISO in an interest-bearing escrow account maintained at a bank or financial institution that is reasonably acceptable to~~designated by~~ the ISO;

(e) a certificate of deposit in the name of the ISO ~~from~~issued by a bank or financial institution that is reasonably acceptable to~~designated by~~ the ISO;~~ or~~

(f) a payment bond certificate in the name of the ISO ~~from~~issued by a bank or financial institution that is reasonably acceptable to~~designated by~~ the ISO; or~~.~~

(g) a prepayment to the ISO.

~~Letters of credit, guarantees, surety bonds, payment bond certificates, escrow agreements and certificates of deposit~~Financial Security instruments as listed above ~~must cover all applicable outstanding and estimated liabilities under Section 12.3 and~~ shall be in such form as the ISO may reasonably require from time to time by notice to Market Participants or FTR Bidders,~~Scheduling Coordinators, UDCs or MSSs~~ or in such other form as has been evaluated and approved as reasonably acceptable by the ISO. The ISO shall publish and maintain standardized forms related to the types of Financial Security listed above on the ISO Home Page. The ISO shall require the use of standardized forms of Financial Security to the greatest extent possible.

12.1.2.1 Process for Evaluating Requests to Use Non-Standardized Forms of Financial Security.

A Market Participant or FTR Bidder that seeks permission to use a form for Financial Security other than one or more of the standardized forms posted on the ISO Home Page shall seek such permission in a written request to the ISO that explains the basis for the use of such non-standardized form. The ISO shall have ten (10) Business Days from receipt of such request to evaluate it and determine whether it will be approved as reasonably acceptable. If the ISO does not respond to such request within the ten (10) Business Day period, the request shall be deemed to have been denied. Until and unless the ISO approves the use of a non-standardized form for Financial Security, the Market Participant or FTR Bidder that submitted such request shall be required to use one of the standardized forms for Financial Security described in this Section 12.1.2.

12.1.2.2 Expiration of Financial Security.

Each Market Participant or FTR Bidder shall ensure that the financial instruments it uses for the purpose of providing Financial Security will not expire and thereby cause the Market Participant's or FTR Bidder's

Aggregate Credit Limit to fall below the Market Participant's or FTR Bidder's Estimated Aggregate Liability. The ISO may treat a financial instrument that does not have an automatic renewal provision and that is not renewed or replaced within thirty (30) days of its date of expiration as being out of compliance with the standards for Financial Security contained in this Section 12 and may deem the value of such financial instrument to be zero, and may draw upon such Financial Security prior to its stated expiration if deemed necessary by the ISO.

12.1.2.3 Risk of Loss of Financial Security Amounts Held and Invested by the ISO.

In accordance with the ISO's investment policy, the ISO will invest each Financial Security Amount of a Market Participant or FTR Bidder only in bank accounts, high-quality money market accounts, and/or U.S. Treasury/Agency securities unless a specific written request is received from the Market Participant or FTR Bidder for a different type of investment and the ISO provides its written consent to such alternative investment. A Market Participant or FTR Bidder that provides a Financial Security Amount that is held and invested by the ISO on behalf of the Market Participant or FTR Bidder will bear all risks that such Financial Security Amount will incur a loss of principal and/or interest as a result of the ISO's investment of such Financial Security Amount.

~~A Scheduling Coordinator, UDC or MSS which does not maintain an Approved Credit Rating shall be subject to the limitations on trading set out in Section 12.3.~~

12.1.3 Self-Supply of UDC Demand.

Notwithstanding anything to the contrary in the ISO Tariff, a Scheduling Coordinator or UDC that ~~had an Approved Credit Rating on January 3, 2001, and~~ is an Original Participating Transmission Owner or is a Scheduling Coordinator for an Original Participating Transmission Owner shall not be precluded by Section 12.3 from scheduling transactions that serve a UDC's Demand from –

(1) a resource that the UDC owns; and

(2) a resource that the UDC has under contract to serve its Demand.

12.1.4 Allocation of Aggregate Credit Limit for FTR Auction Participation.

An FTR Bidder may elect to allocate a portion of its Aggregate Credit Limit toward satisfying the credit requirements for participating in auctions of FTRs, as set forth in Section 36.2.6.

12.1.5 Estimated Aggregate Liability.

The ISO will periodically calculate the Estimated Aggregate Liability of each Market Participant and FTR Bidder, based on all charges and settlement amounts for which such Market Participant or FTR Bidder is liable or reasonably anticipated by the ISO to be liable for pursuant to the ISO Tariff. The Estimated Aggregate Liability for each Market Participant or FTR Bidder shall be determined and applied by the ISO consistent with the procedures set forth in the ISO Credit Policy & Procedures Guide posted on the ISO Home Page. The ISO shall upon request provide each Market Participant or FTR Bidder with information concerning the basis for the ISO's determination of its Estimated Aggregate Liability, and the ISO's determination may be disputed in accordance with the procedures set forth in the ISO Credit Policy & Procedures Guide. The ISO shall compare each Market Participant's or FTR Bidder's Estimated Aggregate Liability against its Aggregate Credit Limit on a periodic basis.

12.2 Review of Creditworthiness.

The ISO may review the creditworthiness of any Market Participant or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~ which delays or defaults in making payments due under the ISO Tariff and, as a consequence of that review, may require such Market Participant or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~, whether or not it has~~ (or is deemed to have)~~ an Unsecured~~Approved~~ Credit Limit~~Rating~~, to provide credit support in the form of any of the following types of Financial Security:

(a) an irrevocable and unconditional letter of credit by a bank or financial institution reasonably acceptable to the ISO;

(b) a cash deposit standing to the credit of an interest-bearing escrow account maintained at a bank or financial institution designated by the ISO;

(c) an irrevocable and unconditional surety bond posted by an insurance company reasonably acceptable to the ISO;~~ or~~

(d) a payment bond certificate in the name of the ISO from a financial institution designated by the ISO; or~~.~~

(e) a prepayment to the ISO.

The ISO may require the Market Participant or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~ to maintain such ~~credit support~~Financial Security for at least one (1) year from the date of such delay or default.

12.3 ~~Limitation on Trading~~Posting and Releases of Financial Security.

~~A Scheduling Coordinator, UDC or MSS that does not maintain an Approved Credit Rating, as defined with respect to either payment of the Grid Management Charge, or payment of other charges, shall maintain security in accordance with Section 12.1. For the avoidance of doubt, the ISO Security Amount is intended to cover the entity's outstanding and estimated liability for either (i) Grid Management Charge; and/or (ii) Imbalance Energy, Ancillary Services, Grid Operations Charge, Wheeling Access Charge, High Voltage Access Charge, Transition Charge, Usage Charges, and FERC Annual Charges.~~ Each Market Participant or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~ required to provide a~~n~~ ~~ISO~~Financial Security Amount under Section 12.1.2 shall notify the ISO of the initial ~~ISO~~Financial Security Amount ~~(separated into amounts securing payment of the Grid Management Charge and amounts securing payments of other charges)~~ that it wishes to provide at least fifteen (15) days in advance and shall ensure that the ISO has received such ~~ISO~~Financial Security Amount prior to the date the Market Participant commences activity through the ISO,~~Scheduling Coordinator commences trading or the UDC or MSS commences receiving bills for the High Voltage Access Charge and Transition Charge~~ or the date the FTR Bidder participates in the applicable auction of FTRs. A Market Participant or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~ may at any time increase its ~~ISO~~Financial Security Amount by providing additional ~~guarantees or credit support~~Financial Security in accordance with Section 12.1.2. A Market Participant or FTR Bidder~~Scheduling Coordinator, UDC or MSS~~ may request that ~~reduce~~ its ~~ISO~~Financial Security Amount be reduced or released by making its request ~~giving the ISO~~ not ~~less~~fewer than fifteen (15) days prior to the date on which~~notice of~~ the reduction or release is requested to occur.~~, provided that the Scheduling Coordinator, UDC or MSS is not then in breach of this Section 12.3.~~ The ISO shall evaluate the request and inform the Market Participant or FTR Bidder within ten (10) Business Days either that a reduction or release of the Financial Security Amount is permissible, that a reduction or release of the Financial Security Amount is impermissible, or that the ISO requires more information from the Market Participant or FTR Bidder in order to make its determination. The ISO may decline to reduce or release a Financial Security Amount or may release a lesser amount for any of the following reasons:

(a) The Estimated Aggregate Liability for the Market Participant or FTR Bidder cannot be accurately determined due to a lack of supporting settlement charge information.

(b) The most recent liabilities of the Market Participant or FTR Bidder are volatile to a significant degree and a reduction or release of the Financial Security Amount would present a high likelihood that, after the Financial Security Amount was reduced or released, the Estimated Aggregate Liability for the Market Participant or FTR Bidder, as calculated by the ISO, would exceed its Aggregate Credit Limit.

(c) The Market Participant has provided notice or otherwise demonstrated that it is terminating or significantly reducing its participation in the ISO markets. The ISO may retain a portion of the Financial Security Amount to ensure that the Market Participant is adequately secured with respect to pending liabilities that relate to settlement re-runs or other liabilities for which the Market Participant may be responsible under this ISO Tariff.

~~The ISO shall release, or permit a reduction in the amount of, such guarantees or other credit support required to give effect to a permitted reduction in the ISO Security Amount as the Scheduling Coordinator, UDC or MSS may select.~~

12.4 Calculation of Ongoing Financial Security Requirements.

~~Following the date on which a Scheduling Coordinator commences trading, the Scheduling Coordinator shall not be entitled to submit a Schedule to the ISO and the ISO may reject any Schedule submitted if, at the time of submission, the Scheduling Coordinator's ISO Security Amount is exceeded by the Scheduling Coordinator's estimated aggregate liability for (i) Grid Management Charge and/or (ii) Imbalance Energy, Ancillary Services, Grid Operations Charge, Wheeling Access Charge, Usage Charges, and FERC~~

~~Annual Charges on each Trading Day for which Settlement has not yet been made in accordance with Section 11.3.1 and the Scheduling Coordinator's estimated liability for High Voltage Access Charge and Transition Charge for which Settlement has not yet been made in accordance with Section 11.3.~~ Following the date on which a Market Participant commences trading, if the Market Participant's Estimated Aggregate Liability, as calculated by the ISO, at any time exceeds its Aggregate Credit Limit, the ISO shall direct the Market Participant to post an additional Financial Security Amount within five (5) Business Days that is sufficient to ensure that the Market Participant's Aggregate Credit Limit is at least equal to its Estimated Aggregate Liability. The ISO shall also notify a ~~Scheduling Coordinator~~Market Participant if at any time its Estimated Aggregate Liability~~such outstanding liabilities~~ exceeds 90% of its Aggregate Credit Limit.~~the relevant portion of the ISO Security Amount.~~ For the purposes of calculating the ~~Scheduling Coordinator's~~Market Participant's ~~e~~Estimated ~~a~~Aggregate ~~l~~Liability, the ~~estimate~~ISO shall include (1) outstanding charges for Trading Days for which Settlement data is available, and (2) an estimate of charges for Trading Days for which Settlement data is not yet available. To estimate charges for Trading Days for which Settlement data is not yet available, the ISO will consider available historical Settlement data, and other available operational and market data as described in the ISO Credit Policy & Procedures Guide posted on the ISO Home Page.~~appropriately adjusted to reflect recent market prices and trends, or other available information for individual Scheduling Coordinators.~~

12.5 ISO Enforcement Actions Regarding Under-Secured Market Participants.

Following the date on which a Market Participant commences trading, if a Market Participant's Estimated Aggregate Liability, as calculated by the ISO, at any time exceeds its Aggregate Credit Limit, the ISO may take any or all of the following actions:

(a) The ISO may withhold a pending payment distribution.

(b) The ISO may limit trading, which may include rejection of Schedules and/or limiting other ISO market activity. In such case, the ISO shall notify the Market Participant of its action and the Market Participant shall not be entitled to submit further Schedules to the ISO until the Market Participant posts an additional Financial Security Amount that is sufficient to ensure that the Market Participant's Aggregate Credit Limit is at least equal to its Estimated Aggregate Liability.

(c) The ISO may require the Market Participant to post an additional Financial Security Amount in lieu of an Unsecured Credit Limit for a period of time.

(d) The ISO may restrict, suspend, or terminate a Market Participant's Service Agreement.

In addition, the ISO may restrict or suspend a Market Participant's right to schedule or require the Market Participant to increase its Financial Security Amount if at any time such Market Participant's potential additional liability for Imbalance Energy and other ISO charges is determined by the ISO to be excessive by comparison with the likely cost of the amount of Energy scheduled by the Market Participant.

~~Following the date on which a UDC or MSS commences operation, the UDC's or MSS's Scheduling Coordinator shall not be entitled to submit a Schedule to the ISO and the ISO may reject any Schedule submitted if, at the time of submission, the UDC's or MSS's ISO Security Amount is exceeded by the UDC's or MSS's estimated aggregate liability for Grid Management Charge, and/or High Voltage Access Charges and Transition Charges for which Settlement has not yet been made in accordance with Section 11.3. The ISO shall notify a UDC or MSS if at any time such outstanding liabilities exceed 90% of the relevant portion of the ISO Security Amount. For the purposes of estimating the UDC's or MSS's aggregate liability for High Voltage Access Charges and Transition Charges, the UDC's or MSS's liability shall be equal to the billed Demand use (in MWh) for a month in the UDC's or MSS's Service Area (including exports from the Service Area) multiplied by the ISO's estimated High Voltage Access Charge and Transition Charge for that month, as such estimated cost is notified by the ISO to UDCs and MSSs from time to time.~~

~~**12.3.1** The ISO shall notify the relevant Scheduling Coordinator if it rejects a Schedule under Section 12.3 in which event the Scheduling Coordinator shall not be entitled to submit any further Schedules until it has demonstrated to the ISO's satisfaction that its ISO Security Amount has been increased sufficiently to avoid the limit on trading imposed under Section 12.3 from being exceeded.~~

~~**12.3.2** The ISO may restrict, or suspend a Scheduling Coordinator's right to Schedule or require the Scheduling Coordinator to increase its ISO Security Amount if at any time such Scheduling Coordinator's liability for Imbalance Energy is determined by the ISO to be excessive by comparison with the likely cost of the amount of Energy scheduled by the Scheduling Coordinator.~~

* * *

30.4.1.1 Stage One Validation.

During stage one validation, each incoming Schedule will be validated to verify proper content, format and syntax. The ISO will check that the Scheduling Coordinator had not exceeded its ~~Security Amount~~Aggregate Credit Limit and verify that the Scheduling Coordinator is certified in accordance with the ISO Tariff. The ISO will further verify that the Scheduling Coordinator has inputted valid Generating Unit and Demand location identification. Scheduled Reliability Must-Run Generation will be verified against the contract reference numbers in the ISO's Scheduling Coordinator database. A technical validation will be performed verifying that a scheduled Generating Unit's output is not beyond it's declared capacity and/or operating limits. If there is an error found during stage one validation, the Scheduling Coordinator will be notified immediately through WEnet. The Scheduling Coordinator can then look at the notification messages to review the detailed list of errors, make changes, and resubmit the Schedule if it is still within the ISO's timing requirements. Additionally, if the ISO detects an invalid contract usage (of either Existing Contract rights or Firm Transmission Rights), the ISO will issue an error message in similar manner to the Scheduling Coordinator and allow the Scheduling Coordinator to view the message(s), to make changes, and to resubmit the contract usage template(s) if it is still within the ISO's timing requirements. The Scheduling Coordinator is also notified of successful validation via WEnet.

* * *

[From ISO Tariff Appendix A
(Master Definitions Supplement)]

Aggregate Credit Limit — The sum of a Market Participant's or FTR Bidder's Unsecured Credit Limit and its Financial Security Amount, as provided for in Section 12 of the ISO Tariff.

~~**Approved Credit Rating**~~ — ~~With respect to whether security must be posted for payment of the Grid Management Charge:~~

~~(a) A short-term taxable commercial paper debt rating of not less than any one of the following: (i) A1 by Standard and Poor's Corporation; (ii) F1 by Fitch Ratings; or (iii) P1 by Moody's Investors Service. This rating shall be an issuer, or counterpart rating, without the benefit of credit enhancement.~~

~~(b) A short-term tax exempt commercial paper debt rating of not less than any one of the following: (i) A1 by Standard and Poor's Corporation; (ii) V1 by Fitch Ratings; or (iii) VMIG1 by Moody's Investors Service. This rating shall be an issuer, or counterparty rating, without the benefit of credit enhancement.~~

~~With respect to whether security must be posted for payment of all charges other than the Grid Management Charge:~~

~~(c) A short-term tax exempt commercial paper debt rating of not less than any one of the following: (i) A2 by Standard and Poor's Corporation; (ii) F2 by Fitch Ratings; or (iii) P2 by Moody's Investors Service. This rating shall be an issuer, or counterparty rating, without the benefit of credit enhancement.~~

~~(d) A short-term tax exempt commercial paper debt rating of not less than any one of the following: (i) A2 by Standard and Poor's Corporation; (ii) V2 by Fitch Ratings; or (iii) VMIG2 by Moody's Investors Service. This rating shall be an issuer, or counterparty rating, without the benefit of credit enhancement.~~

~~(e) A long-term debt rating of not less than any one of the following: (i) A- by Standard and Poor's Corporation; (ii) A- by Fitch Ratings; or (iii) A3 by Moody's Investors Service. This rating shall be an issuer, or counterparty rating, without the benefit of credit enhancement.~~

~~With respect to whether security must be posted for payment of all~~

~~charges:~~

~~(f) A federal agency shall be deemed to have an Approved Credit Rating if its financial obligations under the CAISO Tariff are backed by the full faith and credit of the United States.~~

~~(g) A California state agency shall be deemed to have an Approved Credit Rating if its financial obligations under the CAISO Tariff are backed by the full faith and credit of the State of California.~~

~~(h) Another credit rating approved by the CAISO Governing Board.~~

Estimated Aggregate Liability

The sum of a Market Participant's or FTR Bidder's known and reasonably estimated potential liabilities for a specified time period arising from charges described in the ISO Tariff, as provided for in Section 12 of the ISO Tariff.

Financial Security

Any of the types of financial instruments listed in Section 12 of the ISO Tariff that are posted by a Market Participant or FTR Bidder.

~~ISO~~Financial Security Amount

The level of Financial ~~s~~Security posted~~rovided~~ in accordance with Section 12.~~1~~ of the ISO Tariff by ~~an Scheduling Coordinator~~ Market Participant or FTR Bidder.~~Applicant who does not have an Approved Credit Rating. The ISO Security Amount may be separated into two components: (i) the level of security required to secure payment of the Grid Management Charge; and (ii) the level of security required to secure payment of all charges other than the Grid Management Charge.~~

Material Change in Financial Condition

A change in or potential threat to the financial condition of a Market Participant or FTR Bidder that increases the risk that the Market Participant or FTR Bidder will be unlikely to meet some or all of its financial obligations. The types of Material Change in Financial Condition include but are not limited to the following:

(a) a credit agency downgrade;

(b) being placed on a credit watch list by a major rating agency;

(c) a bankruptcy filing;

(d) involvency;

(e) the filing of a material lawsuit that could significantly and adversely affect past, current, or future financial results; or

(f) any change in the financial condition of the Market

Participant or FTR Bidder which exceeds a five percent reduction in the Market Participant's or FTR Bidder's tangible net worth for the Market Participant or FTR Bidder's preceding fiscal year, calculated in accordance with generally accepted accounting practices.

Unsecured Credit Limit The level of credit established for a Market Participant or FTR Bidder that is not secured by any form of Financial Security, as provided for in Section 12 of the ISO Tariff.

ISO TARIFF APPENDIX T

Scheduling Coordinator Application

The information provided for this application will be treated as confidential information

PART A

SCHEDULING COORDINATOR APPLICATION FORM

This application is for approval as a Scheduling Coordinator ("SC") by the California Independent System Operator Corporation ("ISO") in accordance with the ISO Tariff.

I. Administrative Requirements

SC Applicant's Legal Name:

____

Address of principal place of business:

____

____

____

Authorized Representative: ____

Address: ______________________________________

____

Phone: ______________________________________

Fax: ______________________________________

E-mail: ______________________________________

Type of entity: ____

(Municipal utility, power marketer, investor owned utility, federal or state entity or other)

State of Incorporation or Partnership: ______________________

Proposed commencement date for service: ____________________

II. Scheduling Coordinator Customer Information

2.1 The information required under Part C, the ISO Application File Template, must be provided for represented Scheduling Coordinator Metered Entities, which are Generators. The Scheduling Coordinator Applicant must submit all requested information prior to final certification, which must occur fourteen (14) days before the commencement of service.

2.2 Information for Scheduling Coordinator Metered Entities, which are End Users or Eligible Customers, must be kept in a standard business format based on generally accepted accounting principals. The ISO shall have the right to inspect and audit a Scheduling Coordinator's accounts and files relating to its Scheduling Coordinator Metered Entities after giving two Business Days notice in writing.

2.3 The Scheduling Coordinator Applicant must submit a list of all ISO Metered Entities, which it will represent.

III. Security Requirement

3.1 The Scheduling Coordinator Applicant will submit a completed credit application to receive~~has~~ an ~~Approved~~Unsecured Credit Limit~~Rating~~ as set forth in the ISO Tariff and the ISO Credit Policy & Procedures Guide: (yes/no).

The Scheduling Coordinator Applicant has submitted a completed credit application to receive an Unsecured Credit Limit as set forth in the ISO Tariff and the ISO Credit Policy & Procedures Guide: (yes/no). OR

~~The Scheduling Coordinator Applicant's credit rating is __________.~~

~~Please attach certified documentation of an Approved Credit Rating from Standard & Poor's, Moody's Investors Services or the equivalent. Scheduling Coordinator Applicant must also submit, before final certification, an executed letter of understanding for payment providing contact details in case of default. OR~~

~~3.2 The Scheduling Coordinator Applicant will provide an irrevocable and unconditional guarantee from a company which has an Approved Credit Rating: (yes / no).~~

~~The Scheduling Coordinator Applicant must submit a signed irrevocable and unconditional guarantee in an ISO approved form and certified documentation of the other company's Approved Credit Rating before final certification. OR~~

3.2~~3~~ The Scheduling Coordinator Applicant will provide Financial Security in a form listed in Section 12.1.2 of the ISO Tariff: (yes/no).

Acceptable forms of Financial Security include:

(a) an irrevocable and unconditional letter of credit issued by a bank or financial institution that is reasonably acceptable to the ISO;

(b) an irrevocable and unconditional surety bond issued by an insurance company that is reasonably acceptable to the ISO;

(c) an unconditional and irrevocable guaranty issued by a company that is reasonably acceptable to the ISO;

(d) a cash deposit standing to the credit of the ISO in an interest-bearing escrow account maintained at a bank or financial institution that is reasonably acceptable to the ISO;

(e) a certificate of deposit in the name of the ISO issued by a bank or financial institution that is reasonably acceptable to the ISO;

(f) a payment bond certificate in the name of the ISO issued by a bank or financial institution that is reasonably acceptable to the ISO; or

(g) any other form of security that has been evaluated and approved as reasonably acceptable by the ISO.

~~an irrevocable and unconditional letter of credit issued by a bank or financial institution that is reasonably acceptable to the ISO: (yes / no).~~

~~Amount: $__________.~~

~~The Scheduling Coordinator Applicant must submit a signed irrevocable and unconditional letter of credit in an ISO approved form before final certification. OR~~

~~3.4 The Scheduling Coordinator Applicant will provide a cash deposit standing to the credit of the ISO in an interest-bearing escrow account maintained at a bank or financial institution that is reasonably acceptable to the ISO: (yes / no).~~

~~Amount: $____________. The Scheduling Coordinator Applicant must enter into an escrow agreement in an ISO approved form before final certification.~~ AND

3.3~~5~~ The Scheduling Coordinator Applicant must provide its bank account information before final certification. The Scheduling Coordinator Applicant's bank must be capable of performing Fed-Wire System transfers.

IV. Technical Requirements

4.1 Does the Scheduling Coordinator Applicant have the computer hardware, software and communication capabilities for interface compatibility with the ISO system for data transmission, for electronic data interchange (EDI) and for Fed-Wire System transfer accounts? (yes / no) If no, please submit a proposed completion date to be fully operational so that an ISO staff site visit can be arranged.

4.2 For Loads and Generating Units located within the ISO Controlled Grid, does the Scheduling Coordinator Applicant have any scheduling restrictions imposed by the parties they represent? (yes / no) If yes, provide full details on a separate sheet of paper.

4.3 Does the Scheduling Coordinator Applicant have adequate staffing to operate a Scheduling Coordinator's operational facility twenty-four (24) hours a day for 365 days a year? (yes / no). If no, please submit a proposed completion date to be fully operational so that an ISO staff site visit can be arranged.

V. Third Party Contractual Requirements

5.1 The Scheduling Coordinator Applicant confirms that all of its Scheduling Coordinator Customers which are located within the ISO Controlled Grid and which should execute agreements with the ISO have entered into or will enter into, prior to the certification of the Scheduling Coordinator Applicant, all required agreements with the ISO to enable them to meet the requirements of the ISO Tariff: (yes / no).

(a) Represented Generators have signed Participating Generator Agreements: (yes / no).

(b) Represented UDCs have signed UDC Operating Agreements and Meter Service Agreements: (yes / no).

(c) Represented ISO Metered Entities have signed Meter Service Agreements: (yes / no).

(d) Wholesale Customers it will represent have warranted to the Scheduling Coordinato Applicant that they are eligible for wholesale transmission service pursuant to the provisions of the FPA Section 212(h): (yes / no).

(e) Each End-Use Customer it will represent which requests Direct Access service has warranted to the Scheduling Coordinator Applicant that the End-Use Customer is eligible for such service: (yes / no).

5.2 The SCHEDULING COORDINATORApplicant confirms that all of the parties which it represents as Scheduling Coordinator Customers have granted it all necessary agency authority, whether actual, implied or inherent, to enable the Scheduling Coordinator to perform all of its obligations under the ISO Tariff: (yes / no).

5.3 Notwithstanding 5.2, the Scheduling Coordinator confirms that it will have the primary responsibility, as the principal, for all Scheduling Coordinator payment obligations under the ISO Tariff : (yes / no).

VI. Additional Information and Obligations

6.1 The Scheduling Coordinator Applicant agrees to provide such further information to the ISO as the ISO may deem necessary to process the application and certify the Scheduling Coordinator Applicant as a Scheduling Coordinator now and on a continuing basis.

6.2 Subject to the ISO Tariff, the Scheduling Coordinator Applicant agrees to promptly report to the ISO within seven (7) Business Days or earlier any changes regarding the information provided by it referred to in the ISO Tariff and in the application with the exception of the security requirement data referred to in Part III of Part A in this Appendix which must be updated within three (3) Business Days. The Scheduling Coordinator shall be responsible if a failure to submit revised technical data more promptly extends the period during which schedules are rejected by the ISO.

6.3 The Scheduling Coordinator Applicant agrees to enclose herein the non-refundable application fee of $500 to cover the application processing costs, site visit and costs of providing ISO Tariff.

Please make check payable to:
The California Independent System Operator Corporation

6.4 Scheduling Coordinator Applicant agrees to promptly execute and return the Scheduling Coordinator Agreement, Meter Service Agreements, Interim Black Start Agreements, software licensing agreement, letter of understanding, letter of credit, guarant~~ee~~y, escrow agreement, as applicable, and Fed-Wire System bank account number, after receiving its application approval letter from the ISO.

6.5 Final certification is contingent upon Scheduling Coordinator Applicant fulfilling all financial and technical requirements as referenced in the ISO Tariff (including Part C of this Appendix, the ISO Application File Template).

Scheduling Coordinator Applicant certifies by its signature on this Application Form that:

(1) all information it is submitting is correct and accurate; and that

(2) the Scheduling Coordinator Applicant has read and agrees to be bound by the ISO Tariff as may be in force or amended from time to time.

Name of Organization:

____

Scheduling Coordinator Applicant's Name (please print):

____

Scheduling Coordinator Applicant's Title:

____

Scheduling Coordinator Applicant's Signature:

____

State of ______________________}

ss

County of ______________________}

[SEAL]

Sworn and subscribed
before me this ____ day of
_________________,19___.

Notary's Signature: ____

Please send application and required information to:

California Independent System Operator Corporation
c/o Schedule Coordinator Application Processing Office
151 Blue Ravine Road,
Folsom, CA 95630

ATTACHMENT C

CALIFORNIA ISO

California Independent
System Operator

Memorandum

To: ISO Finance Committee

From: Phil Leiber, Treasurer & Director of Financial Planning; Byron Woertz, MRTU

cc: ISO Board of Governors, ISO Officers

Date: June 8, 2005

Re: ISO Credit Policy for Scheduling Coordinators – Proposed Changes

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This memorandum requires Board action.

Executive Summary

On May 6, 2005 Management informed you of a "final draft" set of recommended changes to its policies and procedures to enhance the financial security in the ISO's markets. The ISO discussed these proposed changes with stakeholders at an April 26th, 2005 web conference, and has received written comments from several Scheduling Coordinators (SCs) regarding the proposed changes.

We classified the changes in three categories:

- Changes that the ISO already has implemented;
- "Phase 1" changes that the ISO proposes to implement in 2005. These are the changes addressed in this Board memorandum; and
- "Phase 2" changes that Management proposes to pursue in 2006.

With this memo, Management requests authorization to proceed with preparing and filing the Tariff language for the recommended Phase 1 changes and to develop detailed procedures for implementing each of the changes.

Motion

MOVED:

That the ISO Governing Board approves the "Phase 1" changes to the ISO Credit Policy for Scheduling Coordinators, as set forth in Attachment A to the memorandum to the ISO Finance Committee dated June 8, 2005, and directs ISO Management to proceed with developing Tariff language (as necessary) and operating procedures to implement the policy changes.

Proposed Changes

Over the past three and a half years, the ISO has considered several changes to its policies for ensuring adequate financial security for all market participants. The ISO has communicated regularly with stakeholders as it has considered each of these options, most recently through stakeholder meetings on November 30, 2004 and on April 26, 2005. The table included in Attachment A, "SC Credit Policy: Changes Under Consideration," describes the credit review team's proposed changes to the ISO's credit policies. Section numbers refer to the sections of the document posted on the ISO web site for stakeholder review[1].

Matters Considered and Changes Already Implemented

The ISO has already implemented several improvements and changes which did not require Tariff revisions, including:

- Requiring SCs that use more than one Scheduling Coordinator Identification (SCID) number to schedule their market transactions to provide sufficient security for all SCIDs' obligations in aggregate;
- Requiring new SCs to post security for at least 14 days of expected market transactions, with the SC's posting requirement to be reviewed weekly and adjusted as necessary;
- Implementing the Scheduling Coordinator Aggregate Liability Estimator ("SCALE") as the tool for estimating SCs' financial liabilities;
- Continuing to allow "net creditor" months to offset "net debtor" months within an SC's security posting requirements; and
- To reduce volatility in security posting requirements, basing security posting requests on the lesser of (1) the most recent SCALE figure or (2) a moving average of the most recent SCALE estimates over the past month. No further changes are expected to the SCALE tool until 2006, at which point the new Settlements and Market Clearing system will generate liability estimates. .

Proposed Phase 1 Changes

Management is requesting the Board's approval to move forward with the Phase 1 changes identified in Attachment A. These include the following:

Credit Limits for SCs - At present, SCs with an Approved Credit Rating[2] receive unlimited unsecured credit in the ISO's markets. Management proposes to set credit limits for each SC, based on credit ratings, other third party credit assessments and entity-specific financial data. The ISO proposes specific approaches for:

- Rated Public / Private Corporations,

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[1] At http://www.caiso.com/docs/2003/04/21/2003042117001924814.html.

[2] Defined in the Tariff. In short, entities that have an A-/A3 Moody's/S&P long-term credit rating , A2/P2 short-term rating, or whose obligations are backed by the State or Federal Government

- Unrated Public / Private Corporations,
- Rated Governmentally Owned Utilities, and
- Unrated Governmentally Owned Utilities[3].

Other changes include providing additional granularity in calculating credit limits by using long-term rather than short-term ratings, creating a $250 million unsecured credit cap for any single entity, and eliminating separate credit standards for market and GMC obligations.

Setting credit limits for entities is the most substantive of the changes proposed, and will require additional ongoing effort by the ISO. Rather than hire additional analysts to perform complex credit assessments, the ISO intends to maintain a generally objective "rules-based" approach and to obtain assistance from third party credit organizations to evaluate and administer the credit limits. Management intends to post on the ISO website the specific information to be used to set such limits, and how the assessments for each entity type will be performed. The documents distributed for stakeholder review illustrate the proposed approach for each entity type. The annual cost for the third party assistance anticipated to be necessary is likely to be in the very low six-figure range, less than the cost of expanding the ISO's credit staff to perform similar services.

ISO-Approved Security Documents - In general, SCs use pro-forma security documents for letters of credit, guarantees and other security documents, although there have been a few exceptions. Management proposes to require SCs to use standardized documents to the greatest extent possible. In special circumstances, the ISO will consider exceptions, but SCs must allow the ISO 10 business days to consider the exception. Until and unless the ISO approves an exception, SCs must use standardized documents.

Security Agreement Expiration - Currently, all security documents remain in effect through their stated expiration date. All security documents will expire and be considered void 30 days prior to their stated expiration dates. SCs can avoid a lapse in security coverage by ensuring that documents are renewed at least 30 days prior to expiration or by providing for perpetual effectiveness.

Credit Insurance - The ISO does not currently have a credit insurance program in place. Over the past several months, the ISO has discussed with several insurance companies the possibility of offering credit insurance to provide additional assurance of payment to suppliers for unsecured market and GMC liabilities.. This insurance would cover the portion of outstanding market and GMC liabilities that is not secured by collateral, which would include the liabilities of entities granted some unsecured credit under the proposed change noted above. There would likely be an overall limit for the entire market and limits per Scheduling Coordinator. The insurance would be part of an overall credit management approach and would not replace collateral requirements or credit monitoring by the ISO. In fact, the ISO would have to maintain or enhance its oversight of credit requirements as a condition of insurability and in order to maintain an overall lower premium. If such a program is determined to be

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[3] After the publication for stakeholder review of our proposed approach for setting limits for various entity types, we determined that additional opportunities for unsecured credit should be provided for unrated Governmental Owned Utilities. Accordingly, we will grant unsecured credit to these entities based on the formulas published to date (which provide unsecured credit of up to 5% of net assets if certain financial ratios are met), and may provide unsecured credit based on an assessment of other quantitative and qualitative factors as set forth in FERC's November 2004 credit policy statement.

cost effective and of value in encouraging additional entities to supply power during this summer's expected tight conditions, Management may proceed to purchase the credit insurance. Quotes received in early June indicate coverage costs are higher than anticipated, but Management will continue to negotiate cost and terms with carriers in an attempt to structure and attractive program.

Number of Days Included in Liability Calculation - Although the ISO generally requires SCs to post security from the previously- paid invoice to the next scheduled invoice (approximately 102 days), there have been exceptions. Management proposes to eliminate the "Weekly Period" posting option and will require a security posting based on a level number of days outstanding from invoice-to-invoice. As the ISO moves to accelerated payments (planned for Q1 2006), it is projected that security posting requirements for all SCs will decrease by approximately 50 percent.

Risk of Loss for Funds Held By the ISO - The ISO Tariff does not currently address how to remedy the situation where funds held by the ISO as security for SCs are invested (consistent with the ISO investment policy) for their account, suffer a loss of principal. Management proposes to add a section to the ISO Tariff that addresses the risk of loss of funds held and invested by the ISO on behalf of Market Participants. Market Participants will bear any risk of loss of principal and/or interest of such funds. The updated ISO Investment Policy (also scheduled for approval at this Board meeting) will specify that it will only invest such funds in a bank account, high-quality money market fund, or US Government security unless a specific agreement between the ISO and SC specifies another type of investment (also limited to investments permissible in the ISO investment policy).

Proposed Phase 2 Changes

Management proposes to take no action currently on Phase 2 changes listed in Attachment A until 2006. Should Management desire to proceed with these changes, we will return to the Board for approval.

Stakeholder Comments

The ISO received written comments from approximately 10 entities following the two stakeholder meetings on credit matters. **Appendix 1** contains a record of stakeholder comments and questions about the proposed changes, and ISO responses to this feedback. Such comments were also posted to the ISO web site as received[4]. The feedback covers a range of issues on various elements of the ISO's proposal. Several stakeholders have requested additional details about the changes, and some have noted ongoing discussions with the ISO regarding special circumstances. However, since the April 26 stakeholder meeting, the ISO has not received comments opposed to any of the ISO's proposed changes. Importantly, many entities have expressed support for, and none have opposed the proposal to set specific credit limits for individual SCs.

Timeline for Moving Forward

If the Board approves the proposed changes, Management will continue working to prepare necessary Tariff changes. Our intent is to coordinate the Tariff filing for credit policy changes with other needed Tariff filings in the near future. Our best estimate is that such a filing could take place in September, 2005. In that case, the proposed changes could take effect as soon as November, 2005. Management will work

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[4] At http://www.caiso.com/docs/2003/04/21/2003042117001924814.html.

with internal business units, stakeholders, and outside vendors who are to support the ISO in the administration of the credit limit setting process to ensure that operating procedures are in place prior to FERC approval of the Tariff changes so that the revised policies may be implemented as early as possible.

The ISO will plan to address "Phase 2" changes during 2006.

Attachment A - SC Credit Policy: Proposed Changes (Summary)

Creditworthiness

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
4.1	Credit Limits for SCs with ACR	SCs with an Approved Credit Limit (ACR) are given unlimited credit in the ISO's markets.	The ISO would set credit limits for each SC, based on credit ratings, other third party credit assessments and entity-specific financial data. The ISO proposes specific approaches for: • Rated Public / Private Corporations, • Unrated Public / Private Corporations, • Rated Governmentally Owned Utilities, and • Unrated Governmentally Owned Utilities. Other changes include providing additional granularity in calculating credit limits, creating a $250 million unsecured credit cap for any single entity and eliminating the use of short-term credit ratings in establishing credit limits.	Phase 1
4.2	SC Identification Number (SCID)-Specific Credit Limits.	In general, the ISO does not allow SCs that use more than one SCID to schedule their transactions to segregate the financial liabilities represented by each SCID. There have been some exceptions to this rule.	The ISO will maintain its current policy without exceptions. The ISO believes that each SC represents a single financial risk, regardless of the number of SCIDs under which it schedules. Collateral posted by an SC with the ISO will secure obligations of all SCIDs scheduled by that SC.	Already Implemented
4.3	ISO-Approved Security Documents	In general, SCs use pro forma security documents for letters of credit, bill guarantees and other security documents. There have been a few...	The ISO will require SCs to use standardized documents to the greatest extent possible. In special circumstances, the ISO will consider exceptions, but SCs must allow the ISO 10 business days to consider the exception. Until and unless the ISO approves an exception, SCs must use standardized documents.	Phase 1

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
		have been a few exceptions.		
4.4	Security Agreement Expiration	All security documents remain in effect through their stated expiration date.	All security documents will expire and be considered void 30 days prior to their stated expiration dates. SCs can avoid a lapse in security coverage by ensuring that documents are renewed at least 30 days prior to expiration or by providing for perpetual effectiveness.	Phase 1
4.5	Credit Insurance	The ISO does not offer credit insurance, either to individual SCs or for the overall market.	The ISO will continue discussions with Aon Risk Services on various insurance proposals. It will update SCs as it finalizes the proposals.	Phase 1 (possibly) or Phase 2

Liability Obligation Calculations and Security Posting Requirements

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
5.1	Liability Obligation Calculations for New SCs	A new SC must post financial security for its maximum estimated financial liabilities. The ISO offers a tool for estimating liabilities, but there is no minimum posting requirement.	The ISO will continue to offer the tool, an Excel-based spreadsheet, for estimating financial obligations based on the SC's expected market activities. SCs will be required to post security to cover a minimum of two week's worth of expected market activities. The ISO will monitor each SC's liabilities weekly and request adjustments to posted security as appropriate.	Already Implemented
5.2 – 5.4	SCALE Tool	In April, 2004, the ISO implemented SCALE as the tool for estimating SCs' financial obligations.	The ISO will continue to use SCALE to estimate SCs' liabilities.	Already Implemented
5.5	Number of Days Included	Although SCs' financial liabilities vary over the	The ISO will eliminate the "Weekly Period" posting option and will require a security posting based on a level number of days	Phase 1

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
	in Liability Calculation	course of a billing cycle, the ISO requires SCs to post financial security to cover their financial liabilities from the previously paid invoice to the next scheduled invoice (approximately 102 days). When PG&E and SCE began using cash deposits to provide their security, the ISO allowed them to adjust their cash postings weekly to reflect their varying liabilities.	outstanding from invoice-to-invoice. As the ISO moves to accelerated payments (planned for Q1 2006), each SC's posting requirement is expected to decrease by approximately 50 percent.	
5.6	Price Volatility and Forecasted Liabilities	The SCALE tool is based in part on market prices for energy and ancillary services, prices that, in the past, have experienced high volatility. The ISO has considered measures that could mitigate this price volatility.	SCALE uses an average of prices over the past 15 days. Recent market prices have not shown significant price spikes. The ISO believes that the potential risk reduction achieved by implementing some sort of volatility mitigation would not justify the anticipated expense or complexity.	Already Implemented
5.7	Security Postings for Special Circumstances	The ISO does not increase or decrease security posting requirements for special circumstances such as adjustments from disputes, refund orders, Good Faith Negotiations or other adjustments to	If the ISO is able to quantify an SC's financial obligations resulting from these special circumstances with a reasonable degree of certainty, it will adjust its security posting requests appropriately. It will not adjust security posting requests if it cannot do so with reasonable certainty or if the SC would not be able to post additional security significantly sooner than it could respond to the current invoice payment that includes the actual adjustments.	Phase 2

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
		historical charges; SCs leaving the market; or SCs making significant changes to their business practices that affect financial obligations.		
5.8	Security Posting Requirement By Individual Trade Months	The ISO determines its security posting requests based on all un-invoiced trade months. Thus, if an SC is a net creditor in one outstanding month and a net debtor in another outstanding month, the two obligations will net against each other.	The ISO will continue this practice. The ISO settles each trade month separately, based on SCs' credits and debits during that month. Thus, there is a small possibility that there would be insufficient funds to clear the market in the case where an SC that was a net debtor defaulted on their invoice and that SC was using a different month's net credit to offset its financial obligation. However, SC payment defaults have not been a recent problem. The ISO believes the risk of additional defaults is not great enough to justify a change in this policy.	Already Implemented
5.9	Changes Resulting from New Settlement System	The ISO estimates SCs' financial obligations based on current market rules and the current settlement cycle and schedule.	As the ISO implements changes to its Settlements system, including improvements to its liability estimating tools, the Finance Department will review these impacts on SCs' outstanding financial obligations and recommend appropriate changes to its credit policies and procedures.	Phase 2
5.10	Changes Resulting From Accelerated Payments	The ISO estimates SCs' financial obligations based on current market rules and the current settlement cycle and schedule.	As the ISO implements Accelerated Payments, the Finance Department will review this impact on SCs' outstanding financial obligations and recommend appropriate changes to its credit policies and procedures.	Phase 2
5.11	Adjustments to Security Postings	Each week, the ISO estimates each SC's security posting requirements. Based on	The ISO will base its security posting requests on the lesser of (1) the most recent SCALE figure; or (2) a moving average of the most recent SCALE estimates over the past month. This has proven to reduce volatility in security posting requests.	Already Implemented

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
		the weekly estimate the ISO may request additional security or the SC may request a return of some portion of their posted security.		

Enforcement

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
6.1	Unsecured Obligation Penalties	If an SC fails to provide adequate financial security, there is no financial penalty.	The ISO will continue to study how penalties might be implemented. The credit review team has considered such a penalty based on the difference between an SC's security posted and actual settlement charges . However, the ISO would not be able to Implement such a penalty until the completion of the SaMC project.	Phase 2
6.2	Late Payment Penalties	There is no current penalty for SCs that fail to pay invoices by the deadline specified in the ISO Tariff.	The credit review team considered such a penalty. However, the ISO would not be able to Implement such a penalty until the completion of the SaMC project.	Phase 2
6.3	SC Suspension, Disconnection and Termination	The ISO Tariff allows the ISO to suspend an SC's scheduling privileges and/or terminate an SC Agreement under certain circumstances.	The ISO is recommending changes to this policy. We invite stakeholder discussion of the current tools to address non-compliance with the collateral requirements including suspension of scheduling privileges and termination of an SC Agreement, and how they might be made more effective for all types of SCs. Any suspension/termination and disconnection process should include the following: • Due process - notice and opportunity to be heard prior to	Phase 2 or later

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
			adverse action; • The right to cure; • Notice to other affected parties, including regulatory authorities and utilities; and • Maintenance of obligations. Any suspension/termination and disconnection process should expressly provide that SC obligations under the SC Agreement remain (e.g. obligation to pay any amounts due under SC agreement and/or Tariff) even if the SC is suspended/terminated.	

Other Issues

Sect.	Description	Current Policy/Procedure	Proposed Policy/Procedure	Implementation Phase
7.1	Risk of Loss for Funds Held by the ISO on Behalf of Market Participants	The ISO Tariff does not currently address how to remedy the situation where funds held by the ISO as security for SCs are lost.	The ISO will propose a section to be added to the ISO Tariff that addresses the risk of loss of funds held and invested by the ISO on behalf of Market Participants. Market Participants would bear any risk of loss of principal and/or interest of such funds. The ISO investment policy will specify that it will only invest such funds in a bank account, high-quality money market fund, or US Government security unless an agreement between the ISO and SC specifies another type of investment (which would also be limited to an investment specified in the ISO Investment Policy).	Phase 1

CALIFORNIA ISO

California Independent
System Operator

Appendix 1

SC Credit Policy
CAISO Response to Stakeholder Comments

June 2005

Prepared by: Allen Yoho / Phil Leiber / Byron Woertz

Table of Contents

(Sections in this document correspond to those in the document posted for stakeholder comment)

Scheduling Coordinator Credit Policy Review

CAISO Response to Stakeholder Comments

The following stakeholder feedback was received by the CAISO subsequent to the November 2004 and April 2005 stakeholder meetings. Each section contains questions raised by the CAISO on each issue for stakeholder consideration, stakeholder comments and questions, and CAISO responses to the stakeholder comments and questions.

3. Review Process Overview

Stakeholder Responses

Automated Power Exchange

We have a general concern that if this proposed credit policy is implemented prior to the payment acceleration process (instead of the two being simultaneously implemented), APX, which is a small privately-held company, could be negatively impacted financially by having to post credit in the first place (based on the proposed credit policy), and then having to adjust the credit posting requirement again when the payment acceleration system is put into operation.

CAISO Response:

We are not clear about the concern expressed by APX here. The changes proposed here may result in some unsecured credit being extended to additional entities who must be 100% collateralized today—this may benefit APX rather than impose an additional burden.

Calpine

In light of the many Credit changes that have been implemented at the other ISOs since November 2003, Calpine recommends that the CAISO reopen its Credit Policy Benchmarking study and reassess what parts of the current CAISO credit policy can be improved and develop specific recommendations.

Also, the CAISO should set-up a standing credit policy stakeholder group, who meets regularly to aid it and its stakeholders in credit related matters. Also, stakeholders should elect other stakeholders to the Chair and Vice-Chair leadership positions. This policy would be consistent with the policies of ERCOT and NEPOOL.

CAISO Response

We believe this is a good idea as well and will consider how to structure such a group.

City of Santa Clara

Many of the questions put forth by the CAISO are the type of issues that would be best considered and addressed by a stakeholder advisory group on credit issues.

CAISO Response

We believe this is a good idea as well and will consider how to structure such a group.

Northern California Power Administration (Supportive)

Forming a stakeholder advisory group for credit issues is a good idea. I'd recommend it have a good representation of the market participants.

CAISO Response

We believe this is a good idea as well and will consider how to structure such a group.

Strategic Energy

Under the CAISO's proposed rules, could Strategic receive an open line and then reserve the right to post either a Guaranty or a Letter of Credit to cover the exposures?

CAISO Response

Yes. SCs may choose to post more than one form of security, if such postings are required (for SCs that owe funds, and would not have a sufficient unsecured credit limit). An SC could choose to post collateral even if it had unsecured credit capacity with the ISO. An SC could also choose not to apply for unsecured credit, and instead post collateral.

4. Creditworthiness

4.1. Setting Credit Limits (Supplemental Information in Appendix A)

<u>Stakeholder Questions</u>

The Team believes that changes to eliminate the unlimited extension of credit are necessary, and that the above process is a reasonable approach for accomplishing this. The CAISO invites stakeholders' comments on the following questions:

1. Do you agree with the recommended tiered approach to limiting the credit exposure of SCs with ACRs?
2. Is it reasonable to allow extend some credit to entities with a lower investment grade rating using this tiered approach?
3. Should a percentage of tangible net worth approach be used? What other approaches could be used?
4. Should the CAISO apply this approach to municipal or other governmental entities? If not, what other method could be used?
5. The CAISO is considering using Moody's KMV to obtain an additional, potentially more timely indicator of credit risk than relying on only the national credit rating agencies ratings. Is this approach worthwhile?
6. Should the CAISO implement an additional limit, for example, 35% of the CAISO's total market receivables, as an upper limit to any individual SC's initial limit to avoid concentration of credit risk? If so, what would be an appropriate limit?
7. Do you support implementing a single credit standard that eliminates the separate treatment for GMC obligations?

Stakeholder Responses

Automated Power Exchange (further explanation required)

We do not see a proposed solution to this in the recommendation as it relates to privately-held companies. How would privately-held companies be evaluated and assigned a credit rating? We would be opposed to financial statement-only assessments to determine credit worthiness or credit ratings. We believe our historical activity with the CAISO should be factored into the rating.

CAISO Response:

We have added a provision to potentially provide some credit to entities without a credit rating—as encouraged in FERC's November 2004 policy statement on credit.

A Moody's KMV EFF can be calculated for any company, including privately held companies, with the RiskCalc product. The RiskCalc model requires as inputs approximately 10 financial statement metrics. CAISO will be relying primarily on such a quantitative approach for unrated companies.

We might at a later date incorporate other qualitative measures such as payment history.

California Department of Water Resources (Supportive)

No entity should be granted unlimited credit.

CAISO Response:

Agreed. Our initial and this revised proposal are based on this view.

It is reasonable to allow some credit to entities with a lower than investment grade rating under the tired approach especially when combined with the use of an alternative scoring model such as the Moody's KMV product.

CAISO Response:

The CAISO is proposing to implement a rule that provides only those entities with default probabilities less than the average lowest investment grade default probability unsecured credit. See the proposed change above and the example in Attachment A.

In theory, the method proposed could allow an entity with a lower than investment grade rating from some national credit rating agency with at least some unsecured credit due to the blending of all of the entity's credit ratings, and further blending this with Moody's KMV default probability .

Some other measure of liquidity (such as a working capital ratio or a quick ratio) might provide a better measure.

CAISO Response:

TNW is used as a scaling factor to recognize entities of different sizes and to gauge how much credit to extend after first determining that an entity is likely creditworthy. This is part of a two step process, with the first step consisting of answer the question, should any credit at all be extended. That first step will in many cases consider other financial metrics as suggested (the Moody's KMV score for most SCs will be generated with their "RiskCalc" product which considers approximately 10 financial metrics, including liquidity measures.

" Writer appears uncomfortable with TNW as the scaling factor for the credit limit, questioning it's usefulness vis a vis other alternatives such as working capital. This is also raised by NCPA (also suggests a working capital variant) and PGE (which does not offer an alternative). I agree that TNW may not be the best factor, and appears to have been chosen because it is already in place at some other ISO/RTOs. If the CalSO wanted to engage the MKMV research team, we could examine various factors and suggest the best factor on a validated basis." Jim Herrity Moody's / KMV

A tiered approach should also be used to determine the amount of unsecured credit for municipalities and governmental agencies. Unfortunately, the use of a Moody's KMV score is unavailable for this class of market participant so the supposed benefit of "quickness" of recognition to changes in financial health isn't realized. The CAISO could attempt to compensate for this by having two different scales of % of net worth in initial unsecured credit. For example, for the class of market participants that a Moody's KMV score is available a combined numeric rating score of < 1.5 yields 7.5%. For a municipal or governmental agency where only a long-term bond rating is available, that same numeric rating score of < 1.5 could yield a 7.0% or 6.5%. Maybe this isn't necessary since municipal and governmental agencies have the ability to collect revenues to cover costs but again, the name of the game here is free cash flow and the ability to make payments in a timely manner.

CAISO Response:

This is an interesting issue and a good observation. Either approach would appear to have merit. We have elected to stay with a single table of percentages, even in the absence of a Moody's KMV score for such entities.

The use of the Moody's KMV model is worthwhile.

CAISO Response:

We agree.

The use of a concentration limit is also worthwhile, but feel that 35% may be too high of a limit. 25% or maybe even 20% may be more appropriate.

CAISO Response:

We have rethought the issue of concentration caps and removed this provision in our revised proposal, replacing it with a maximum limit for any entity. We believe this approach will provide adequate protection for suppliers/creditors, and have seen potential problems with administering a concentration cap.

The implementation of a single credit standard for GMC and Market Charges is acceptable.

CAISO Response:

Our initial and this revised proposal include this.

City of Santa Clara (Supportive)

No unlimited credit granted to any SC

CAISO Response:

We agree.

Credit limits should be tiered limits based on a calculated ISO-specific and transparent credit rating.

CAISO Response:

We agree the process should be as transparent as possible, and believe our proposal meets that goal.

Unsecured credit limits should only be available to investment grade (i.e., greater than BBB- or Baa3) rated entities or unrated, but otherwise clearly determined to be credit-worthy.

CAISO Response:

The CAISO is proposing to implement a rule that provides only those entities with default probabilities less than the average lowest investment grade default probability unsecured credit. See the proposed change above and the example in Attachment A.

The use of Moody's KMV default probability models for publicly-traded entities in setting initial (and ongoing) unsecured credit limits is intriguing and deserves more discussion.

CAISO Response:

We have incorporated that approach into our initial and this revised proposal.

We believe that the large rating agencies already include some qualitative factors (management style, etc.) in their long-term ratings. This should for the most part satisfy the FERC's recent Policy Statement and in a manner that is considered more impartial than may occur if the CAISO was to attempt that analysis. It would appear that the KMV default probabilities provide a more rapid but yet completely quantitative analysis of default risk.

CAISO Response:

We agree that the national rating agencies consider both qualitative and quantitative factors in setting limits, and with your statement with respect to FERC's recent policy statement. The Moody's KMV default probabilities come from two models: for public firms, "Credit Edge" looks at stock prices and other factors, and is updated frequently. For non-public firms (or subsidiaries of publically traded firms), "RiskCalc" relies on approximately 10 financial statement metrics, that could be updated once per quarter. The latter is a quantitative approach, while an argument can be made that the former approach does consider qualitative factors to the extent investors as a whole consider these things, which affects stock prices.

There needs to be more specific discussion of how municipal utilities will be treated in a CAISO credit review. The default method appears to be that instead of a blended rating comprised of 50 percent of the Agency Rating and 50 percent of the rating implied by the KMV default probability, public power agencies would be rated strictly on the Agency Rating. This would still provide a transparent and objective method of determining the CAISO's Approved Credit Rating (ACR).

CAISO Response:

If a municipal utility has a credit rating from a national credit rating agency, that would be used as 100% of the determination of which tier of allowable credit they would receive (i.e. no Moody's KMV rating is available for municipals, so a blended rating could not be used.) We have also added a provision to our proposal to potentially provide some credit to municipal utilities without a credit rating.

A limitation on any one individual participant's unsecured credit to no more than some percentage of the CAISO's total market accounts receivable is acceptable. Something in the 30% range should be a reasonable cap. (With lower cap for unrated agencies.)

CAISO Response:

We have rethought the issue of concentration caps and removed this provision in our revised proposal, replacing it with a maximum limit for any entity.

SVP strongly supports one set of credit rating rules used for all charges that eliminates the separate treatment for GMC obligations.

CAISO Response:

Our initial and this revised proposal includes this.

Northern California Power Administration (Supportive)

The ISO suggested using a credit limit based on Total Net Worth. This is a quantitative approach and it does not take into account the qualitative factors as described in FERC's Policy Statement.

Current tangible net worth is an even better indicator if this path is chosen. An entity is not going to sell its plant and equipment to pay monthly bills. The difference between current tangible assets and current tangible liabilities shows the amounts available, in the short-term, for paying bills.

CAISO Response:

Tangible Net Worth is used as a scaling factor to recognize entities of different sizes and to gauge how much credit to extend after first determining that an entity should be eligible for some unsecured credit. This is part of a two step process, with the first step consisting of answering the question, should any credit at all be extended. That first step will in many cases consider other financial metrics (the Moody's KMV score for most SCs will be generated with their "RiskCalc" product which considers approximately 10 financial metrics, including liquidity measures.

Total Net Worth is not a good indicator of an entity's ability to pay a monthly invoice. Tangible net worth works better.

CAISO Response:

We propose to use tangible net worth.

The City of Riverside mentioned using a "cash flow" approach in rating munis since Moody's KMV does not work for munis. A good cash flow forecast – identifying when revenues will be received and when obligations come due – requires a great deal of assumptions and hard work. I'd like more information on how Riverside's cash flow approach would work.

CAISO Response:

We would need more information about that approach to evaluate it fully. We are cognizant of the need to control costs and staffing and we are interested in a solution that will not require significant additional staffing or cost.

We have discussed the method proposed by Riverside's with them briefly and have determined that an alternate approach such as the ERCOT method of calculating unsecured credit for Municipal Utilities or another quantitive approach . Also, a Municipal Utility with an investment grade credit rating will have its average default probability from rating agencies weighted 100% since Moody's KMV does not calculate default probabilities for these entities.

Pacific Gas and Electric Company

What is the process that the CAISO will follow if it can't get KMV default probability for a particular entity?

CAISO Response:

We would use only the national credit rating agency score.

What particular aspects of the proposed policy are consistent with other ISO practices?

CAISO Response:

We have borrowed heavily from the practices at other ISOs, including NYISO and ERCOT, including the fundamental "tiering" concept of looking at factors to determine creditworthiness, then determining how much credit to extend based a matrix.

What is the underlying reason for using Tangible Net Worth as a basis for granting unsecured credit line?

CAISO Response:

We want to have some relatively simple measure that incorporates entity size and overall financial health. Other ISO's (NYISO/ERCOT/PJM/MISO) have used this measure. We recognize that a broader range of measures might provide an even better picture of an entities credit worthiness, but we are trying to balance the benefits that might be derived from a more comprehensive review against the not insignificant costs of administering such reviews in an environment of considerable concern about CAISO administrative costs.

How will the CAISO handle cases in which a non-investment grade counterparty has a large Tangible Net Worth number but has a poor cash flow from operations?

CAISO Response:

That would likely be reflected in the Moody's KMV score, and have an effect on the creditworthiness decision. We should be able to obtain KMV scores for all entities other than governmentally owned utilities.

How will the CAISO take into account an entity's liquidity in granting a credit line?

CAISO Response:

The rating agency scores and Moody's KMV scores should reflect liquidity concerns to a reasonable degree. Liquidity is considered by Moody's KMV in their RiskCalc model, which will be used to determine an EDF for most SCs.

We realize more direct measures of liquidity are possible. Another participant in the stakeholder process discussed with CAISO the use of the following approach:

(1) Net Cash provided by Operating Activities over the past 12 month period

(2) Less: Changes in working capital in the past 12 month period

(3) Add: Working Capital at the end of the 12 month period (current assets less current liabilities)

We recognize this approach also has merit, and might represent an even better measure of an entity's ability to meet its short-term obligations. Our concerns about it include:

- It is a different approach than used by peer ISOs, which use TNW as a basis for scaling.
- Given the need for an "automated" means to collect and calculate the credit limits, this approach may require more manual calculation and analysis.

We would appreciate the views of other parties on such an approach.

What rating is the CAISO planning to use from S&P - senior unsecured debt; senior secured debt; or issuer rating?

CAISO Response:

Our preference is for an issuer rating. If an entity only has a senior unsecured debt rating, we would propose to reduce that rating by one notch for our purposes.

What if a company doesn't have a senior unsecured debt rating because it has issued no senior unsecured debt – how will the CAISO handle this issue?

CAISO Response:

Such an entity can elect to obtain an issuer rating from the national rating agencies and/or an equivalency rating from Moody's KMV. Additionally, we have added in this revised proposal a means to consider such an entity's financial condition and grant some unsecured credit on that basis without a credit rating.

How often will the CAISO perform credit reviews?

CAISO Response:

We will further consider this issue over the next coming months, when we learn more about what systems and tools we will have available to assist in credit management, and the staff that might be dedicated to this function. As an initial thought, we would expect to perform updates at least quarterly for public/private companies and at least annually for municipal utilities.

What will it do if the SC has no S&P rating?

CAISO Response:

An entity may have a rating from one rating agency but not another (such as S&P.) We would use ratings that are available from the national credit rating agencies and weight each available rating to develop a composite rating. See other responses for how we would treat entities with no ratings from national credit rating agencies.

PG&E agrees that credit risk arises from both GMC and market, but would like to know how the CAISO intends to bill these two types of services?

CAISO Response:

Currently, separate invoices are issued for GMC and market charges. Upon implementation of the new SaMC system, a single invoice will be issued for market and GMC charge. This issue is independent of whether there should be separate credit standards for GMC and market charges, but as indicated we are proposing to move to a single standard.

What is the basis for the % of net worth associated with the rating score?

CAISO Response:

We have reviewed the methodologies used by other ISOs including NYISO in establishing such tiers.

What is the basis for the 35% factor to take into account the concentration limit in A/R?

CAISO Response:

NYISO ISO has a 20% concentration limit. We considered that too low based on the number and concentration of participants in the California energy market. However, we have eliminated the concentration cap from this revised proposal.

What is the current concentration in A/R?

CAISO Response:

As would be expected, this changes and has varied widely. At times, the concentration has been significant (in excess of 75%).

What has the highest number been over the last 12 months?

CAISO Response:

See below.

How long did it stay at the number?

CAISO Response:

Concentration has remained high for several months.

Strategic Energy (Supportive)

Credit Limits should be developed using a tiered structure. The ISO could utilize a sliding scale to protect against "cliff-like" credit events.

CAISO Response:

We believe our proposed structure does this.

"Using the proposed inverse of the default probability applied to the 'scale' factor (TNW) as proposed accomplishes this." Jim Herrity Moody's / KMV

For non-rated entities, the ISO should look to the ERCOT/PJM & NYISO models, where unsecured credit can be granted based upon an entity's net worth, total debt/EBITDA, &

EBIT/Interest ratios. Many financially strong companies exist that do not have S&P or Moody's ratings.

CAISO Response:

Our revised proposal includes a provision for non-rated entities.

"Other ISO/RTOs implement a series of models based on financial statement ratios, however, no model has the level of validation and transparency of RiskCalc. Additionally, RiskCalc should provide more stable results since it was developed on the largest known private firm default database and tested on separate hold out samples. Furthermore, MKMV obtains new test data from participating institutions quarterly to ensure that the model continues to perform well as economic conditions change." Jim Herrity Moody's / KMV

A combination of Options C and D from Appendix A should be utilized.

CAISO Response:

The CAISO will rely primarily on a quantitative approach initially, and may review incorporating qualitative measures into the unsecured credit assessment process at a later date.

The CAISO never discusses giving a SC more credit capacity if it is on positive credit watch, only negative. This is a double standard. A Company should receive some benefit for an improving credit profile.

CAISO Response:

We will opt to be conservative on this matter, and make an adjustment only for potential downward adjustments, but will continue to consider this matter. Because we are blending the credit ratings that a company has, and a Moody's KMV rating, we believe this provides a fair opportunity for the consideration of improving factors about a company.

The CAISO may want to limit its concentration of credit exposure to any one company. The 35% appears reasonable, but we're unaware if this number has ever come close to existing or being violated. If the value is too high, what is the purpose?

CAISO Response:

The 35% limit would be expected to have an effect on the amount of unsecured credit granted to participants in the future—so it isn't likely to be "too high". However, we have opted to eliminate this aspect of our initial proposal. We will instead pursue a maximum unsecured limit for individual participants of $200 million (yet to be finalized) or another limit as set by the ISO Governing Board.

The Moody's/KMV model relies heavily on the equity markets and the broader market may unfairly impact a market participant's credit score.

CAISO Response:

We recognize that no measure is comprehensive, and other considerations may not be adequately reflected in a Moody's KMV score. However, we believe this is a move in the direction of considering factors beyond the national credit rating agency ratings, and a move toward the quantitative and qualitative measures as listed in FERC's November 2004 policy statement. We note that Moody's KMV scores are derived from two models. The model for public companies would be applied only to those SCs were the public company has a direct relationship with the ISO—few SCs have this. In most cases a subsidiary of such companies is the SC, and a different Moody's KMV model (using "RiskCalc") would consider financial data to determine the EDF score. Moody's KMV clarifies here:

"Equity market prices do play a significant role in the MKMV public firm model. The writer implies that the broader market may unfairly impact the firm's equity price, and the resultant MKMV EDF. In essence, the writer implies that the market might not always be efficient. While MKMV does not necessarily assume that the price reflects all the relevant information about a firm we do know that it is difficult to consistently beat the market. For example, over 90% of managed funds were unable to outperform the market in 1998. That is, it is difficult to pick stocks consistently and difficult to know when the market is under- or overvaluing a firm. The market reflects a summary of many investors' forecast and it is unusual if any one individual's, or committee's, forecast is better. Consequently, we believe that the best source of information regarding the value of a firm is the market." Jim Herrity Moody's / KMV

Strategic requests that the CAISO provide training and an explanation of Moody's KMV model to all SCs before implementing this change. Most SCs probably have no familiarity with this model, yet are being asked to agree with its use in setting the SC's Unsecured Credit Limit.

CAISO Response:

As part of the commitment to transparency in the process we intend to implement, we recognize the value of this, and will take steps to ensure that SCs understand what is being done. Moody's KMV does have some published material on their approach that should explain the basis for their EDF measures:

http://www.moodyskmv.com/products/RiskCalc_private.html

http://www.moodyskmv.com/products/edf_rc31_usa.pdf

One of the benefits of the proposed approach is that it will be repeatable and objective, i.e. the ISO and the SC should arrive at the same determination of the credit limit based on same data.

4.2 BAID / SCID specific security postings

Stakeholder Responses

Automated Power Exchange

The recommendation proposed by the CAISO will change our current relationship with our SCIDs and provides a barrier in the ease of entry into the California energy market. Specifically, we currently have an individual SCID who has credit posted directly with the CAISO, but we are not required by the CAISO to post any credit for any of our other SCIDs. In essence, this particular SCID takes responsibility directly with the CAISO for its own security. This protects the SCID that has their own credit posted directly with the CAISO in case any of our other SCIDs default on payment to the CAISO, and vice versa.

If the proposed policy goes into effect, can we post multiple letters of credit as security under one scheduling coordinator?

CAISO Response:

Part 1: The current situation with APX is anomalous and the CAISO has requested that APX rectify the situation. The CAISO has a direct relationship with its SCs and not the SC's customers. It is up to an SC to manage the credit risk of its clients or portfolio.

Part 2 : Yes. Multiple security instruments may be posted provided the security instruments are unconditional with respect to applying to an overall SC.

This will affect APX which has multiple SCID's, which are both generator and load customers, currently we (excluding one of our participants who has a separate credit agreement posted with the CAISO) are in a net creditor position with the CAISO. However, with the proposed policy, All APX ID's will be included in the calculation and we will need to post credit for APX as a whole.

CAISO Response:

CAISO's legal department is reviewing this particular customer's credit vehicle to determine how it will fit into the revised CAISO credit policy.

California Department of Water Resources (Objection)

While it is true that the Department has one SC agreement, the two entities that transact in the CAISO markets are separate legal entities (have two distinct funding sources). The Department would prefer to not aggregate these two entities (the State Water Project and California Energy Resource Scheduling).

CAISO Response:

The operative legal document is the SC Agreement. Where two entities are scheduled by one SC with a single SC Agreement, one of the entities has, in effect, appointed an agent—the party to the SC Agreement—for its transactions. As noted earlier, the CAISO is willing to except separate security instruments, which could represent the obligations of different entities, provided the instruments were unconditional. As a further alternative, each entity could enter into separate SC Agreements. Each entity would then have its own posting requirements and would be treated separately by the CAISO.

City of Santa Clara (Supportive)

SVP supports the CAISO's recommendation for each SC to provide appropriate financial security for all SC IDs for which it is responsible for on a "net" basis.

4.3 CAISO Approved Security Agreements (Supplemental Information in Appendix B)

Stakeholder Questions

1. Should CAISO require the use of standard forms? If yes, should exceptions be allowed, and under what circumstances?

Stakeholder Responses

City of Santa Clara (Supportive)

It is reasonable for the CAISO to require that security agreements all conform to California law and venue, and to accept fewer deviations from standard forms.

CAISO Response:

We agree.

It is reasonable that any such necessary action be arbitrated or litigated in a California venue.

CAISO Response:

We agree.

Prior to a security agreements expiration, is the CAISO monitoring to determine if a guarantor is still viable on an on-going basis (i.e. between expirations)?

CAISO Response:

Yes, we periodically review credit ratings of guarantors, and would do so under our proposed revisions to the credit policy.

Pacific Gas and Electric Company

How will the CAISO reach agreement with its stakeholders on a standard form L/C?

CAISO Response:

Like other ISOs/RTOs, the CAISO is considering submitting forms to the FERC as part of its credit polices. Whether the CAISO submits specific forms to FERC for approval or not, the CAISO would post them for stakeholder comment. The CAISO's goal in this respect is not necessarily to "reach agreement" with its stakeholders, but to develop commercially reasonable forms that are generally acceptable to stakeholders while meeting the interests of the CAISO and the interests intended to be protected by the CAISO's security policies.

Strategic Energy (Supportive)

Surety Bonds should continue to be an acceptable form of credit support.

CAISO Response:

We are not proposing to eliminate surety bonds as a form of security.

A standard form for L/C's, guarantees, etc. is reasonable if the form of the document is "common in the industry". For example, the ERCOT form of guaranty is impossible and its L/C will only be issued by one bank in our bank group.

CAISO Response:

The CAISO intends to use forms that are commercially reasonable.

Strategic would like the opportunity to review the CAISO's standard-form documents for the Guaranty and the Letter of Credit before they are adopted.

CAISO Response:

We agree this would be a good step, and will do so. Our goal is to have standard forms that strike a reasonable balance between the needs of the ISO and participants, and which can be quickly used with a minimum of administrative effort on either side.

4.4 Security Agreement Expiration and Liability Obligation Coverage Limitation Issue

Stakeholder Questions

1. Should the CAISO consider a shorter lead-time in advance of a security agreement's expiration, (i.e., 20, 15 or 10 days)?
2. What other alternatives could address this issue, such as requiring "evergreen" agreements that renew automatically unless cancelled with advance notice?

Stakeholder Responses

California Department of Water Resources (Supportive of suggested approach)

We also agree with the wisdom of having an alternative or replacement form of security in place 30 days prior to the expiration of the existing form as a way to protect market participants. I believe what we are thinking here is a type of "evergreen" agreement – with the goal of not having a lapse in the form of security as long as some form of security is required.

CAISO Response:

We encourage "evergreen" agreements. The 30-day issue is to address parties that do not provide evergreen agreements.

Strategic Energy (Supportive)

The concept of a security agreement having zero value 30 days before expiration is reasonable for L/C's only. Any form of guaranty accepted by the CAISO should include language stating that obligations incurred prior to the expiration date remain obligations after the expiration date if the guaranty is not extended.

CAISO Response:

The CAISO form guaranty currently in use includes language that provides that obligations incurred prior to the expiration date remain obligations after the expiration date. The purpose of reducing the value to zero ensures for timely extension of the guaranty or timely substitution of another credit instrument for going forward obligations. Thus, the CAISO's proposal is also appropriate for guaranties.

4.5 Credit Insurance (Supplemental Information in Appendix C)

Stakeholder Responses

Automated Power Exchange

Structure 1 - Would this be coverage for all SCIDs? It looks like cost recovery is still an issue.

CAISO Response:

As soon as the CAISO finds out more information related to costs and insurance structure, we will advise market participants.

Has there been any further progress made on a resolution?

CAISO Response:

Progress is slowly continuing, but we have nothing of substance to report on this at this time.

How will this process be managed?

CAISO Response:

See other responses below.

In other words, is this a blanket cost for all participants in the CAISO or only for participants required to post credit?

CAISO Response:

That is yet to be determined and is the essence of the "cost recovery issue". Upon a move to payment acceleration, the outstanding receivables to the CAISO market will decrease significant, and the cost of insurance will decrease correspondingly, making the cost recovery issue less important.

City of Santa Clara (Objection – only because Payment Acceleration should be implemented first.)

This should only be considered after more effort has been made to shorten settlement periods and consider other security requirements.

CAISO Response:

Currently, the CAISO is focusing on implementing the major recommendations addressed in this document. Due to the limited human resources associated with this undertaking, the insurance issue has slowly progressed. As the assessment of credit insurance is further reviewed in the near future, the Credit Policy Team will ensure that the effects of a shortened settlement cycle are taken into consideration.

It is premature for CAISO to be seeking insurance quotes, as appears to be the case, before implementing any of the other credit policy improvements. The costs of the policy would become just another pass-through GMC charge anchored at a high price quote that then voids the serious effort of improving CAISO settlement structure and credit policy. SVP would submit that unnecessarily high GMC costs create barriers to market entry.

CAISO Response:

We have explored two options, the second of which would not be paid for at all by the CAISO. We recognize cost recovery is a significant issue for the "pool coverage" approach (Option 1) and will proceed cautiously on this issue. We do note that the November 2004 FERC policy statement did encourage the consideration of this issue, but raised issues similar to those City of Santa Clara has raised.

Pacific Gas and Electric Company's

What does the CAISO expect would be covered with credit insurance – all unsecured credit, all A/R, a portion of A/R, etc?

CAISO Response:

As soon as the CAISO finds out more information related to costs and insurance structure, we will advise market participants.

Strategic Energy (Interested in the concept)

This is an interesting idea. Can this insurance be provided at a reasonable cost? Please provide an update to market participants on how discussions progress with Aon.

CAISO Response:

As soon as the CAISO finds out more information related to costs and insurance structure, we will advise market participants.

We continue to think this is an interesting idea and would like to see more information on how this insurance could be provided at a reasonable cost. As the discussions with Aon progress, we would like to receive updates from the CAISO on this topic.

CAISO Response:

CAISO is working with an insurance broker as of May 2005, and have received a proposal from one insurer during May. We will receive proposals from at least one other insurer, and negotiate for as favorable of terms and coverage cost as possible. We will keep market participants informed of our progress.

Costs appear to be somewhat higher than we had anticipated, apparently due to the increased turmoil in the bond markets and higher credit risk premiums given the GM, Ford downgrades, and other events such as the United Airlines pension fund issues.

5. Liability Obligation Calculations and Security Posting Requirements

Stakeholder Responses

City of Santa Clara (Supportive however it desires the implementation of a stakeholder advisory group to assist with the development of SCALE policy.)

SVP would recommend the creation of a well-represented stakeholder advisory group to discuss the refinements to and accuracy of SCALE, the number of days to include in a liability calculation, the price volatility problems, and what level of security postings above the estimated aggregate liability is still appropriate if SCALE is refined. CAISO should be prepared to provide empirical evidence related to the different recommendations to the stakeholder advisory group.

The advisory group would also be able to assist the CAISO Finance Department develop the credit management functionality in the SaMC system.

CAISO Response:

After reviewing the practices of the other ISO's we find the stakeholder advisory group concept to be interesting and worthwhile to explore. We look forward to reviewing proposals submitted by stakeholders on this issue.

Pacific Gas and Electric Company

What risk would the CAISO take on if it used a simple method to compute exposure for posting?

For example, use 2 times (once the new system goes in) the highest settled amount from the previous 12 months. The formula would then be [2*Highest Monthly Bill less the Unsecured Credit Line – posted collateral = Collateral to post]. The formula could be set every 12 months unless there was a sharp increase in monthly charges incurred by the SC.

CAISO Response:

Historically, the CAISO has worked toward calculating each SC's liabilities based on the most recent operational data available. Over the years the process has gotten more sophisticated and complex, and the accuracy level of the estimation process has improved significantly. Simpler approaches are possible, if one is willing to accept two drawbacks, because a simpler approach is likely to result in a less accurate estimate of an SC's liability. These drawbacks are that the SC will either be forced to maintain more security than is necessary to cover their obligations, or the ISO market creditors will be exposed to potential default risk from an under-secured participant.

With the existing approach, if an SC wants to avoid frequent collateral adjustments, they have that ability: post sufficient collateral to cover their highest outstanding obligations.

What would some of the benefits be if the CAISO went to a simplified approach?

CAISO Response:

See above.

What would be some of the pitfalls?

CAISO Response:

See above.

5.1 Liability Obligation Requirements for New SCs

Stakeholder Response

California Department of Water Resources (Supportive)

With respect to new SC's we agree with the CAISO recommendations to require the SC to post security to cover 14 days of estimated charges, increasing postings as needed as well as with the use of the simplified spreadsheet to estimate obligations.

CAISO Response:

Agreed, and see our response below.

City of Santa Clara (Supportive)

When a new entity without an ACR is certified as an SC, it is reasonable to allow the new SC to ramp up its obligation at the current number of days of participation plus 30 initial days, eventually ramping to the maximum obligation.

CAISO Response:

Agreed, and see our response below.

Strategic Energy

A new SC should have to post collateral equal to its forecast MWh's over a 30-day time frame multiplied by the average on-peak price for the past 30 days.

CAISO Response:

We will adopt an approach that is generally consistent with this in that our approach will rely on: (1) a forecast of requirements by the SC (2) recent energy and A/S prices. We are also willing to permit the collateral to increase as transactions are incurred (ramp up period.) We are not looking at substantive changes to our current approach on this matter.

5.3 Refinements to SCALE

Stakeholder Responses

California Department of Water Resources (Supportive)

The CAISO should use more conservative assumptions to provide greater assurance that SCs with a financial security posting obligation are adequately secured.

CAISO Response:

We will continue to attempt to appropriately balance the need to have a conservative estimate of obligations to protect market creditors, with the avoidance of unrealistically high estimates resulting in costly collateral postings by purchases. Accuracy is the goal we will continue to strive for. We may periodically "fine tune" the SCALE process to best achieve this objective.

5.5 Number of Days Included in Liability Calculation

Stakeholder Response

California Department of Water Resources (Supportive)

Permitting SCs the discretion to post security for either a fixed period or a variable period is acceptable.

CAISO Response:

See below.

Strategic Energy

We like the idea of having a SC select the period of time used in the cycle (70 -102 days).

CAISO Response:

We will provide flexibility, but have decided to limit this, as described in the proposal. .

The proposal for a "Level posting period" of 102 days is excessive and burdensome, especially when compared to the requirements of other ISOs. Strategic urges the CAISO to make it a high priority to reduce this requirement as soon as possible. Strategic is concerned that the CAISO's Payment Acceleration Project continues to slip and is now scheduled to be implemented in mid-2006.

CAISO Response:

CAISO recognizes the need to substantially reduce the length of the payment cycle and is committed to doing so. We have, and continue to view this as a high priority project. It is scheduled for implementation as soon as possible in 2006 upon the completion of the new Settlements and Market Clearing system, which is a requirement for payment acceleration.

As for the level posting requirement, nearly all SCs are posting to that requirement today—there are just a few who have posted on a weekly basis in recognition of the fluctuating number of days outstanding. We allowed for that flexible approach on a "pilot program" basis in 2003. We believe that given the move to substantially reduce the length of the payment cycle (albeit in 2006), it make senses to return to posting requirement that matches the somewhat longer-term positions of each SC (maximum outstanding over the course of the payment cycle). The weekly approach will be permitted to continue in some circumstances, such as for new SCs until they have transacted for the number of days in the payment cycle.

The number of days in the level posting period will drop when Payment Acceleration is implemented.

5.6 Price Volatility and Forecasted Liabilities

Stakeholder Responses

California Department of Water Resources (Supportive)

We agree that the CAISO should revisit this issue and implement a volatility adjustment if a significant increase in price volatility is seen.

CAISO Response:

We will continue to monitor this issue.

5.7 Liability Obligation Calculation and Security Posting Requirements for Special Circumstances

Stakeholder Questions

1. Is five percent of the net absolute value of historical charges an acceptable base requirement amount for SCs leaving the market or with substantial activity level changes? If not, what would be an acceptable percentage?

Stakeholder Responses

Automated Power Exchange

The new rerun period is June 20, 2001 through June 30, 2004; APX IDs will be affected. APX has potential liabilities that will be affected by this rerun, which could at any time; put us at a margin call position with the CAISO. APX strongly opposes the rerun liabilities be included in the current credit posting calculation. The CAISO has not determined when they would start rolling estimated liabilities into credit calculations or how much time they would give a SCID to react.

CAISO Response:

Currently, rerun estimated charges are not available due to settlement system constraints. However, if these charges are calculated by the settlement system and are invoiced significantly after the calculation date (one or two months later), CAISO will include the charges in the SCALEs.

California Department of Water Resources (Supportive)

What constitutes "substantially reduced participation" in the CAISO markets? This needs to be quantified prior to adoption of the recommendation to hold a 5% residual security posting for a period of one year. Upon implementation of a new settlement system in 2005, revisit the one-year residual security posting holding period if a shorter holding period is warranted.

CAISO Response:

We agree that defining terms precisely is always desirable, but in this case it may not be possible to quantify this matter further. We will continue to consider this issue.

5.8 Security Posting Requirements by Individual Trade Months

Stakeholder Responses

Bonneville Power Administration

From the seller's perspective, buyers from the CAISO must be fully secured at all times. Accommodations in the EAL calculation that increase the risk of default by purchasers are undesirable. If the CAISO practice of settling each month independently requires additional security from purchasers, then purchasers should post sufficient security for each month regardless of any prospective offsets, as long as the CAISO continues this settlement practice.

CAISO Response:

We appreciate this perspective—it is why we raised the issue. We do believe at this time however, that the risk of any loss from this situation is very remote (allowing balances of different months to offset means at worst, a participant doesn't pay month 1's bill and no security is available because they are a creditor in month 2. We can apply funds they would have received in month 2 to their month 1 balance.) As we will be moving to a substantially reduced number of days transactions outstanding in 2005, this issue will largely be resolved anyway. Further, see comment on FERC Credit Policy statement on netting above.

California Department of Water Resources (Supportive)

The continuance of the policy that allows net creditor months to offset net debtor months is preferred.

Should this policy be applied across the board equally? This seems like a perfect place to follow the November 19 FERC Order and "consider qualitative and quantitative factors" and possible exercise the discretion to not make this policy the same for all market participants.

CAISO Response:

We prefer a consistent approach to the extent possible, but as suggested, may need to exercise discretion in appropriate circumstances.

Strategic Energy

A SC's potential collateral posting should include all debits/credits. To exclude a company's long position in the marketplace would unfairly punish the SC.

CAISO Response:

We agree, and we believe the FERC Policy Statement on credit has spoken on this matter—balances are to be netted to the extent possible.

5.10 Payment Acceleration Effects on Liability Obligation Calculations and Security Posting Requirements

Stakeholder Responses

City of Santa Clara (Supportive)

SVP supports the highest priority being given to reducing the numbers of days for which settlement is outstanding.

Also, improve the system for allocating partial payments, such that it does not require "up to 5 days" to re-allocate.

CAISO Response:

We will continue to focus resources on the items that providing the greatest benefit to stakeholder—we believe payment acceleration meets this criteria.

The Settlements and Market Clearing system being developed currently will significantly automate the market clearing process, including allocating partial payments (if any).

Northern California Power Administration (Supportive)

Shorter payment cycles are the best way to reduce the liability. The easiest way to shorten the payment cycle is to bill on estimates. A second billing cycle would true up the difference between the estimated bills and actual bills.

CAISO Response:

We agree. The ISO payment acceleration team is working to do exactly that.

6. Enforcement

Stakeholder Responses

City of Santa Clara (Supportive)

Any enforcement discussion should include a discussion of the market participants due process rights. Some charges may be too difficult for a market participant to estimate before settlement. Penalties without a cure or "safe-harbor" right may be too harsh.

A charge penalty could reasonably be assessed if an SC were to exceed its approved credit limit and /or financial security in excess of a reasonable bandwidth percentage.

With respect to Late Payment Penalties, the question not being discussed in this section is why there is a "delay of up to five days in the distribution of payments" because of a failed payment by any SC. Has the system become so convoluted that what should be an automatic recalculation and pro-rata takes days to run?

What will the CAISO do with the Late Payment penalties, above and beyond interest, collected? Will it be used to fund a reserve account or some other offset to the benefit of all the market participants?

CAISO Response:

We agree the due process rights are important and will be addressed. These are essential, and are in fact a primary reason why we have found this to be a particularly challenging issue. We also agree that some charges are can be difficult to assess, and this makes the "safe harbor" approach of value.

With respect to the delay in distribution of payments because of a failed payment by an SC, the current system has become quite complicated. This will be improved with the deployment of a new Settlement and Market Clearing System later this year.

Late payments penalties would likely be used in a manner as suggested above. Precise details are yet to be determined.

6.1 Unsecured Obligation Penalties

Stakeholder Questions

1. Should the CAISO implement penalties for failure to comply with financial security policies?
2. What would be an appropriate level of penalty (as a percentage of the difference between obligation and posted security)?
3. Should a "safe-harbor" be provided to waive penalties if an SC had complied with the CAISO's security posting requests?
4. What alternative approaches would encourage compliance with the posting requirements?

Stakeholder Responses

Bonneville Power Administration

Whatever method the CAISO chooses for notification that an SC's balance is reaching or has exceeded the amount of posted security, that notification must be delivered promptly to sellers so that they can adjust their marketing in response their assessment of the risk that they won't be paid. If the CAISO limits access to information that an SC's purchases are not fully secured, as in the current proposal to distribute notice to financial contacts rather than posting the notice on the web, it is misleading sellers by failing to inform them of this risk. Even posting the notice on the web requires sellers to monitor CAISO postings; the appropriate action by the CAISO would be to actively notify all SCs rather than passively post the information and leave it to affected parties to discover it.

CAISO Response:

CAISO staff carefully considered various options with respect to making information available to market participants about "undersecured SCs" during 2003, and encountered numerous potential obstacles, such as (1) the need for very accurate information prior to being sufficiently confident of making such an announcement (2) legal claims if such a publication was found to be inaccurate (3) other factors.

We believe that the various reforms noted in this document, including penalties for undersecured SCs will reduce the likelihood of SCs participating in the ISO markets while undersecured.

We will continue to carefully consider this issue.

California Department of Water Resources (Supportive)

A penalty for an unsecured obligation and a "safe-harbor" or avoidance of penalties is acceptable.

However a different standard between a municipal or governmental agency and a private entity when it comes to the number of days allowed between a CAISO posting request and receipt of such request. Unequal treatment can be rationalized by following FERCs words in its November Order where it said to consider the "nature of the organization and operating environment".

CAISO Response: We will further pursue a penalty approach with a safe harbor, as discussed above.

We recognize that some entities have internal procedures and controls that make prompt responses more difficult. We will need to further consider this issue. We are not aware of difference response types by entity type at other ISO/RTOs. In any event. we hope that we have provided enough collateral options (including prepayments) that all entities can use a method that best suites their situation.

Pacific Gas and Electric Company

How complicated would this penalty process be to administer?

CAISO Response: This proposal is only in the conceptual stage currently. We believe it can be implemented and administered with reasonable efforts, but will continue to carefully consider expected costs and benefits. We do think the benefits are meaningful in terms of providing appropriate incentives for participants to be adequately secured.

How likely is this to result in compliance with CAISO requests?

CAISO Response: We think it will improve compliance. Penalties will work well in light of the following: (a) SC has primary responsibility to post adequate security, but ISO must also monitor balances and request security as appropriate. (b) If SC believes the ISO estimate is inappropriate, SC can invoke the "Appeal Procedure" (as documented in existing Credit Policy Guide). (c) If SC turns out to be incorrect and is undersecured, a penalty would be applied for the amount of the unsecured portion of their obligation.

How would the simplified Security Requirement calculation method mentioned above alleviate the need for a penalty process?

CAISO Response: In one sense, it might help. It might help in the sense that there would be no need for the ISO and an SC to debate whose estimate was correct. If the posting requirement was for example "the highest two months bills in the past 12 months", this would be objective and transparent. The downside is that wouldn't necessarily be a good indicator of a current obligation. Market creditors would be exposure to credit risk in the event of a default by an undersecured SC, or that SC may have to post more security than is necessary based on their current activity.

This is an issue in which only various trade-offs appear possible. There is no single solution that solves all objectives. Payment acceleration does make all of this much less significant.

6.2 Late Payment Penalties

Stakeholder Questions

1. Are the suggested penalty amounts appropriate?
2. What other approaches should the ISO consider to encourage SC compliance with the payment deadlines?

Stakeholder Responses

Northern California Power Administration (Supportive if the penalty amount is higher than a participants cost of capital)

The ISO mentioned using a 1% penalty for late payments with a maximum amount of $10,000. If an entity's cost of money, the cost of obtaining money to pay the invoice, exceeds the penalty, it will not be an effective penalty.

> **CAISO Response**: We agree with your point that the penalty must exceed the cost of funds to be effective. We think the proposed penalty would be effective because it is 1% per day, not 1% per year.

6.3 SC Suspension, Disconnection and Termination Policy Revision

Stakeholder Questions

1. Is there a suspension, disconnection and termination policy / structure implemented at another ISO that the CAISO could use as a basis for resolving this issue?
2. How could these procedures be further improved to reduce the risk of payment defaults and losses to CAISO market creditors?

Stakeholder Responses

None received.

ATTACHMENT D

Board of Governors 6/15/2005 **Approval of Credit Policy for SCs**

MOVED that the ISO Governing Board approves the "Phase 1" changes to the ISO Credit Policy for Scheduling Coordinators, as set forth in Attachment A to the memorandum to the ISO Finance Committee dated June 8, 2005, and directs ISO Management to proceed with developing Tariff language (as necessary) and operating procedures to implement the policy changes and further directs Management to conduct an analysis for additional security measures and to provide a status report at the next meeting.

Moved: Gage Second: Cazalet

Board Action: **Passed** Vote Count: **5-0-0**	
Cazalet	Y
Gage	Y
Lowe	Y
Willrich	Y
Wiseman	Y

Moved: Cazalet Second: Gage

Committee Action: **Passed** Vote Count: **2-0-0**	
Cazalet	Y
Gage	Y

Motion Number: <number>

CERTIFICATE OF SERVICE

I hereby certify that I have served the foregoing document upon each of the entities described in that document in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, California on this 7th day of March, 2006.

Sidney M. Davies BRM

Sidney M. Davies