Southern California Edison ("SCE") hereby submits its comments on the California Independent System Operator's (CAISO's) final draft proposal on Enhancements to California ISO Credit Policy, dated November 10, 2009.

SCE appreciates the opportunity to submit comments regarding the proposed enhancements to the CAISO's credit policy. SCE's comments will be divided in to two sections; the first section will be comments related to the presentation discussed at the November 17th stakeholder conference call and the second section will be specific comments related to the Credit Business Practice Manual (BPM) changes.

SCE Comments on November 17th Stakeholder Meeting

1. Calculation of Unsecured Credit Limit

SCE continues to support the CAISO's proposal to simplify the calculation of Unsecured Credit Limits (UCL). Specifically, SCE supports the CAISO proposal to: (1) conversion of a market participants short term rating to a lowest equivalent long term rating if only a short term rating exists, (2) blend the Moody's KMV equivalent rating and the lowest credit agency issuer rating, (3) replace the default probability table with fixed percentage of Tangible Net Worth (TNW) or Net Assets (NA) based on Moody's KMV and lowest credit agency rating, and (4) simplify the current 8-step process to 6-steps.

2. Definition of Tangible Net Worth

SCE continues to support the CAISO desire to exclude from the determination of a stakeholders unsecured credit limit certain assets such as assets reserved for a specific purpose (restricted assets, affiliate assets), derivative assets, and other assets reasonably believed to be unavailable to settle a claim. SCE also supports the CAISO retaining the ability to reduce a market participants UCL, as part of the qualitative assessment step of the new 6-step process to address assets that the CAISO deems risky or highly volatile.

3. Reduction in Maximum Amount of Unsecured Credit to $150 Million

SCE continues to oppose the CAISO's proposal to modify the maximum amount of unsecured credit a market participant can be awarded prior to observing actual market exposures under MRTU. Ultimately a reduction of the maximum unsecured credit limit to $150 million or something lower may be prudent but without actual market results any reduction will be based on an arbitrary assumption of MRTU market volumes. SCE continues to recommend the CAISO wait until 1 year after the start of MRTU to make the determination on a reduction in the maximum unsecured credit limit.

If the CAISO continues to move forward with the reduction of the maximum amount of unsecured credit SCE requests the CAISO to provide additional clarification on its intent to further reduce the maximum amount of unsecured credit on pro-rata basis when payment acceleration goes live. Specifically, SCE request the CAISO to clarify if the pro-rata reduction will be a 1 for 1 percentage reduction or will the CAISO adjust the percentage of unsecured credit reduction based on actual MRTU market exposures? SCE has concerns that any further reductions without first determining a baseline maximum unsecured credit limit using actual MRTU market exposure could cause a reduction that is not realistic given the MRTU market volumes.

4. Guarantees from Foreign Entities

SCE supports the CAISO final proposal to accept guarantees from non-U.S. companies per the strict criteria described in the draft final proposal. SCE further, supports the CAISO only accepting a foreign guarantee from companies with a credit rating of A-/A3 or better and limiting the maximum amount of a foreign guarantee to $25 million.

5. Blanket Parental Guarantees

SCE remains opposed to the CAISO's proposal to require that parents who provide a guarantee to one of its affiliates participating in the CAISO market extend that guarantee to all of its affiliates, regardless of the fact if those affiliates may already be providing the CAISO with their own sufficient financial security. As previously stated SCE feels that the foundation for a sound credit policy is the development of credit rules that provide the CAISO with sufficient financial security to cover the potential market exposure of each individual market participant, not introducing the concept of blanket affiliate guarantees. CAISO should focus its efforts in the development of credit monitoring tools and systems that provide them with the means to continuously mark to market each individual market participants financial position and develop the processes and procedures to react to rapid changes in an individual market participants financial situation in near real-time. Individual affiliates of a parental company are individual corporate entities who may have completely different business models, risk tolerances, and market objectives. Accounting for these differences by requiring a parental guarantee to be a blanket guarantee blurs the line between individual corporations and pools risks together instead of properly accounting for the risks of each affiliate individually.

Furthermore, SCE believes the CAISO proposal discriminates between market participants who fall under a blanket guarantee and those who do not. First, the CAISO proposal, with respect to potential default, treats market participants who are under a blanket affiliate guarantee differently than a market participant who is not. Secondly, the CAISO's proposal limits the ability for market participants operating under a blanket affiliate guarantee from utilizing the full denomination of available collateral to participate in the CAISO market while not placing the same restrictions on market participants not operating under such a guarantee.

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Differential Treatment Under Potential Default Conditions

The blanket affiliate guarantee proposal put forth by the CAISO allows the CAISO to reallocate excess collateral (in the form of the guarantee) from one affiliate to another affiliate. The CAISO argues this provision, acting as a backstop mechanism, will reduce the default risk to the market by accessing the excess collateral of one affiliate to cover the potential losses of another. The CAISO does not have this same backstop mechanism for market participants not operating under a blanket affiliate guarantee who exceed their collateral and subsequently default on a portion of their outstanding balance.[1] Rather, the only protection the CAISO has against exposure to a default, if an individual market participant is not operating under a blanket affiliate guarantee, is the collateral requirements of the individual market participant.

SCE views this differential treatment of participants as potentially discriminatory. In effect, it requires parent companies offering a guaranty with multiple entities doing business in the CAISO to provide superior credit support for their affiliates, as compared to a stand-alone entity doing business with the CAISO. The CAISO should not penalize – through supplemental credit requirements – companies that have multiple entities doing business in the CAISO. Rather, each stand-alone entity should have comparable credit standards, irrespective of whether or not it has affiliates in the CAISO's markets.

The result of this discriminatory approach may result in reducing competition in the CAISO. That is, an entity may want to do business with the CAISO via multiple affiliates, but it requires the use of parental guarantees to do this. At the same time, the CAISO's proposed rules make such guarantees close to unmanageable, and in the end may create an unnecessary barrier that prevents this entity from doing business with the CAISO.

By allowing a guarantee to offset the potential default risk between affiliates the CAISO proposal does not apply the same credit mechanisms for different entities, and ultimately discriminates between market participant operating under a blanket affiliate guarantee and those who do not. The end result may be reduced competition.

Restricts Full Participation in the CAISO Market

By allowing the CAISO to reallocate excess collateral (in the form of the guarantee) from one affiliate to another affiliate the CAISO's proposed blanket affiliate guarantee has the potential to create the perverse result of reducing the total credit/collateral available to the CAISO. While the CAISO's proposal does not require a corporate parent to enter into a blanket affiliate guarantee it does require that if such a guarantee is extended to one affiliate it must be extended to all. This requirement even applies to affiliates that operate completely autonomously from its other affiliates, and that are perfectly able and willing to post sufficient collateral to the CAISO for their stand-alone market

[1] It is important to note that the CAISO is not proposing to reallocate excess collateral from one affiliate to another for affiliates who do not operate under a guarantee.

participation. A result of this requirement and the CAISO's authority to reallocate collateral between affiliates, unlike today, a parent company may be unable or unwilling to issues any guarantees at all.

In contrast, the CAISO has no such collateral reallocation rights between affiliates or individual market participants who are not operating under the proposed affiliate blanket guarantee.

Thus, rather than this proposal providing additional collateral to the market, SCE is concerned it may, in effect, backfire, and parental guarantees – including any excess collateral provided by these guarantees that the CAISO currently enjoys - may be viewed as too risky to the provider, and thus none will be issued. That is, under current rules parental guarantees can be judiciously allocated and managed on an individual affiliate basis. The CAISO's proposal removes the ability for parental guarantees to be managed with precision, and instead adopts a "guarantee one, guarantee all" broad-brushed approach to the issue, and as a result, in instances of multiple affiliates, the CAISO may lose access to parental guarantees altogether.

Furthermore, if a parent is required to guarantee both a regulated and unregulated affiliate under a blanket guarantee, there are additional disparate impacts as a result of the regulated utility's obligations under the California Public Utilities Commission's Affiliate Transactions Rules. Because the regulated utility is required to maintain independence from its parent company under the Commission's ring-fencing requirements, the requirement that the parent must guarantee the regulated utility's obligations simply because the parent is guaranteeing the affiliate will impose additional administrative burdens on the regulated utility to ensure that the blanket guarantee does not create a material change to the ring-fencing requirements and to ensure that it is clear to the creditors of the parent, the regulated affiliates, and the unregulated affiliate that the blanket guarantee does not commingle the assets of the separate entities and does not entitle any creditor to look to the regulated utility's assets to satisfy an obligation of the parent or unregulated affiliate. If the blanket guarantee proposal moves forward, then there should be an explicit exemption for regulated utilities.

In summary, SCE feels that the CAISO's proper focus should be on establishing adequate and non-discriminatory credit requirements for all market participants individually. The CAISO's proposed blanket affiliate guarantee discriminates between market participants and may in fact, have the effect of eliminating parental guarantees, and may also create a barrier that reduces entry and competition in the CAISO's markets. SCE's position remains that the appropriate protection for all CAISO market participants is for the CAISO to ensure that its credit and other requirements provide sufficient protection depending on the risk profile of each individual company and each individual affiliate.

However, if the CAISO continues to move forward with the proposal as documented in the draft final proposal SCE advises that the CAISO include clear language in its tariff, BPM, and the guarantee itself clearly stating that under the CAISO's blanket guarantee proposal "Under no circumstances will the CAISO commingle assets or collateral of each of the individual affiliates operating under the guarantee. The CAISO may only access assets of the guarantor."

6. Reduction in Collateral Posting Time

SCE continues to support the CAISO's proposal to reduce the time required to respond to a collateral call from (5) business days to (3) business days.

7. Maximum Amount of Collateral Available for CRR Auction

SCE continues to supports the CAISO's proposal to limit the amount of collateral for a CRR auction to 90% of a participant's available credit. SCE agrees with the CAISO's decision to apply this rule to all Candidate CRR holders, even those Candidate CRR holders who otherwise do not participate in the ISO market.

8. Financial Penalties for Late Payers

SCE continues to support the CAISO's proposal to assess financial penalties when a market participant pays an invoice late two or more times within a rolling twelve-month period. SCE further supports the CAISO's proposal to reduce a market participants Unsecured Credit to $0 and require cash collateral for those participants who pay late a third time within a rolling twelve month period. However, SCE continues to oppose funds resulting from financial penalties being used to fund a market reserve account, rather SCE supports using such funds to offset GMC charges.

9. Financial Penalties for Failure to Timely Post Collateral

SCE continues to support the CAISO's proposal to assess financial penalties when a market participant fails to post financial security within the prescribed posting period the third and each subsequent occurrence within a rolling twelve-month period. However, SCE continues to oppose funds resulting from financial penalties being used to fund a market reserve account, rather SCE supports using such funds to offset GMC charges.

10. Loss Sharing Methodology

SCE supports the CAISO's decision to not include the policy discussions to modify the current tariff defined default loss sharing methodology with the current proposed credit policy enhancements. This issue was already addressed and decided in the development of MRTU. Further, the current rules were a key factor in SCE's decision to support MRTU – proposal to change these foundational rules even before MRTU starts is unjustified. The current rules allocate risk in proportion to net receivables and prevent the unjust and unreasonable result of forcing market participants that must schedule both supply and demand through the CAISO from being forced to support credit for the rest of the market. We see no compelling reason to change the current rules.

SCE Comments on Credit BPM Changes

4.1 Purpose of Unsecured Credit Limit
The UCL is the level of credit established for a Market Participant that is not secured by any form of Financial Security. A maximum UCL of ~~$250~~ $150 million has been specified in CAISO Tariff. The purpose of this limit is to protect CAISO and its participants from undue exposure caused by the default of an individual Market Participant. This limit has been set based on a maximum of 95 days of charges outstanding according to the current CAISO payment calendar.

SCE Comment: Last sentence references the $250 million dollar limit is based on a maximum of 95 days of charges outstanding according to the current payment cycle. Is that sentence still relevant given the $100 million dollar reduction?

~~5.~~45.6 Financial Security through Affiliates
In those cases where a Market Participant is a subsidiary or affiliate of another entity and prefers to utilize the consolidated financial statements and other relevant financial information of that entity for obtaining credit, a signed corporate guaranty is required. A guarantor is considered reasonably acceptable and a corresponding Financial Security Amount is set based on the guarantor's credit evaluation according to the same procedures that a Market Participant undergoes as described in Section 3.1, Unsecured Credit Assessment Requirements. If the guarantor has two or more subsidiaries or affiliates participating in the CAISO market, the guaranty must back the obligations of each subsidiary or affiliate by executing a variation of CAISO's form Guaranty, referred to as an Affiliate Guaranty.

SCE Comment: If CAISO continues to move forward with its blanket affiliate guarantee proposal SCE advises the CAISO to add language to its BPM to state that under such a guaranty: "Under no circumstances will the CAISO commingle asset or collateral of each of the individual affiliates operating under the guarantee. The CAISO will only access assets of the parent guarantor."