

# Memorandum

**To:** CAISO Board of Governors

**From:** Anna McKenna, Counsel  
Charles A. King, P.E., VP, Market Development & Program Management

**Date:** March 1, 2007

**Re:** Briefing on Upcoming Congestion Revenue Rights (CRR) Tariff Filings

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*This memorandum does not require Board action.*

## EXECUTIVE SUMMARY

The California Independent System Operator Corporation (CAISO) is currently engaged in a number of activities to facilitate implementation of the Market Redesign and Technology Upgrade (MRTU) on January 31, 2008. One of these activities is preparation for the first annual and monthly Congestion Revenue Rights (CRR) Allocation and Auction, which is scheduled to take place this summer and which will distribute CRRs to be effective at the start of MRTU. The CAISO will be allocating through the CRR Allocation process three types of CRRs: 1) seasonal CRRs for on-peak and off-peak hours, that span over a one-year period (*i.e.*, Seasonal CRRs); 2) seasonal CRRs for on-peak and off-peak hours, that span over a ten-year period (*i.e.*, Long-Term CRRs); and 3) monthly CRRs for on-peak and off-peak hours (*i.e.*, Monthly CRRs) for the first month of MRTU. In addition, the CAISO will be awarding Seasonal CRRs and Monthly CRRs for the first year of MRTU through the CRR Auction process and will be allocating CRRs to entities that sponsor new transmission upgrades or expansions but do not elect to recover the cost of their transmission investment through the Transmission Access Charge or other regulatory mechanism.

In order to allocate and auction CRRs, the CAISO must obtain specific information on Existing Transmission Contracts (ETCs), Converted Rights (CVRs) (contract rights brought to the CAISO when new entities became Participating Transmission Owners) and Transmission Ownership Rights (TORs) (facilities in the CAISO Control Area not under the CAISO's operational control). The CAISO must also obtain and verify certain necessary information from entities that intend to participate in the CRR Allocation and must also register and qualify entities that intend to participate in either the CRR Allocation or CRR Auction or that intend to obtain CRRs through the Secondary Registration System (*i.e.*, Candidate CRR Holders). In support of this effort, the CAISO will be supplementing its Tariff with additional implementation detail consistent with policies previously approved by the CAISO Board of Governors and conditionally approved by the Federal Energy Regulatory Commission (FERC). The CAISO would have filed this detail with its original MRTU filing on February 9, 2006, but was not able to do so at that time because it had not yet fully developed

the implementation details. The CAISO did, however, at that time file for authority to collect and verify the required CRR Source and CRR Sink information and to register and qualify Candidate CRR Holders.

The CAISO intends to file make this filing with the FERC on March 9, 2007. In that same filing, the CAISO will also request authority to conduct the information collection and verification for TRTC Instructions, and the registration and qualification of Candidate CRR Holders, prior to the effective date of the MRTU, so that CRR Allocation and Auction activities can be conducted and completed in a timely manner.

The CAISO is not requesting any action from the Board of Governors on this matter as all the proposed changes are consistent with previously approved policy for MRTU, but provides this informational memorandum to advise the Board of CRR related regulatory activities, as they are critical to implementation and are important to interested stakeholders.

## **DISCUSSION**

### **I. Information Required In Preparation for the First Annual CRR Allocation and Auction**

#### **A. Transmission Rights and Transmission Curtailment (TRTC) Instructions**

As approved by the FERC, the CAISO will be honoring ETCs, TORs, and CVR under the MRTU. The CAISO will be honoring such rights by affording valid and balanced ETC, TOR and CVR Self-Schedules: 1) a scheduling priority over other Self-Schedules in the event that uneconomic adjustments are required; and 2) the "perfect hedge," which consists of the complete reversal of any charges associated with the Marginal Cost of Congestion component of Location Marginal Prices (LMPs) under MRTU. In order to receive such preferred treatment under MRTU, ETC, TOR and CVR<sup>1</sup> Self-Schedules must be validated and balanced according to operating instructions to be provided by transmission owners of the facilities that are affected by such rights (*i.e.*, Participating Transmission Owners, Non-Participating Transmission Owners and New Participating Transmission Owners). These operating instructions are provided in what going to be called TRTC Instructions under MRTU, which consist of detailed descriptions of transmission service requirements under such rights. The CAISO will model these rights in its allocation and auction of CRRs based on the TRTC Instructions and the forecasted usage of such rights. A high-level specification of the content of the TRTC Instructions is set forth in Sections 16.4.5 and 17.1.4 of the MRTU Tariff.

The "perfect hedge" treatment for such rights means that the CAISO will not be collecting Congestion revenue from valid and balanced ETC, TOR and CVR Self-Schedules. At the same time, the payments made to entities that hold CRR are funded by the congestion revenues collected through the LMPs charged to entities that use the transmission grid. Therefore, pursuant to Section 36.4 of the MRTU Tariff, it is incumbent upon the CAISO to properly model and evaluate use of these rights in its allocation and auctioning of CRRs to prevent the perfect hedge treatment of ETCs, TORs, and CVRs from causing revenue inadequacy. Consequently, in its distribution of CRRs the CAISO must account for the prospective use of such rights in its markets to ensure that the CAISO distributes CRRs such that revenue adequacy risk is minimized. The CAISO will, therefore, be accounting for such rights in its simultaneous feasibility tests conducted in the allocation or auction of such rights.

Since these provisions were initially filed in the MRTU Tariff, the CAISO has developed additional details of necessary information that are contained in the draft Business Practice Manual for Market Operations and in the guideline documents and template through which these instructions will be collected. The CAISO will be supplementing its tariff

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<sup>1</sup> Note that CVR Self-Schedules are afforded the scheduling priority and perfect hedge only in the Day-Ahead Market and not in the Real-Time Market.

provisions with additional detail it believes it should have included in its initial filing. This includes the following additional detail:

- a) a requirement that parties provide physical sources and sinks for validation of ETC, TOR and CVR Self-Schedules as scheduling priority is provided only to physical sources and sinks, as well as clarification that custom Load Aggregation Points are physical sinks;
- b) a requirement that parties specify which Scheduling Coordinator will be entitled to the "perfect hedge" settlement given that different Scheduling Coordinators may submit ETC, TOR or CVR Self-Schedules at the applicable sources and sinks for such schedules; and
- c) a requirement that parties specify the source/sink resource maximum capacity (MW) that can be scheduled.

In addition, the CAISO will be requesting that parties provide the CAISO with forecasted usage of such rights for the annual and monthly period that CRRs will be in effect. This forecasted usage will be considered by the CAISO in its modeling of ETCs, TORs and CVRs.

The TRTC Instructions and forecasted usage information will be collected from the relevant parties this spring in preparation for the first annual and monthly CRR Allocation and Auction to commence later this summer. The CAISO will be working with Participating Transmission Owners, Non-Participating Transmission Owners and New Participating Transmission Owners to complete the TRTC Instructions. Recognizing that parties will be required to better understand nodal modeling and the way such rights will be honored under MRTU, the CAISO has adopted a business process to work with the relevant transmission owners to assist them in the completion of the TRTC Instructions. This is necessary because parties do not have experience in dealing with the nodal model and the CAISO will be required to assist them in identifying the appropriate locations as identified in the Full Network Model as they relate to rights under their contracts and ownership.

#### **B. Load Eligibility for Participation in CRR Allocation**

A Candidate CRR Holder's eligibility in the annual or monthly CRR Allocation will be based on the entity's load metric which is based on the entity's load duration curve that is exceeded only 0.5 percent of the time in the relevant season or month based on the entity's historical load data (for the annual process) and load forecast data (for the monthly process). Therefore, the CAISO will be required to obtain and verify load duration curves from all Candidate CRR Holders that intend to participate in the CRR Allocation to be held this summer. Because the tariff provisions that allow the CAISO to conduct such activity will not be in effect until the start of MRTU, in its March 9 filing with FERC, the CAISO will be requesting authority to conduct such activity in advance of the general effectiveness of the MRTU Tariff.

#### **C. Source Verification**

In the first annual CRR Allocation process, load serving entities will be required to demonstrate and the CAISO will verify that such entities hold rights to actual physical sources either through ownership or by contract for nomination of such sources in the allocation process. As filed in its current MRTU Tariff, the CAISO was intending to use the fiscal year 2004-2005 for verification that such rights were held by parties. Most recently, through the stakeholder process on Long Term CRRs, stakeholders have requested and CAISO management has agreed to move the historical year to 2006. In addition, the CAISO will be considering any potential changes to the source verification rules in light of lessons learned from the latest CRR Dry Run. The CAISO will be making a filing later this spring (approximately March 30) for any necessary changes to the tariff and will also be requesting that FERC authorize

the CAISO to conduct its collection and verification of sources during the pre-CRR Allocation and Auction period later this spring.<sup>2</sup>

## II. Registration and Qualification of CRR Entities

Consistent with Section 36.5 of the MRTU Tariff as conditionally approved by FERC in its September 21 Order, only entities that are registered and fully qualified as Candidate CRR Holders or CRR Holders may obtain CRRs through the CAISO CRR Allocation, CRR Auction or Secondary Registration System. Candidate CRR Holders are entities that have been fully registered and qualified to obtain CRRs either through the CRR Allocation, CRR Auction or Secondary Registration System. CRR Holders are entities that have been qualified as Candidate CRR Holders by the CAISO and have since obtained CRRs either through the CRR Allocation, CRR Auction or Secondary Registration System.

In order to qualify and be registered as a Candidate CRR Holder with the CAISO, parties must fulfill creditworthiness and training requirements. Even entities that are already registered with the CAISO as Scheduling Coordinators must meet these additional requirements and therefore, even such entities must go through the Candidate CRR Holder registration and qualification process. The CAISO will, however, seek to find synergies with existing registration information for such entities and will eliminate redundancies in the application of a Scheduling Coordinator seeking to also become a Candidate CRR Holder as appropriate.

Once such parties and the CAISO have completed the registration and qualification process, in order to qualify as a Candidate CRR Holder, a party must execute a CRR Entity Agreement. The CRR Entity Agreement is a pro forma agreement that requires the Candidate CRR Holder or CRR Holder to comply with all the requirements of the tariff that apply to such entities. This is a necessary agreement for the CAISO because the parties that will be participating in obtaining CRRs are not necessarily Scheduling Coordinators and, even if they are Scheduling Coordinators, new tariff provisions will apply to any Candidate CRR Holder or CRR Holder that do not apply to Scheduling Coordinators.

## III. Stakeholder Process

The proposed changes are consistent with previously approved policy that was fully vetted through the stakeholder process prior to the CAISO filing its MRTU Tariff on February 9, 2006. In addition, the CAISO has provided for a stakeholder process to review the specific proposed tariff changes to be made as follows:

- February 13, 2006 – Presentation to PRAG regarding filing and TRTC and CRR activity in preparation for first annual and monthly CRR Allocation and Auction;
- February 15, 2006 - Posted proposed changes to tariff language, including changes to the TRTC Instructions; new provisions for registration and qualification of entities that intend to obtain CRRs through the allocation, auction or the Secondary Registration System; the pro-forma agreement; and specific guidelines not to be filed but that will be used in working with transmission owners to prepare the TRTC Instructions;
- February 20, 2006 – Presentation and discussion of proposed changes at the MRTU Implementation Workshop

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<sup>2</sup> These changes to the tariff are scheduled to be made with FERC in a March 30, 2007 filing. At this time, the CAISO does not believe that any of these changes will be material deviations from the MRTU policy previously approved by the ISO Board of Governors. In the event that such changes are found to be material deviations, management will apprise the ISO Board of Governors of any such changes.

- February 27, 2006 - Presentation and discussion of proposed changes at the MRTU Implementation Workshop
- February 15 to March 6 – Stakeholder comment period on proposed changes. Comments to be provided to the CAISO Board after March 6.
- Filing at FERC March 9, 2007