Stakeholder Comments Template

Subject: Credit Policy Enhancements Straw Proposal

Submitted by	**Company**	**Date Submitted**
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This template has been created for submission of stakeholder comments on the topics covered in the October 27, 2008 Credit Policy Enhancements stakeholder call. Upon completion of this template, please email your comments (as an attachment in MS Word format) to CreditPolicyComments@caiso.com. All comments will be posted to CAISO's Credit Policy Stakeholder Process webpage at http://www.caiso.com/docs/2003/04/21/2003042117001924814.html.

Submissions are requested by close of business on **November 4, 2008 or sooner**.

Please submit your comments to the following questions for each topic in the spaces indicated.

1. Are you generally in favor of the ISO establishing credit policies, such as the three enhancements presented during this stakeholder process, that result in more conservative unsecured credit limits?

    - APM Comment: APM recommends establishing credit policies that result in more conservative unsecured credit limits. However, APM disagrees with some of the enhancements proposed during the stakeholder process. Specifically, APM does not recommend the use of Moody's KMV Spot Credit Rating because APM is unaware of the methodology used in determining the spot ratings, and cannot advocate its use. In addition, APM doesn't recommend excluding restricted assets from the TNW calculation unless those assets match a liability that is reported on the balance sheet.
    - CAISO Response: The use of Moody's KMV data was stakeholdered and ultimately approved by FERC in CAISO's 2006 Tariff change. Since 2006, CAISO has been using Moody's KMV Estimated Default Frequency (EDF) and Moody's KMV Agency Rating 5 Year Median Default Probabilities in the calculation to determine the amount of unsecured credit to allow a Market Participant. A Moody's KMV EDF has an associated "equivalent rating" (a CAISO term defined in the straw

proposal) assigned by Moody's KMV that effectively equates this value to an equivalent agency rating. The CAISO views the EDF and its equivalent rating as generally interchangeable for the purpose of the unsecured credit limit calculation, and as such does not see this as a material change to policy and is not CAISO's intent to reopen a discussion on a topic that has been stakeholdered and approved (i.e., the general use of the Moody's KMV data in setting unsecured credit limits).

CAISO agrees that a restricted asset should be offset by matching restricted liability when a matching restricted liability exists but only if that result yields a value greater than zero. Without this test, a Market Participant with restricted liabilities that exceeded restricted assets could increase their Tangible Net Worth based on the proposed formula for Tangible Net Worth.

2. Do you support the ISO's straw proposal to use the lowest Credit Agency Issuer Rating when two or more issuer ratings are available? If only a short term rating is available, do you support the use of the lowest equivalent long term rating?

- APM Comment: APM recommends using the lowest Credit Agency Senior Unsecured Debt Rating over the Issuer Rating. If the Issuer Rating is unavailable, then APM recommends using the lowest Issuer Rating. APM cannot recommend using an equivalent long term rating because the methodology used to convert the short-term rating into a long-term rating has not been disclosed.
- CAISO Response: Current CAISO credit policy (approved in 2006) states that CAISO will utilize issuer or underlying ratings in its unsecured credit calculation. In the current policy, accommodation is made for entities not having an issuer or underlying rating. A senior long-term unsecured rating can be used if an issuer rating is unavailable but will be lowered by one rating level to account for the risk that the obligations to CAISO have a lower claim priority.

  Current credit policy also accommodates the use of short-term ratings instead of an issuer rating (see Section 3.3 of the Business Practice Manual for Credit Management). Both Moody's and S&P publish equivalent long-term ratings for each of their short-term ratings. Currently, CAISO practice (as highlighted in Section 3.3) is to use the middle equivalent long-term rating when only a short-term rating is available. CAISO's straw proposal to use the lowest equivalent long-term rating instead is a more conservative approach consistent with other credit policy enhancements presented during this stakeholder process.

3. Do you agree with the concept that having a large portion of Total Assets comprised of assets that are generally unavailable to settle a claim such as restricted assets, affiliate assets and derivative assets (i.e., using the net of these asset categories if an offsetting liability is reported) should result in a lower or even no Unsecured Credit Limit? If you

agree, should the ISO specifically exclude these types of assets in the definition of Tangible Net Worth as originally presented or consider them as part of the qualitative assessment in step 8 of the eight-step process as presented in the straw proposal?

- APM Comment: APM does not recommend the exclusion of restricted assets from the definition of TNW unless those assets match a liability reported on the balance sheet. It is APM's opinion that approving this proposal without consideration of a matching liability could result in an understatement of an entity's TNW. However, APM does recommend that CAISO exclude highly volatile assets such as derivative assets from their TNW definition.
- CAISO Response: See previous comments.

4. Do you support the ISO's straw proposal to reduce the current maximum amount of unsecured credit to $150 million on the condition that the ISO reassess this amount with the release of Payment Acceleration and after MRTU has been successfully running through the summer months of next year?

- APM Comment: APM originally recommended that CAISO reduce the maximum amount of unsecured credit assigned to a creditworthy party to $100 million. It is APM's opinion that a lower maximum is appropriate for the current economic environment, and would lower the inherent credit risk related to participation in the CAISO market. In addition, APM believes that further timing efficiencies could be improved upon, which would enable additional reductions to the maximum unsecured credit limit. However, APM supports the incremental downward adjustment to $150 million instead of $100 million as originally proposed by CAISO due to the unknown impact CRRs and/or other MRTU charges may have on the market participants' Estimated Aggregate Liability (EAL) used to calculate their unsecured credit.
- CAISO Response: CAISO agrees that lower limits are an effective means of reducing credit risk. CAISO is committed to further reducing maximum unsecured credit limits on a pro-rata basis with the implementation of Payment Acceleration (i.e., in the same proportion as the reduction in settlement cycle) and after monitoring the impact of MRTU on EAL.

5. Do you support the ISO's straw proposal to accept non-U.S. and non-Canadian guarantees if the ISO adopts strict criteria similar to PJM and MISO? In addition, do you support the straw proposal to adopt MISO's maximum unsecured credit limits based on a minimum country rating and the guarantor's credit quality?

- APM Comment: APM does not recommend CAISO to expand its credit policy to accept Financial Security from other non-US based entities unless those entities possess a physical headquarters based within the US. Both PJM and MISO require foreign entities to maintain an agent for acceptance of service process in the U.S. Therefore, APM recommends CAISO to adopt criteria similar to PJM and MISO when accepting guarantees from non-U.S. and non-Canadian entities. However, APM cannot recommend the assignment of a maximum unsecured credit limit for foreign entities based on MISO's methodology because APM is not aware of the details of this methodology.

- CAISO Response: Like PJM and MISO, CAISO believes the requirement to maintain an agent for the acceptance of service process in the U.S. is an important condition for accepting a foreign guaranty.

  As far as the assignment of unsecured credit limits based on MISO's approach, CAISO recognizes that, in spite of all the restrictive criteria the CAISO may use in allowing a foreign entity to post a guaranty, there may be some residual risk in accepting such guarantees, above the risk of accepting guarantees from domestic entities. As such, CAISO believes it is inappropriate to extend the same levels of unsecured credit to a foreign entity as it would a non-foreign entity. The MISO approach recognized this additional risk by offering lower limits while at the same time recognizing that some foreign entities are a better credit risk than others based on offering different levels of unsecured credit based on credit ratings.

6. Do you support the ISO's continued development of the Affiliate Guaranty? What are your legal department's concerns, if any, with the ISO's form Affiliate Guaranty?

   - APM Comment: APM recommends that CAISO require a Guarantor to provide the same Guaranty for all of its affiliates in the CAISO market in order to mitigate the risk of payment defaults. As a result, APM recommends the continued development of the Affiliate Guaranty.
   - CAISO Response: Noted.

7. With the knowledge that the ISO already has response time built into a collateral request, do you support the ISO's straw proposal to reduce the time to post additional Financial Security to three (3) Business Days?

   - APM Comment: APM supports a reduction to the amount of time CAISO grants its market participants to post additional Financial Security. However, APM maintains its original recommendation to reduce the grace period to two (2) business days rather than the proposed three (3) business days.
   - CAISO Response: In CAISO's opinion, reducing the time to post additional collateral to two (2) business days (versus three (3) business days as proposed in the straw proposal) does not materially further reduce credit risk. As pointed out in the straw proposal, the CAISO has a five business day (i.e., seven (7) calendar day) cushion of coverage built into the current EAL calculation to compensate for the time to respond to a

collateral request. A comparable cushion will continue to exist under the straw proposal. . Accordingly, CAISO believes three (3) business days represents an appropriate balance between relevant factors related to this issue.

8. Do you support the ISO's straw proposal to limit the amount of collateral for a CRR auction to 90% of available credit? Do you agree that Candidate CRR Holders that do not otherwise participate in the ISO market should be excluded from this policy?

   - APM Comment: APM requires more information about the CRR Credit Requirement calculation process before it provides a recommendation.
   - CAISO Response: CAISO encourages APM to contact CAISO credit staff to further discuss any concerns.

9. Upon finalization of all post MRTU design and implementation details of the financial penalties enhancement for late payers, do you support the ISO's straw proposal to assess Market Participants a financial penalty of an amount not to exceed $20,000 calculated as the greater of 2% of the invoiced amount but not less than $1,000 when a Market Participant pays an invoice late two or more times within a rolling twelve month period? Secondly, do you support the straw proposal that reduces a Market Participant's Unsecured Credit Limit to zero and require cash collateral for those Market Participants who pay late a third time within a rolling twelve month period? Thirdly, do you support funding a market reserve account with these financial penalties to a limit of $5,000,000 with any funds in excess of this amount used as a credit toward the GMC revenue requirement in the subsequent year? Lastly, do you support the immediate implementation of the progressive discipline program, as outlined in the straw proposal document?

   - APM Comment: APM recommends the immediate implementation of the progressive discipline program as described above.
   - CAISO Response: Noted.

10. Upon finalization of all post MRTU design and implementation details of the financial penalties enhancement for not posting Financial Security within the posting period, do you support the ISO's straw proposal to assess Market Participants a financial penalty of an amount not to exceed $20,000 calculated as the greater of 2% of the invoiced amount but not less than $1,000 when a Market Participant fails to post Financial Security within the prescribed posting period on the third and each subsequent occurrence within a rolling twelve month period? In addition, do you support funding a market reserve account with these financial penalties to a limit of $5,000,000 with any funds in excess of this amount used as a credit toward the GMC revenue requirement in the subsequent year? Lastly, do you support the immediate implementation of the progressive discipline program similar to the one described for late payers for failing to post on time?

    - APM Comment: APM recommends the immediate implementation of the progressive discipline program as described above.

- CAISO Response: Noted.

11. Considering the Credit Working Group (CWG) structure and governance limitations described in the straw proposal, how would you see the CWG complementing the ISO's existing stakeholder process? Besides Market Participant credit and risk management professionals, who outside the ISO would add value and bring expertise to the CWG?

    - APM Comment: APM recommended the creation of a CWG in order to provide a means to formalize their approach to managing credit policy change. APM believes that a CWG would add value to CAISO by supplying a platform for which future credit policy enhancements can be introduced, and a structured process that would push the development and implementation of these enhancements. APM recommends that CAISO establish a monthly meeting/conference call. These meetings should start by addressing existing credit enhancement proposals, and end with the introduction of new proposals to be discussed in the next meeting.
    - CAISO Response: Noted. CAISO will consider stakeholder comments on this matter, and work to arrange a CWG for future credit policy changes.

12. Please provide detailed pros and cons as well as consequences of the ISO continuing with its existing loss sharing policy. Are there certain credit policy enhancements that more equitably result in Market Participants sharing the risk of participating in the ISO market?

    - APM Comment: APM maintains its original recommendation that CAISO change its loss sharing/chargeback mechanisms to include the allocation of a payment default to all market participants on a pro rata basis. In addition, APM maintains its recommendation that CAISO set a minimum chargeback amount similar to the one imposed by PJM, in which all market participants are required to contribute a minimum of $10,000 regardless of their market participation. APM believes that all market participants should be subject to the same amount of risk in order to promote fairness and foster competition within CAISO.
    - CAISO Response: CAISO is committed to exploring loss sharing and other credit policy enhancements that would better equalize the risk among all Market Participants participating in the CAISO market. Due to widely disparate views on this issue as well as CAISO resource and system constraints as previously described during the course of this stakeholder process, the CAISO will continue discussion of this topic outside of the current credit policy enhancement stakeholder process.

13. Are you in agreement with the ISO's decision to remove the market funded reserve account and credit insurance from further consideration during this stakeholder process?

- APM Comment: APM is in full agreement to remove the market funded reserve account and credit insurance proposals from further consideration during this stakeholder initiative process.
- CAISO Response: Noted.