

Stakeholder Comments Template

Subject: Credit Policy Enhancements

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 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"?)

Powerex is generally in agreement with the CAISO's proposed Alternative 3.

Powerex also strongly suggests that the CAISO should review both exposure and ratings on a daily basis to ensure market participants are not inadvertently exposed to credit risks due to participation in the CAISO market.

The current process of calculating exposure and reviewing ratings weekly is inadequate in the current credit environment especially given the large quantity of money that will be clearing through the CAISO markets under MRTU.

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?

Powerex generally agrees with the proposal to expand the definition of TNW to exclude highly volatile assets. However, Powerex does not support the exclusion of restricted assets from TNW without further discussion to ensure some parties are not unfairly penalized.

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?

Powerex strongly supports the reduction of the maximum UCL to \$100 million (Alternative 2). The CAISO should also consider adding a concentration limit to UCL similar to the 20% of receivables as per the ISO-NE and NYISO credit policies.

Post- Payment Acceleration, Powerex supports another review of the UCL to see if the maximum amount can be further reduced.

In the event the CAISO decides not change the current loss sharing mechanism (Question 10 below), Powerex would support a much lower UCL of \$10 million or a fully collateralized system.

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?

Powerex supports Alternative 2 and agrees with the CAISO that the current credit instruments with Canadian entities are appropriate.

Powerex believes the CASIO should consider Alternative 3 for non-US/non-Canadian based entities based on rules similar to those adopted by ISO-NE subject to successful resolution of legal hurdles.

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?

Powerex agrees in principle with CAISO proposal. However, Powerex feels that cross default clauses between affiliates and the ability to net positions in the event of a default would be very effective in avoiding situations similar to what occurred at PJM.

Powerex also asks the CAISO to clarify whether an affiliate with its own credit rating requires an affiliate guaranty from its parent company or whether the CAISO would rate the affiliate as a stand-alone market participant.

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?

Powerex supports shortening the time allowed to post additional security and has a strong preference for two Business Days. Powerex suggests the lead time to process an LC may not necessarily be a factor in considering a cure period as the participant would always have the option to raise cash to cover the collateral call while waiting for the LC.

Powerex also suggests that the CAISO consider an earlier security call combined with a graduated timeframe for the posting of collateral. For example, allow three days for posting additional collateral at 80% and two days for posting additional collateral at 90%.

Powerex also strongly suggests that the CAISO calculate EAL on a daily basis to further reduce any credit exposure.

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?

Powerex supports setting the amount of available credit for the CRR auction at 80%-90%.

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?

Powerex supports developing a reserve account funded by financial penalties collected as per Questions 11 and 12, below.

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?

Powerex supports the CAISO exploring other default risk mitigation strategies and believes that one of the strategies should include that employed by NGX, where participants are required to fully secure their positions.

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?

Powerex strongly supports Alternative No. 1 since it aligns the interests of all market participants in regards to credit risk and is consistent with other ISOs/RTOs. Aligning the interests of all market participants with respect to credit risk will also align the interests of market participants on most other initiatives such as payment acceleration and unsecured credit limits and agreement on these initiatives can be more easily reached.

In addition the current mechanism may lead to reliability issues when suppliers, in response to an expected or foreseen default, curtail their participation in the CAISO markets. The current mechanism requires suppliers/net creditors to build in this incremental credit risk, compared to other ISOs/RTOs, into their market participation. Therefore, the CAISO should recognize that aligning their loss sharing/chargeback mechanism with other ISOs/RTOs will remove this risk adder and disincentive to supply into the CAISO markets.

The CAISO should also specifically consider the potential reliability issues arising out of a market participant failure, and subsequent supplier incentives to withdraw from the market under the current loss sharing/chargeback mechanism. If participants know that a default will be charged to them disproportionately as net creditors, then they will either remove themselves from the market, or charge a significantly large premium to justify continued participation. When the amount of the default cannot be known with any certainty the premium to justify continued participation will have to be enormous, and in some cases, no amount of premium can justify the risk exposure and continued participation.

The default chargeback mechanism is related to many of the other topics discussed here and in the Payment Acceleration forum. In Powerex opinion, any defaults should be spread amongst all market participants according to their gross participation in the market. In this case, if a market participant does default then suppliers wouldn't have the same incentive to stop selling or start purchasing energy from the CAISO in order to reduce their net exposure. The Gross allocation method won't also unfairly leave a few participants that have net positions outstanding, paying for a larger portion of the default when compared with their participation in the overall market.

Also settling the DA market within a few days of trading (as part the Payment Acceleration project) will materially reduce the amount of actual exposure in the event of a default.

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?

Powerex is in general agreement with all elements of the CAISO proposal, including assessing financial penalties to Market Participants who are late more than once in a rolling 12 month period, the loss of the use of unsecured credit when late a third time, the amount of the penalty, and the use of any penalties to fund a reserve account.

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?

Powerex believes the elements of the CAISO proposal for late payment should also apply to late posting of additional collateral including the loss of the use of unsecured credit. In addition, the CAISO should take all actions already allowed under its tariff if collateral is not provided when required.

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.)?

Powerex supports the creation of a CWG. Powerex could envision the CWG providing the CAISO with a means to keep their credit policies in tune with other markets and would supplement and expedite the existing stakeholder process by providing robust credit policy recommendations and skipping directly to the Straw Proposal stage.