

Memorandum

To: ISO Board of Governors

From: Ryan Seghesio, Chief Financial Officer and Treasurer

Date: October 20, 2011

Re: Briefing on FERC Order 741 - Minimum Capitalization Requirements

This memorandum does not require Board action.

EXECUTIVE SUMMARY

On May 18, 2011, the Board of Governors approved Management's recommendations related to the Federal Energy Regulatory Commission's Order 741 – Credit Reforms in Organized Wholesale Electric Markets. Among those recommendations approved by the Board were minimum capitalization requirements for participation in the ISO market. At the Board meeting, Management committed to informing the Board of the outcome of FERC's ruling on the order across the ISO industry. On September 15, 2011, FERC conditionally approved the ISO's compliance filing effective October 1, 2011. With regards to the minimum capitalization requirements, FERC unconditionally accepted the language approved by the Board and summarized in this memo. FERC also accepted the similar approaches by the other ISO's, a comparison of which can be found within this memo.

MINIMUM CAPITALIZATION REQUIREMENTS

The Board approved the general framework of the ISO's minimum participation requirements, including minimum capitalization requirements, at its May meeting. The capitalization requirements required a market participant to post a secured form of financial security if they were unable to demonstrate, through their financial statements, that they had a minimum of \$1 million tangible net worth or \$10 million of total assets. The posting amount would be \$500,000 for new market participants or market participants who have been in the ISO market less than six months, or their highest obligations to the ISO during the preceding six months was greater than \$100,000. For those market participants whose highest obligations during the preceding six months was \$100,000 or less, the posting requirement would be \$100,000.

In its ruling, the Commission found that the ISO's capitalization requirements were consistent with the Commission's directives. Further, the Commission found the capitalization requirements to be just and reasonable and not unduly discriminatory or

preferential. The Commission agreed with the ISO that the ability to ensure that a market participant is adequately capitalized appropriately considers market risk without unreasonably preventing market entry. In addition, the Commission acknowledged that the ISO committed in its compliance filing to monitor the market regarding barriers to entry for smaller participants and that the ISO is prepared to reassess its capitalization requirements if the revised tariff language proves to inhibit meaningful market participation for smaller entities.

The Commission stated that they understood that there may be more than one just and reasonable set of minimum participation criteria and declined to require RTOs and ISOs to adopt uniform minimum participation criteria, including capitalization requirements. Attachment 1 provides a comparative analysis of the other RTOs and ISOs capitalization requirements that the Commission found to be just and reasonable.

CONCLUSION

In general, the ISO's requirements are in-line with the requirements submitted by the other ISOs. As is the case with all aspects of the credit policy, Management will continue to monitor this provision to ensure its affect has the intended outcome.

ATTACHMENT 1

	California ISO	NYISO	SPP	ISO-NE	PJM	Midwest ISO
Minimum capitalization requirement (no posting requirement)	\$1 million tangible net worth or \$10 million total assets	\$1 million tangible net worth or \$10 million total assets	\$1 million tangible net worth or \$10 million total assets or a credit rating of or equivalent to BBB-	\$1 million tangible net worth or \$10 million total assets or credit rating of BBB-/Baa3 or higher or non-congestion market participants with less than \$100K of obligations	\$1 million tangible net worth or \$10 million tangible assets for congestion participants (half these requirements for non-congestion participants)	\$1 million tangible net worth or \$10 million total assets (half these requirements for non-congestion participants)
Posting requirement (secured form of financial security that cannot be used for any other market activity except as noted)	<p>\$500K for new market participant, existing market participants with less than six months in the market or market participants whose obligations to the ISO exceed \$100K in the preceding six months</p> <p>\$100K for market participants whose obligations to the ISO exceed \$100K in the preceding six months</p>	\$500K for participants in the congestion market, otherwise, \$200K for all other participants	\$200K or two times participant's potential obligations if participant's activity is expected to exceed \$100K	<p>15% of financial assurance requirements for participants in the congestion market plus suspension from entering into congestion transactions with a duration greater than one month</p> <p>\$25K - \$500K based on level of financial assurance requirements for non-congestion market participants</p>	<p>\$500K plus 10% reduction in collateral for congestion market participants</p> <p>\$200K plus 10% reduction in collateral for virtual bidding market participants</p> <p>10% reduction in collateral for all other market participants</p>	<p>\$500K to participate in any or all service categories</p> <p>\$200K to participate in any or all service categories except for annual congestion markets</p> <p>\$50K to participate in any or all service categories except for monthly and annual congestion markets</p>