Comments of Pacific Gas and Electric Company

Real-Time Imbalance Energy Offset Straw Proposal

Submitted by		Company	Date Submitted
Ian Quirk	(415) 973-9798	PG&E	May 11, 2011

Pacific Gas & Electric (PG&E) appreciates the opportunity to participate in the stakeholder process for the California Independent System Operator's (CAISO) Impact of Convergence Bidding on Real-Time Imbalance Energy Offset initiative and to submit comments regarding the April 27, 2011 Issue Paper and Straw Proposal.

PG&E supports the CAISO pursuing a short-term settlement rule related to the Real-Time Imbalance Energy Offset (RTIEO) and making an emergency filing to implement it if the proposed thresholds are reached before Board approval. However, we also suggest the CAISO initiate a stakeholder process to develop mid and long-term solutions to the underlying factors creating this uplift. Finally, we seek clarification on the technical details of the proposed settlement rule.

1. Summary of CAISO Proposal

Proposed Settlement Rule for RTIEO

The RTIEO is a market uplift allocated to measured demand. The size of the uplift is driven largely by price differences between HASP and RTD. Though the size of this price divergence is not directly affected by Convergence Bidding, a specific strategy using matched convergence bids can be used to increase the magnitude of the RTIEO.

In order to mitigate the impact of convergence bidding on this uplift, the CAISO has proposed a two phased solution. The short-term fix is a settlement rule which eliminates the profitability for any single scheduling coordinator using a matched pair of convergence bids to profit from differences between HASP and RTD prices. Second, longer-term solution will be pursued through the Renewable Integration Phase 2 initiative.

Emergency Filing

The CAISO has proposed that it will make an emergency filing to FERC if the 30-day rolling cumulative RTIEO attributable to matched convergence bids exceeds $25 million. PG&E understands the CAISO would request the FERC approve the immediate implementation of the CAISO's proposed short-term fix.

2. Comments on Proposed Fix

PG&E Supports Implementing the Proposed Settlement Rule as a Short-Term Fix

Both PG&E and the Department of Market Monitoring (DMM) have been tracking this issue since the early months of MRTU, and it is now well known that convergence bids can be used in a manner which dramatically increases the uplift. For this reason, PG&E is supportive of the CAISO completing this stakeholder process to reduce the impact of this behavior.

Weaknesses in the Settlement Rule Warrant the Development of Mid-Term and Longer-Term Solutions on an Expedited Basis

While we support immediate implementation of the short-term fix presented in this proposal, we also acknowledge this fix has flaws and is not an acceptable long-term solution. PG&E sees two major problems that warrant the pursuit of a long-term fix on an expedited basis.

First, the proposed fix does nothing to address the underlying structural problem creating the RTIEO in the first place. Even before convergence bidding went into effect, the RTIEO was large (roughly $120 million in 2010). As long as structural market differences result in a HASP and RTD price divergence, the potential for price arbitrage via convergence bids remains. It is PG&E's position that work should begin immediately to address this structural market design issue.

Second, the settlement rule only applies if a single scheduling coordinator has a matched position. It is possible that market participants could get around this provision through the use of financial swaps or direct cooperation with affiliates or a third party. Participants could also use a physical transaction to take the other side of the matched pair to avoid this settlement rule. While this behavior may not begin immediately, it will almost surely develop if price divergence remains between HASP and RTD. This weakness again highlights the need to begin developing a more sustainable solution on an expedited timeline.

The CAISO has suggested it will develop a long-term solution through Phase 2 of its Renewable Integration Initiative, but the market design phase of this initiative may span several years. For this reason, PG&E recommends the CAISO immediately begin another stakeholder process to investigate intermediate-term solutions that do not require wholesale market design changes.

Potential ideas for this intermediate-term solution could include changes to the prices that HASP bids settle on or making all virtual bids settle between day-ahead and real-time. Alternatively, a mid-term solution could involve changing the way any remaining RTIEO is allocated to market participants. On a general level, this would mean allocation to any participant, physical or virtual, who has changed its position between day-ahead and real-time. Rather than provide a detailed discussion here, we point the CAISO and other participants to the stakeholder initiative from 2009 which attempted to deal with this issue[1]. It may be desirable to re-examine the options discussed in that stakeholder process.

---

[1] Straw Proposal. Mitigation and Allocation of Real-Time Imbalance Energy Offset Costs. http://www.caiso.com/2432/2432e7916dfa0.pdf

Finally, until a long-term solution is reached, convergence bidding position limits on the interties should not be raised above current levels. Specifically, the planned increase in October from 5% to 25% should be delayed if no action has been taken to resolve the underlying causes of the RTIEO uplift issue.

3. Comments on Emergency Filing

Support Proposed Threshold for Emergency Filing

Our current understanding is that the CAISO would make an emergency filing to implement this proposed fix if the RTIEO due to matched convergence bids exceeded $25 million on a rolling 30 day basis. If this understanding is correct, we support the CAISO's proposal to make such an emergency filing.

4. Technical Details of Proposed Settlement Rule

Request More Examples and Greater Clarity on Proposed Rule in Next Draft

Regarding the examples given in the paper, there seems to be some inconsistencies between what is presented in the equations defining the rule and what is shown in the tables. In the next paper we request the CAISO to further clarify exactly how this rule will work and better align the language used in the equations with what appears in the examples. Specific questions are listed below:

1. In table 2, does the “Internal Virtual Demand” represent the net internal virtual position or just the participant’s virtual demand position? This question also applies to the "Intertie Virtual Supply” quantity.
2. Will increasing HASP imports from day-ahead imports in table 2 result in a negative liability to offset the Intertie Virtual Supply? Worded differently, will participants essentially receive a "credit" for this type of behavior?
3. How will applying this rule to reduced or increased import quantities interact with rules already established (HASP Settlement Rule) to deter implicit virtual bidding? Would there be an opportunity for a double charge, double credit, or offsetting charges?
4. Could the CAISO provide some examples where this rule results in a credit? All that is provided in the paper are examles of when it results in a charge.