Stakeholder Comments Template

Subject: Credit Policy Enhancements

Submitted by	Company	Date Submitted
Jerry Green *(916) 574-1296*	*California Department of Water Resources – State Water Project*	*October 3, 2008*

This template has been created for submission of stakeholder comments on the topics covered in the September 22, 2008 Credit Policy Enhancements stakeholder meeting. 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 October 7, 2008 or sooner.

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

1. Do you support CAISO's proposal (Alternative 3) to replace the use of Credit Rating Default Probabilities and Moody's KMV Default Probabilities with the use of agency issuer ratings and Moody's KMV Spot Credit Rating in its eight-step process credit assessment process? Do you agree that these ratings should be blended according to the same percentages already established in the eight-step process? Do you agree that Moody's KMV Spot Credit Rating should be used, according to the same blending percentages, to assess whether a financial institution meets CAISO's "reasonably acceptable" test for accepting a Letter of Credit or an Escrow Account (i.e., the blending must yield a result greater than or equal to four (4.00) to be "reasonably acceptable"?)

   Response: We support using Alternative 3 and we think it's prudent to apply the 50% weighting to Moody's KMV Spot Credit Rating (with the other 50% weighting being a blend of the average of all available credit agency issuer ratings). In determining the amount of unsecured credit the CAISO is willing to provide it is crucial to be able use current up to date market information. To the last question we agree that in order to accept an LOC or an Escrow Account the financial institution should have at least a blended minimum rating of A- (S&P/Fitch) or A3 (Moody's).

2. Do you support CAISO's proposal to expand the definition of Tangible Net Worth to exclude assets that are earmarked for a specific purpose such as restricted assets and assets related to affiliated entities? Do you also agree that CAISO should also exclude highly volatile assets such as derivative assets?

   Response: Yes to both questions.

3. Do you support CAISO's proposal (Alternative 2) to reduce the maximum amount of unsecured credit that it will assign to the most creditworthy party to $100 million?

   Response: Yes.

4. Do you support CAISO's proposal (Alternative 2) to allow Guarantees and other forms of Financial Security to be issued from Canadian entities? Do you support expanding this policy to accept Financial Security from non-US / non-Canadian based entities using rules similar to those adopted by ISO New England if CAISO can clear the legal hurdles and complexities of developing the necessary processes and agreement language for accepting Financial Security from foreign entities? Are ISO-NE's restrictions sufficient and necessary? Should other safeguards be put in place? Should CAISO consider extending this policy to other types of Financial Security such as Letters of Credit?

   Response: I'm not well enough versed in the legal aspects pertaining to this topic but I'm assuming that the legal staff at the CAISO is so if they feel that they have adequately protected the Market Participants we are in favor of accepting Financial Security from foreign entities. That said the more safeguards that could be put in place obviously the better off all Market Participants will be.

5. Do you agree that an Affiliate Guaranty, where a Guarantor backing the obligations of one Affiliate must provide the same Guaranty for all of its Affiliates in the CAISO market, is essential to help mitigate the risk of a payment default by an under-secured and thinly capitalized Affiliate? Does the concept presented present regulatory issues for non-regulated parents backing regulated and non-regulated affiliates?

   Response: Yes we agree that the CAISO should take steps to avoid the types of defaults that took place in the PJM market so yes a Guarantor providing an Affiliate Guaranty should be required to provide the same Guaranty for all of its Affiliates. The credit enhancement proposed by the CAISO in its September whitepaper should be implemented. I can't speak to the second question.

6. Do you support CAISO's proposal (Alternative 1) to reduce the time to post additional Financial Security from five (5) Business Days to three (3) Business Days?

   Response: While the concept of shortening the cure period would allow the CAISO to limit its exposure to weak counterparties, given the current tightening and dislocation in the credit markets, for a counterparty that isn't facing a solvency issue but merely needs to secure approval for an increase in an existing letter of credit or secure a new one, the shorter cure period may not result in the desired outcome. We aren't quite sure how the CAISO fairly handles these different situations but a one-size-fits-all approach may not be suitable.

7. Should CAISO change its policy allowing 100% of Market Participant's available credit (i.e., Aggregate Credit Limit minus Estimated Aggregate Liability) to be available for a Congestion Revenue Rights ("CRR") auction? Is setting the amount of available credit at 90% of available credit a reasonable approach to ensure some buffer remains in place for a Market Participant's other market activities? Should a lower threshold be considered?

   Response: Yes we recommend the CAISO change its policy to allow some buffer and a threshold lower than 90% should be considered.

8. Are you in favor of the CAISO funding a reserve account as a means of providing a source of funds in the case of a payment default? How would you propose that such an account be funded?

   Response: We are in favor of the concept of the CAISO funding a reserve account but obviously there are many details that would need to be discussed and agreed upon by the Market Participants such as the size of a reserve account to strive for and how soon we would want the account to reach the desired level. Of the four assessment mechanisms outlined in the whitepaper (page 19) we are leaning towards an assessment based on dollar values of total monthly settlement statement but probably need to have a clearer understanding of the implications of each of the four mechanisms (or any other that might be in consideration) before taking a more definitive stance on any particular mechanism.

9. Are there other payment default risk mitigation strategies, of those that were presented, that you support and would want CAISO to investigate further such as a Line of Credit, credit insurance, establishing a captive insurance company, developing a blended finite risk program or a capital market transfer to provide potential funding sources in the case of payment default? Are there other strategies that were not covered that CAISO should investigate and/or pursue?

   Response: Based upon reading the whitepaper we aren't in favor of the CAISO pursuing the options (other than the reserve account) discussed in the whitepaper.

10. Do you support CAISO changing its loss sharing/chargeback mechanism to include the allocation of a payment default to all Market Participants – not just net creditors during the default month? What measure should be used to apportion exposure to the chargeback?

    Response: We are in favor of modifying the current methodology for socializing defaults to one that matches other ISO's/RTO's and doesn't put the entire burden on net creditors of the market for the month in which the payment default took place. We don't have any specific recommendation as to how to apportion the chargeback but believe that fairness and equitability should be the goal.

11. Do you agree with CAISO's proposal to assess financial penalties on Market Participants who are late in paying their invoices two or more times in a rolling 12 month period? Are the financial penalties sufficient to ensure compliance with the payment provisions of the CAISO Tariff? Do you agree that Market Participants who are late a third time in a rolling 12 month period should also have to post cash in lieu of any unsecured credit for a period of 12 months of on-time payments? Do you agree that any penalties collected should fund a reserve account that can be used as a source of funds in the case of a payment default?

    Response: We are in favor of the proposal to assess financial penalties to those Market Participants who are late in paying their invoices two or more times in a rolling 12 month period (unless of course there was some sort of a "force majeure" event that prevented meeting the 10 a.m. PPT deadline). We don't know if the financial penalties are sufficient to ensure compliance but what the CAISO has suggested is a decent place to start.

    We are very much opposed to requiring a Market Participant to post cash in lieu of any unsecured credit if that Market Participant is late in making timely payments for a third time in a rolling 12 month period (obviously this requires a qualifier since the amount of "lateness" is important; a little late requiring cash in lieu of unsecured credit is too harsh, if the lateness is "days" then yes that Market Participant should be required to post cash in lieu of any unsecure credit).

    We are in agreement that any penalties collected should go towards funding the reserve account that will be used as source of funds to cover payment defaults.

12. Do you agree with CAISO's proposal to assess a financial penalty on a Market Participant who is late in posting additional collateral on the third and each subsequent time in a rolling 12 month period? Are the financial penalties sufficient to ensure compliance with the collateral posting provisions of the CAISO Tariff? Do you agree that any penalties collected should fund a reserve account that can be used as a source of funds in the case of a payment default?

    Response: We have mixed feelings about whether or not the CAISO should assess a financial penalty for failure to post additional collateral on the third and each subsequent time in a rolling 12 month period. With respect to the first alternative of assessing a Market Participant a nominal penalty of $1,000 we wouldn't think that would be enough of an incentive on its own but we aren't adverse to implementing such a policy as a means to help fund a Reserve Account. To the penalty associated with the second alternative (not to exceed $10,000) our thoughts on this are similar to our response to topic number 6 (shortening the cure period) above in that we believe some judgment by the CAISO should be warranted based on the specific circumstance. If the Market Participant is making a good faith effort to provide additional Financial Security (such as in the situation where they are trying to either increase the amount on an existing LOC or secure a new LOC) than assessing up to a $10,000 penalty doesn't seem appropriate. If a counterparty is in the midst of a solvency situation assessing up to a $10,000 penalty probably is a futile endeavor.

13. Do you support the creation of a Credit Working Group ("CWG") as a means to formalize the CAISO's approach to managing credit policy change? How do you envision the CWG adding value to CAISO's existing stakeholder process (e.g., regularity of meetings, membership, etc.)?

    Response: We support creating a Credit Working Group as both a means to formalize the CAISO's approach to managing credit policy change as well as a mechanism for credit people to exchange ideas and discuss pertinent topics. If topics warranted it the CWG could meet quarterly or semiannually or as appropriate if there was a need and an interest within the group given that people are busy and there is no need to make this a burden as the intent is to foster communication and an exchange of ideas to the benefit of the CAISO markets and policies.