

**Summary of Preliminary Input on
Potential Areas for Commercial and Tort Liability
Relating to RTO West Activities**

- Risk that parties receiving services from RTO West will not pay for those services. (Please see attached paper entitled “Credit Issues Associated with RTO West Service” for a detailed discussion of this issue.)
- Incremental risk associated with changes in credit status of parties that previously satisfied creditworthiness standards.
- Potential for catastrophic damages and class actions because of:
 - Outage liability
 - Cascading events
 - Failure (in Washington, at least) to timely restore service
 - Expansion of duty beyond the direct customers of the PTO providing service.
- Consequences of dispatch instructions or actions; consequences from approving or scheduling facility outages.
- Possible “gaps” or ambiguities in Agreement Limiting Liability – examples:
 - Who’s responsible for “conditions” (subsection 4.3) caused by poor maintenance (subsection 4.2) on facilities operated by RTO West?
 - What type of interconnection facilities is RTO West assuming liability for contact claims in subsection 4.3?
 - Does the save, defend and hold harmless commitment in subsection 4.3 apply to contacts with those interconnection facilities as well as to facilities operated by RTO West?
- Third-party liability issues need to be addressed in the Tariff. A decision needs to be made as to whether Transmission Customers should enter Service Agreements with RTO West or not. The decision should turn on analysis of the risks and benefits of establishing contractual privity with customers not signatory to the Liability Agreement and the RTO, taking tort and financial liability into account.
- Liability issues should be addressed in any Seams Agreements. We would recommend the subcommittee consider whether an agreement among RTOs similar to the Liability Agreement is necessary and beneficial.

- To the extent RTO West is granted backstop authority in the planning area that might expose it to third-party tort liability, the subcommittee should consider what protections may be available.
- The Scheduling Coordinator Agreement needs to be drafted in a manner insuring the creditworthiness of SCs and protecting PTOs and RTO West from financial liability as a result of failures of an SC. The subcommittee should coordinate with the Scheduling workgroup and propose appropriate provisions for inclusion in the Tariff and SC Agreement.
- As noted above, consideration should be given to whether a Transmission Customer is responsible for liabilities not paid by an SC and /or for the cost of service should an SC default on payments to the RTO. Appropriate Tariff provisions should be proposed and a decision made whether to require customers to enter service agreements with the RTO.
- Consideration should be given to financial security for payment to the RTO when it is the provider of ancillary services to customers. It would seem limiting RTO West's exposure from the provision of ancillary services is no different than its exposure for providing transmission service, but the subcommittee should review this assumption.
- If the RTO as a vendor purchases Integrated Operations Services, do we need an IOS purchase agreement with appropriate liability protections built in. Absent a provision for consequential damages, how can the RTO remain whole if a IOS provider defaults on its obligation in a high market?
- Paying Agent Agreement: The paying agent is a fiduciary who is exempt from certain liabilities. Have we protected the parties to the agreement from malfeasance or negligence of the Paying Agent?

Liability Issues (Other than Tort claims)*

1. Who/what is at risk if a consumer of transmission services purchased from RTO West does not pay? Who/what is at risk if a Scheduling Coordinator does not pay?
2. Who is at risk if a buyer of an FTR in the RTO West market does not/cannot pay? Does it make any difference if the buyer is a consumer-owned cooperative? A publicly-owned PUD? An investor-owned Utility? DSI? Marketer? Broker? ITC?
3. Who is at risk if a buyer of AS does not pay for services it purchases?
4. Who/What is at risk (and what are the consequences) if the supplier for AS doesn't deliver?
5. Who/what is at risk if RTO West goes bankrupt? For what costs? Who is at risk if a Scheduling Coordinator goes bankrupt? Paying Agent? Consumer-owned Cooperative? A publicly owned utility (e.g., East Cupcake PUD)? A Marketer? A broker? A service company? A DSI? An investor-owned PTO? A distribution investor-owned utility that joined an ITC?
6. What happens if a state legislature/PUC refuses to allow RTO Costs to be passed through to IOU customers?
7. What happens to transfer payment agreements if a utility is sold?
8. Who is at risk if RTO West fails to set its uplift charge high enough? Who/what is at risk if a PTO fails to set its transmission rates high enough?
9. Who/what is at risk if RTO West's credit rating is lowered and its cost of debt rises?
10. Who/what is at risk if RTO West can't sell more debt to fund capital program?
11. Who/what is at risk if a broker/marketer/other entity can't meet a margin call?
12. Who is at risk if there is an error in settlement? Checkout? Billing? Metering? Load forecasting? Dispatch instructions by the RTO
13. Who is at risk for RTO operating mistakes? Who pays for risk associated with property or financial loss from such a mistake? What about mistakes by PTOs? Scheduling Coordinators?
14. Who/what is at risk if a PTO/other entity refuses to follow an RTO order?

15. Who/what is at risk if RTO West breaches its tariff? TOA? LIA? GIA? OFSA?
What if breach is caused by Scheduling Coordinator?
16. Who/what is at risk if a PTO breaches its TOA? LIA? GIA?
17. Who/what is at risk if the security coordinator fails to keep the lights on?
18. Who/what is at risk if firm load isn't served because of a failure of RTO West to provide AS in its role as a provider of last resort?
19. Who is at risk for an RTO West Force Majeure (labor strike? act of God? Uncontrollable force?)
20. Who is at risk if BPA can't pay its bills?
21. Who is at risk if BPA can't meet its payments to Treasury?
22. Who/what is at risk if a merchant function of a PTO fails to honor non-converted agreements?
23. Who is at risk if RTO West is hit with attorneys' fees in litigation/arbitration? Fines? Punitive damages?
24. Who/what is at risk if RTO West uses transmission facilities of a PTO that has superfund clean-up liability?
25. Who is at risk for errors and omissions of the board of directors of RTO West? Executive Officers?
26. Who/what is at risk for RTO West employee misconduct?
27. Who/what is at risk if RTO West changes the business environment in which a non-PTO utility operates?
28. Who/what is at risk if RTO West changes flow paths after translation of existing contracts and the value of allocated FTRs change?
29. Who/what is at risk if RTO West fails to plan appropriately?

Tort Liability Issues

We see the following types of potential tort suits:

1. Fender benders and other accidents caused by or involving RTO employees and equipment.
2. Employee suits on various issues relating to hiring, firing, promotions, etc on a variety of grounds.
3. Environmental liability in managing hazardous waste, pollutants, etc under the control of RTO West. An example might be an Electro Magnetic Force suit alleging various kinds of harm from exposure to high voltage radiation.
4. Allegation of negligence implementation of RTO West/TOA standards involving operational issues resulting in outages causing damages to equipment and property (e.g., freezer jam) and lost profits. E.g, suits seeking recovery of increased costs to a utility because RTO West allegedly failed to maintain adequate reliability standards.
5. Suits alleging RTO West fails to control noxious weeds in its approval of maintenance plans.
6. Interference with contract rights when it changes flow paths, thereby rendering some FTRs less valuable.
7. Allegations that RTO West failed to manage its markets properly—FTRs, AS, other.

*Note: While we have brainstormed the list of possible liability issues, we have not complimented this list with recommended or actual remedies already in place in the RTO West proposal. We recognize there are many remedies available to solve these problems!

CREDIT ISSUES ASSOCIATED WITH RTO WEST SERVICE

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There are several basic credit risk questions concerning transactions with RTO West:

1. Which party bears the risk of non-payment for each service contained in the RTO West Tariff and each transaction undertaken by RTO West pursuant to the TOA?
2. Is the party that bears the ultimate credit risk also the party that manages the credit relationship for the transaction?
3. If RTO West is managing credit for transactions for which other parties assume the ultimate credit risk, what is the procedure to protect the party bearing the risk and can that procedure be changed without that party's consent?
4. Can a Scheduling Coordinator act for more than one PTO and/or other entity and thus put one PTO at risk of a default by company loads of another PTO?
5. Conversely, can a Scheduling Coordinator limit itself to be a Scheduling Coordinator for only one PTO?

A list of possible transactions to analyze against the foregoing questions would include:

- Case 1. A PTO, acting solely as its own Scheduling Coordinator, purchases transmission and ancillary services from RTO West for its own Company Loads in states that have not deregulated;
- Case 2. A Scheduling Coordinator (energy marketer or other qualified entity) purchases transmission and ancillary services for loads on a PTO system in a state that has deregulated;
- Case 3. A Scheduling Coordinator purchases transmission and ancillary services from RTO West for: (i) Company Loads on two different PTO systems; or (ii) Company Loads on two different PTO systems and an aggregator's deregulated load.
- Case 4. A network wholesale load in a state that does not deregulate acts as its own Scheduling Coordinator and purchases transmission and ancillary services from RTO West at Company Rates of a PTO.
- Case 5. Party X purchases FTRs sold by RTO West on behalf of a PTO.

- Case 6. RTO West collects funds for services (such as the uplift charge) for services provided by RTO West.

The Scheduling Coordinator Application Outline produced in Stage 1 contains the following statement:

J.1.4 SC Billing

The SC must maintain a contractual relationship with the entities it represents. The SC is responsible for payment of charges for all services provided under the RTO WEST Tariff as defined in Appendix G and the Service Schedules.

[To what extent was a decision reached in Stage 1 that the credit relationship would be with the Scheduling Coordinator, and to what extent was it decided that this would be the exclusive credit relationship?]

It appears to be implicit in the Transmission Operating Agreement (“TOA”) and the Agreement Among RTO West and Transmission Owners to Use Paying Agent (“Use of Paying Agent Agreement”) that the individual Participating Transmission Owner (“PTO”) bears the risk of non-payment for the Company Rate portion of the billing but not for any charges for services provided by RTO West (and presumably not for FTRs).

Section 14.2.3 of the TOA provides that RTO West bills Company Loads for the Company Rate "as a billing agent for the Executing Transmission Owner." RTO West "shall have no ownership interest in the proceeds or receivables of the amounts billed by RTO West as the billing agent for the [PTO]." (§ 14.2.3). The bills prepared by RTO West "shall provide for payment of the Company Rate portion of the bill directly to a paying agent designated by the [PTO]." (§ 14.2.3). Again "as billing agent" for the Executing Transmission Owner, RTO West imposes delinquent charges on late payments, which charges are based on the tariff of the Executing Transmission Owner. The last sentence of § 14.2.3 of the TOA then gives RTO West the right, as billing agent, to "employ such actions to collect delinquent payments and such remedies for nonpayment" as it employs for delinquent payments due RTO West, supplemented by remedies established pursuant to the lawful rate schedules of the PTO. Based on this language, one might conclude that the RTO West's role in collecting revenues for Company Rates is merely as an agent for each Executing Transmission Owner. Therefore, it appears that the PTO bears the risk of nonpayment and the RTO does not spread the risk of non-payment to all customers.

In addition, section 7(d) of the Use of Paying Agent Agreement provides that RTO West's billings to customers "on behalf of each Transmission Owner" may be combined with other bills for other Transmission Owners, but the bill for each Transmission Owner must be separately identified. Thus, the separate billings allow for the tracking of exactly which loads are paying their bills and which are not. The risk of non-payment can therefore fall on the PTO whose Company Load is not paying. Like the TOA, the Use of Paying Agent Agreement provides that the RTO is merely the billing

agent for the owner. (§ 7(a)). The TOA also provides that the RTO has no ownership interest in the proceeds. (§ 14.2.3). The Use of Paying Agent Agreement specifically provides that the revenues from the bills are "the revenue and property of the Transmission Owners . . . in their individual capacities." (§ 8). It would seem to follow that the shortfalls have to fall to the transmission owners as well.

For reference as a drafting guide, the Billing and Settlements Content Group looked at Appendix G of the Desert Star Tariff, which contains a method of payment of the PTO, which is expressly conditioned upon receipt of funds from the Scheduling Coordinator. Section G.7 of Desert Star Appendix G.

In Case 1, as described above, under the TOA and the Use of Payment Agent Agreement it is inferred that the risk of non-payment of the Company Rate by the Company Load remains with the PTO. RTO West has no credit risk. The TOA and the use of Payment Agent Agreement expressly provide that the funds which are paid never become property of RTO West. There is no new credit management issue in this case. Bonneville would bear the risk of non-payment of any wholesale customer on its system. IOU PTO's would bear the risk of non-payment for their retail loads on their systems in states that have not been deregulated.

In Case 2, RTO West would be extending credit to a creditworthy party (depending on credit deposit requirements). Is the creditworthy party the Scheduling Coordinator, the transmission customer, or both? Assuming that the creditworthy party is the Scheduling Coordinator, in a deregulated state the Scheduling Coordinator will likely not be the PTO. To the extent that a transmission customer in a deregulated state is using a PTO's system the ultimate payment of the Company Rate would be payable to the PTO. Question: To what extent do the PTO's credit risk management policies extend to RTO West's extension of credit? Can the PTO direct RTO West to cut off transmission and ancillary service transactions to a Scheduling Coordinator that is at its limit of credit in an overall credit arrangement with the PTO, or can RTO West allow those limits to be exceeded?

In Case 3, assuming that the creditworthy party is the Scheduling Coordinator, what happens if only one of the multiple transmission customers pays the Scheduling Coordinator, while the others default? Does the Scheduling Coordinator make payments to the PTO's pro rata? How do the two PTOs jointly manage the credit risk?

In Case 4 the transmission customer is the also the Scheduling Coordinator. The credit issues raised are essentially the same issues as those raised in Case 2.

In Case 5, RTO West is conducting an auction to sell Firm Transmission Rights for congested paths. The proceeds belong to the PTOs, or to other FTR holders. Question: Is the auction on a credit basis or on a cash-up-front basis, and if on a credit basis, what is the extent of possible value that might be at risk for the credit sale conducted by RTO West? Who gets to set the credit limits?

In Case 6, RTO West has a credit relationship with a purchaser of the services from RTO West and the funds belong to RTO West. There is no credit management issue for PTOs. RTO West's own credit policies placed in the RTO West Tariff will govern any non-payment issues, and RTO West would raise its rates to offset any bad debts. Thus, the credit risk is spread to all RTO West customers.