

FERC ORDER NO. 741 IMPLEMENTATION

FERC ORDER NO. 741 MANDATES	CAISO	ERCOT ¹	ISO NEW ENGLAND	MISO	NYISO	PJM
Limit the amount of unsecured credit extended to any market participant or aggregate corporate family to no more than \$50 million.	The maximum amount of unsecured credit available to any market participant or group of market participant affiliates is \$50 million. ²	Unsecured credit is subject to a \$50 million limit and is granted solely within ERCOT’s discretion. The \$50 million cap also is applied at the “corporate family” level. ³	Effective October 1, 2011, ISO NE lowered to \$50 million the limits of certain types of credit that it previously extended above \$50 million and limited the amount of unsecured credit extended to a corporate family to no more than \$50 million. ⁴	MISO is in compliance and does not extend Unsecured Credit exceeding \$50 million to any market participant or aggregate corporate family. ⁵ Filing date: 6/30/11 Effective date: 10/1/11	The maximum amount of unsecured credit available to any one Market Participant, or group of affiliated Market Participants is \$50 million. ⁶	The total amount of unsecured credit allowance, whether from a market participant’s own creditworthiness or from a guaranty, is capped at \$50 million. ⁷ On November 29, 2011, PJM proposed tariff revisions in compliance with FERC’s September 15, 2011 Order on PJM’s Order No. 741 Compliance Filing to ensure that Seller Credit, which is a form of unsecured credit, is included as part of the \$50 million unsecured credit allowance cap. ⁸
Adopt a settlement period of no more than seven days with an additional seven days to receive payment.	The CAISO has a weekly settlement cycle, issuing invoices every Wednesday , with payment due four business days later. ⁹	In 2011, ERCOT approved Protocol changes to tighten the Real Time settlement and payment cycle: (i) Combining Real Time settlements with DAM settlements into one “daily” invoice with both DAM and RT settlement statements on it; and (ii) Shortening the RT payment timeline by two bank business days. The “daily” invoice will be paid within 3 bank business days instead of five. These changes should ensure that approximately 90% of Real Time days are settled and paid within 15 days with the weighted average settlement and payment cycle being no more than 15	Effective January 26, 2011, ISO NE has implemented twice-weekly billing for hourly charges. ¹¹	MISO is in compliance and invoices on the seven-day settlement of charges and credits (S7) and requires payment within seven days. ¹² Filing date: 6/30/11, 12/14/11 Effective date: 10/1/11	NYISO Services Tariff Section 7.2 and OATT Section 2.7.3 established, effective October 1, 2011, a weekly settlement cycle for approximately 99% of the dollar volume of NYISO-administered market transactions.	PJM’s settlement period for most products and services is one week. Payment on all invoices is due within three business days. ¹³

¹ ERCOT is not subject to FERC regulation or the requirements of FERC Order No. 741. Nevertheless, the ERCOT Protocols and proposed revisions are comparable to the credit reform requirements of FERC Order No. 741.

² See CAISO Tariff § 12.1.1.

³ ERCOT Creditworthiness Standards.

⁴ ISO New England and New England Power Pool, 136 FERC ¶ 61,191 (2011), available at http://www.iso-ne.com/regulatory/ferc/orders/2011/sep/er11-3953-000_9-15-11_credit_order.pdf.

⁵ Link to filing: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-06-30%20Docket%20No.%20ER11-3970-000.pdf>.

⁶ See NYISO Services Tariff Section 26.5.2.

⁷ PJM Tariff, Attachment Q, Section II.F.

⁸ PJM Interconnection, L.L.C., November 29, 2011 Filing, Docket No. ER11-3972, at 13.

⁹ See CAISO Tariff § 11.29.2 & 11.29.10.

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		days. Settlement and payment timelines longer than the above are expected to be primarily due to weekend and holiday schedules. These Protocol changes are expected to be implemented in 2012. ¹⁰				
Eliminate unsecured credit in the financial transmission rights market.	Market participants are required to post secured collateral for bidding or holding CRRs. ¹⁴ A federal agency is deemed to have provided secured collateral if it provides a letter executed by an officer that: (1) attests that the federal agency is lawfully authorized to participate in the CRR Auction and that any debt the federal agency incurs due its participation in the CRR Auction is a debt of the United States; (2) identifies the current year’s appropriations for the federal agency from the United States Congress; and (3) verifies that the amount of the current year’s appropriations for the federal agency from the United States Congress meets or exceeds the amount required to satisfy the credit requirements set forth in Section 12.1. ¹⁵	In 2011, Protocol changes were approved that will ensure that the CRR Auction and CRR forward mark-to-market values are fully collateralized rather than being subject to unsecured credit. These changes are expected to be implemented in 2012. ¹⁶	Effective January 26, 2011, ISO NE has eliminated the use of unsecured credit for FTRs. ¹⁷	MISO is in compliance and has eliminated the use of Unsecured Credit to support financial transmission rights (FTR) allocations and exposure. ¹⁸ Filing date: 2/3/11, 6/30/11 Effective date: 4/5/11, 10/1/11	Market Participants are required to post collateral, and are not permitted to use unsecured credit, to satisfy credit requirements for bidding on or holding TCCs. ¹⁹	In the FTR market, unsecured credit is not allowed, and collateral, which is required on a portfolio basis based upon path-specific historical values, must be established prior to bidding into the auction. ²⁰ On November 29, 2011, PJM proposed tariff revisions in compliance with FERC’s September 15, 2011 Order on its Order No. 741 Compliance Filing to remove the possibility that Seller Credit, which is a form of unsecured credit, could be used as credit for FTRs. ²¹

¹⁰ ERCOT Protocol, Sections 9.5.4, 9.7, 9.9, and 9.11.

¹¹ *ISO New England and New England Power Pool*, 132 FERC ¶ 61,046 (2010), available at http://www.iso-ne.com/regulatory/ferc/orders/2010/jul/er10-942-000_7-16-10_order_unsecured_credit.pdf. Notice of effective date available at http://www.iso-ne.com/regulatory/ferc/filings/2010/nov/er10-2933-001_11-18-10_unsecured_credit.pdf.

¹² Links to filings: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-06-30%20Docket%20No.%20ER11-3970-000.pdf>; <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-12-14%20Docket%20No.%20ER11-3970-000.pdf>.

¹³ PJM Tariff, Section 7.1A.

¹⁴ *See* CAISO Tariff § 12.6.2.

¹⁵ *See* Tariff § 12.6.2.2.

¹⁶ ERCOT Protocol, Sections 16.11.4.1 and 16.11.4.6.

¹⁷ *ISO New England and New England Power Pool*, 132 FERC ¶ 61,046 (2010), available at http://www.iso-ne.com/regulatory/ferc/orders/2010/jul/er10-942-000_7-16-10_order_unsecured_credit.pdf. Notice of effective date available at http://www.iso-ne.com/regulatory/ferc/filings/2010/nov/er10-2933-001_11-18-10_unsecured_credit.pdf.

¹⁸ Links to filings: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-02-03%20Docket%20No.%20ER11-2831-000.pdf>; <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-06-30%20Docket%20No.%20ER11-3970-000.pdf>.

¹⁹ *See* NYISO Services Tariff Sections 26.5 and 26.6.

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Reinforce the ability of the ISO/RTO to offset market obligations owed to market participants against market obligations owed by market participants.	The CAISO expects to file tariff revisions to become a central counterparty to all market transactions by April 30, 2012.	ERCOT expects to adopt the central counterparty model. To that end, ERCOT has initiated due diligence actions designed to ensure the central counterparty alternative can be implemented consistent with all legal obligations and policy purposes that apply to ERCOT as the independent system operator in the ERCOT Region of Texas. These actions include, but are not limited to, investigating the impact on ERCOT’s corporate structure, working with its regulators and market participants to develop all necessary support, and developing and reviewing the most effective means of effectuating the central counterparty approach.	ISO NE has prepared a package of tariff changes that will establish it as central counterparty for market participant transactions. These tariff changes are currently being considered in ISO NE’s stakeholder process. ISO NE expects to file the proposed tariff changes on April 30, 2012. ²²	MISO requested an extension of time to meet this requirement in order to more fully explore the central counterparty approach. MISO initially pursued the security interest option to address this requirement but recently received overwhelming stakeholder support for a central counterparty approach. ²³ Motion date: 1/17/12 Requested filing extension date: 4/30/12	The NYISO anticipates taking title as a central counterparty beginning in Q2 or Q3 2012, contingent upon the NYISO receiving an Advisory Opinion from the New York State Department of Taxation and Finance confirming that taking title will not affect the NYISO’s tax exempt status. Based upon informal conversations with the New York State Department of Taxation and Finance, the NYISO anticipates receiving an Advisory Opinion in February or March 2012.	Effective January 1, 2011, PJM revised its OA and Tariff to establish PJMSettlement Inc. as the central counterparty to transactions in the PJM markets. According to the FERC filing, “[t]he purpose of the filed revisions is to clarify that there is a single, specified counterparty to market participants with respect to all ‘pool’ transactions in the markets operated by PJM and for transmission service.” ²⁴ Under the new PJM regime: - PJMSettlement takes “title to all power that is purchased and sold in the ‘pool transactions’ in the [PJM-administered] markets” ²⁵ ; - the revisions to PJM’s structure establish that “PJMSettlement will be a buyer to each market seller and a seller to each market buyer, <i>taking title to electricity and other products and assuming liability for payables, in its own name and right</i> ” ²⁶ ; and - the interposition of PJMSettlement as a counterparty in PJM-administered markets does not extend to certain bilateral contracts and self-supply transactions (which PJM considers to be non-pool transactions, which is to say,

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PJM Tariff, Attachment Q, Section V.A.

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FERC permitted the use of unsecured credit allowance for FTRs acquired prior to the June 2009 auction, noting that the elimination of the use of an unsecured credit allowance will be complete after May 2012. *PJM Interconnection, L.L.C.*, 136 FERC ¶ 61,190, at P 27 (2011).

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Motion for Extension of Time pending at FERC, available at http://www.iso-ne.com/regulatory/ferc/filings/2012/jan/rm10-30-000_1-9-12_ordr_741_extension.pdf.

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Link to motion: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2012-01-17%20Docket%20No.%20RM10-13-000.pdf>.

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PJM Filing with FERC, *PJM Interconnection, L.L.C., and PJM Settlement, Inc.*, Docket No. ER10-1196-000, at 1 (May 5, 2010).

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Id. at 9.

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Id. (emphasis added).

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						outside of the organized markets it administers). ²⁷
Limit the time period by which a market participant must cure a collateral call to no more than two days.	A market participant has two business days to resolve a request from CAISO for additional collateral, either by posting the collateral or by demonstrating to the ISO’s satisfaction that it is not necessary. ²⁸	If an entity’s Total Potential Exposure, as defined in the Protocols, equals or exceeds its credit limit (<i>e.g.</i> , its financial security plus its unsecured credit, if applicable), ERCOT requires the entity to post additional collateral within two bank business days. ²⁹	Effective October 1, 2011, ISO NE has reduced the permissible time in which to cure a collateral call to no more than two days in two instances where the cure period had previously been more than two days ³⁰	MISO is in compliance and requires all market participants to cure collateral calls within 2 Business Days. ³¹ Filing date: 6/30/11 Effective date: 10/1/11	Market Participants must cure collateral calls within two business days from the date of the NYISO’s request, or any shorter time period specified by the NYISO. ³²	The PJM Tariff provides that a participant has two business days from notification of a breach or a collateral call to remedy the breach or satisfy the collateral call. ³³
Provide minimum participation criteria. that applies equally to all market participants	Market participants must attest annually (subject to ISO verification) that they satisfy minimum participation requirements related to capitalization, risk management, training and operational capabilities to comply with CAISO directions. ³⁴	Through its stakeholder process, ERCOT is in the process of developing new eligibility requirements specifying that a counterparty must: - have appropriate expertise in markets; - have appropriate operational capabilities to respond to ERCOT directions; - meet minimum capitalization requirements; and - maintain a risk management framework appropriate to the ERCOT markets in which it transacts or wishes to transact. Counterparties will be required to provide an annual certification that they have met these requirements, attested by an officer of the company. ERCOT also is proposing minimum capitalization requirements. Proposed	Effective October 1, 2011, new Section II.A in the Financial Assurance Policy establishes minimum criteria for participation in ISO NE’s markets. The criteria require that market participants annually submit a list of principals and a description of, <i>inter alia</i> , any material litigation, sanctions imposed by the FERC, SEC, or CFTC, any bankruptcies, mergers or acquisitions, and any operations in wholesale electricity markets other than ISO NE’s markets. In addition, ISO NE has established capitalization requirements for customers and applicants. Certain small participants are exempted from these requirements. ISO NE also requires that each market participant annually submit certificates that attest that the participant has: risk management procedures and internal	MISO has revised its Tariff to require market participants to meet the minimum participation criteria, including capitalization requirements, in order to remain certified and transact in the market. ³⁹ MISO’s minimum participation criteria apply to all market participants. ⁴⁰ Filing date: 6/30/11 Effective date: 12/31/11	NYISO Services Tariff Section 26.1 sets forth minimum participation criteria related to capitalization, risk management, training, and operational capabilities that each Market Participant must satisfy, and at all times remain in compliance with, to participate in the NYISO-administered markets.	The PJM Tariff currently includes a two-pronged set of minimum participation requirements. The first prong requires market participants to provide an annual certification by a senior officer during a period beginning January 1 and ending April 30. For market participants applying to become new PJM members, such certification must be provided together with the prospective member’s credit application. Appendix 1 to Attachment Q of the PJM Tariff sets forth the certification form, which requires certain representations regarding the participant’s risk management policies and transaction activities. If the participant fails to comply with these provisions, or the certification itself, the participant will be ineligible to transact in the PJM markets. Furthermore, certain FTR Participants must provide

²⁷ *Id.*

²⁸ *See* CAISO Tariff § 12.4.1.

²⁹ ERCOT Protocol, Section 16.11.5 (3).

³⁰ *ISO New England and New England Power Pool*, 136 FERC ¶ 61,191 (2011), available at http://www.iso-ne.com/regulatory/ferc/orders/2011/sep/er11-3953-000_9-15-11_credit_order.pdf.

³¹ Link to filing: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-06-30%20Docket%20No.%20ER11-3970-000.pdf>.

³² *See* NYISO Services Tariff Sections 26.11.

³³ PJM Tariff, Attachment Q, Section VII.

³⁴ *See* CAISO Tariff § 12.1.

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		capitalization requirements are higher for counterparties transacting or wishing to transact in the CRR markets. Counterparties who fail to meet the capitalization requirements would be required to post an “Independent Amount” in addition to any collateral posted with respect to market positions. ³⁵ Each Counter-Party must meet ERCOT’s creditworthiness standards. ³⁶	controls appropriate to the risks that it enters in the market; trained personnel related to its participation in New England Markets; and procedures in place to effectively communicate with ISO-NE. ³⁷ ISO-NE has also filed with FERC, in December 2011, a proposal to include an additional step involving the annual submission by some FTR market participants and other market participants that pose an unreasonable risk to the markets of those entities’ risk management procedures. Under the proposal, ISO-NE also reserves the right to request that any other participant (based on identified risk factors) provide its risk management procedures to ISO-NE. ³⁸			PJM with a copy of their current governing risk control policies, procedures and controls. The second prong addresses participant capitalization requirements. A participant establishes full compliance with the minimum capitalization requirements through audited financials showing either tangible net worth in excess of \$1 million or tangible assets in excess of \$10 million if the participant is active in the FTR market, and half of either amount if the participant is not active in the FTR market. Compliance could be established either by the participant itself or through a guaranty from a compliant guarantor. Participants that are not fully compliant would be allowed to transact through a third party who meets the eligibility standards, or through the provision of collateral (only cash or a letter of credit held by PJM). The “collateral option” requires a minimum \$500,000 of collateral for participants that are active in the FTR market and \$200,000 of collateral for participants that are active in virtual bidding but not FTRs. A 10% reduction would be assessed on all collateral beyond those minimums and the remaining collateral value would then be available to satisfy PJM’s normal

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ERCOT Protocol, Section 16.2.1, 16.8.1, 16.11.5(c), 16.11.4.1, 16.16 (pending implementation).

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ERCOT Protocol, Section 16.11.1.

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ISO New England and New England Power Pool, 136 FERC ¶ 61,191 (2011), available at http://www.iso-ne.com/regulatory/ferc/orders/2011/sep/er11-3953-000_9-15-11_credit_order.pdf.

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http://www.iso-ne.com/regulatory/ferc/filings/2011/dec/er11_3953_002_12-8-11_risk_assessment.pdf.

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Link to filing: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-06-30%20Docket%20No.%20ER11-3970-000.pdf>.

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Link to MISO Tariff: <https://www.misoenergy.org/Library/Tariff/Pages/Tariff.aspx>.

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PJM Tariff, Attachment Q, Section Ia.

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Id., Attachment Q.

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						credit requirements. ⁴¹ PJM’s credit policy applies to all Participants. ⁴²
Provide examples of when a market administrator may invoke the “material adverse change” to justify requiring additional collateral.	Section 12.1.1.5 of the CAISO Tariff lists examples of circumstances constituting a “material change in financial condition” that would permit the CAISO to reduce any unsecured credit available to the affected entity and, as a result, require it to post additional collateral. Examples include a credit agency downgrade, certain financial restatements, and a default in another market.	ERCOT may request additional collateral if ERCOT determines that the calculated exposure does not adequately match the financial risk created by a Counter-Party’s activities under the Protocols. ⁴³	Effective October 1, 2011, ISO NE has added two examples of what may constitute a “material adverse change” ((1) the sanctioning of the market participant or non-market participant transmission customer or any of its principals by the Commission, the Securities and Exchange Commission, the CFTC, any exchange monitored by the National Futures Association, or any entity responsible for regulating activity in energy markets; and (2) a significant change in the market participant’s or non-market participant transmission customer’s market capitalization) and revised the Financial Assurance Policy to provide that, in the event of a material adverse change, the ISO may require additional financial assurance or a different form of financial assurance. ⁴⁴	MISO updated its Tariff by supplementing pre-FERC Order 741 material adverse change measures to add a significant increase in credit default spreads and a significant decrease in market capitalization to material adverse change measures. ⁴⁵ Filing date: 6/30/11 Effective date: 10/1/11	NYISO Services Tariff Section 26.13 sets forth examples of circumstances when the NYISO may declare a material adverse change as justification for requiring additional collateral (e.g., a significant decline in a Market Participant’s market capitalization, a significant increase in a Market Participant’s credit default swap spreads).	PJM may independently determine that there is a material change in the financial condition of a participant from available information regardless of whether the participant has informed PJM of the change. In its FERC Order No. 741 compliance filing, PJM added three additional illustrative examples to the list of what constitutes a material change in financial condition: (i) a financial default in another organized wholesale electric market, futures exchange, or clearing house; (ii) revocation of a license or other authority by any Federal or State regulatory agency, where the license or authority is required or important to the participant’s continued business, such as a market-based rate authorization or a State license to serve retail load; ⁴⁶ and (iii) a significant change in credit default spreads, market capitalization, or other market-based risk measurement criteria, such as a recent increase in Moody’s KMV Expected Default Frequency that is noticeably greater than the increase in its peers rates, or a collateral default swap premium normally associated with an entity rated lower than investment grade. This third addition specifically provides illustration of possible forward-looking metrics which PJM may utilize in determining whether a material adverse change has occurred. If PJM determines that a participant is

⁴³ ERCOT Protocol, Section 16.11.4.1 (3).

⁴⁴ *ISO New England and New England Power Pool*, 136 FERC ¶ 61,191 (2011), available at http://www.iso-ne.com/regulatory/ferc/orders/2011/sep/er11-3953-000_9-15-11_credit_order.pdf.

⁴⁵ Link to filing: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-06-30%20Docket%20No.%20ER11-3970-000.pdf>.

⁴⁶ PJM also revised Sections I.A.5 and I.B.5 of Attachment Q of the PJM Tariff to add that the existence of ongoing investigations of the participant by the CFTC are required to be disclosed.

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						required to provide financial security because of a material change in financial condition, PJM will provide the participant with a written explanation of why such determination was made. ⁴⁷
Engage in periodic verification of market participant risk management policies and procedures.	On December 14, 2011, the CAISO filed proposed tariff revisions with FERC to establish a periodic process for verification of risk management policies and procedures of market participants that hold CRR portfolios that meet certain risk criteria.	Within the scope of the proposed eligibility requirements, market participants would be subject to periodic verification of their risk management framework to be performed either by ERCOT or an agent acting on ERCOT’s behalf. ⁴⁸	As discussed above, the annual certification requirement became effective on October 1, 2011. ⁴⁹ Additional risk management assessment process was filed on December 8, 2011 and is pending at FERC. ⁵⁰	MISO’s filed revisions to its Tariff requiring that all market participants certify the implementation of risk policies and procedures and subjecting the actual policies and procedures to mandatory evaluation on either a random or identified risk basis. ⁵¹ Filing date: 12/14/11 Expected effective date: 2/13/12	Pursuant to Services Tariff Section 26.1.3, the NYISO may require any Market Participant, at any time, to submit its risk management policies and description of internal controls to the NYISO for review. In addition to this existing discretion to request risk management policies and procedures from any Market Participant, on December 14, 2011, the NYISO filed proposed tariff revisions with FERC to establish a periodic process for verification of risk management policies and procedures with respect to Market Participants that pose significant risk in the TCC market. A copy of this filing is available at: http://www.nyiso.com/public/ .	PJM has proposed to verify officer certifications, described above, for all participants speculating in PJM’s FTR markets by requiring such participants to submit applicable risk control policies for review. Additionally, PJM proposes to apply this same verification requirement periodically as a spot check, either randomly or based on identified risk factors, on other market participants to reinforce the importance of the annual officer certification. ⁵² Such review will include verification that: (1) the risk management framework is documented in a risk policy addressing market, credit and liquidity risks; (2) the Participant maintains an organizational structure with clearly defined roles and responsibility that clearly segregates trading and risk management functions; (3) there is clarity of authority specifying the types of transactions into which traders are allowed to enter; (4) the Participant has requirements that traders have adequate training relative to their authority in the systems and PJM markets in which they transact; (5) as appropriate, risk limits are in place to control risk exposures; (6) reporting is

⁴⁷ PJM Tariff, Attachment Q, Section I.B.3.

⁴⁸ ERCOT NPRR 438 (pending stakeholder process).

⁴⁹ *ISO New England and New England Power Pool*, 136 FERC ¶ 61,191 (2011), available at http://www.iso-ne.com/regulatory/ferc/orders/2011/sep/er11-3953-000_9-15-11_credit_order.pdf;

⁵⁰ http://www.iso-ne.com/regulatory/ferc/filings/2011/dec/er11_3953-003_12-8-11_risk_assessment.pdf.

⁵¹ Link to filing: <https://www.misoenergy.org/Library/Repository/Tariff/FERC%20Filings/2011-12-14%20Docket%20No.%20ER11-3970-000.pdf>.

⁵² PJM Tariff, Attachment Q, Section Ia.A (as revised by PJM’s further compliance filing submitted to FERC on November 29, 2011 in Docket No. ER11-3972-002).

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						<p>in place to ensure that risks and exceptions are adequately communicated throughout the organization; (7) processes are in place for qualified independent review of trading activities; and (8) as appropriate, there is periodic valuation or mark-to-market of risk positions. If principles or best practices relating to risk management in PJM-type markets are published by a third-party industry association, PJM, following stakeholder discussion and notice, may apply such principles or best practices in determining the sufficiency of the Participant’s risk controls. PJM may retain outside expertise to perform this review and verification. A Participant’s continued eligibility to participate in the PJM markets is conditioned upon PJM notifying the Participant of successful completion of PJM’s verification. If within 14 days of notification of unsuccessful completion of the verification process, the Participant demonstrates to PJM that it has filed with FERC an appeal of PJM’s risk management verification determination, then the Participant will retain its transaction rights pending FERC’s determination on the appeal.</p>