

**Sempra Energy Stakeholder Comments Regarding CRR Study 2
(May 6, 2004)**

Sempra Energy¹ and several other stakeholders have commissioned Drs. Hogan and Harvey to prepare a detailed analysis of several difficult issues confronting the CAISO in auctioning and allocating financial property rights in the CAISO-operated grid. The first draft of the Hogan/Harvey analysis was provided to the CAISO March 2 for public distribution; the final report will be submitted to the CAISO on May 24, 2004 in accordance with the established schedule. Sempra Energy urges the CAISO to give substantial weight to the Hogan/Harvey analysis, and to follow their recommendations in establishing a financial property right regime to complement the LMP-based spot market being developed in the MD02 proceeding.

In addition to endorsing the Hogan/Harvey CRR analysis, Sempra Energy offers the following stakeholder comments on the CAISO's proposals to establish three to five scenarios for its upcoming CRR Allocation Study 2. Representatives from the Sempra Companies have been participating in all facets of the CRR work, but our current collective understanding of the difficult technical issues under discussion remains incomplete. The comments offered below are meant to be helpful, but certainly not exhaustive or definitive.

- 1. Study Period** – Conducting scenario analysis for more than one year would seem to increase significantly the CAISO's workload without commensurate gain in information. Sempra Energy recommends expediting the CRR Study 2 by confining the scenario analysis to calendar year 2006.

¹ Sempra Energy is the parent company of San Diego Gas & Electric Company. Sempra Energy also owns several energy merchants – Sempra Energy Trading, Sempra Energy Resources, and Sempra Energy Solutions – that provide a full array of energy-related products and services. Sempra Energy offers these stakeholder comments on market design issues on behalf of all its constituent companies.

- 2. CRR Nominations for ETCs / Sequence of Optimization and Simultaneous Feasibility Test (SFT)/CRR Allocation Objective Function / Priorities and Proxy Bids with original objective function (max proxy value)** – Sempra Energy is unable to ascertain whether the CAISO intends to run a scenario that would prioritize all CRR allocation requests on a collective basis in accordance with Southern California Edison's "simple 4-priority approach". Sempra Energy recommends running at least one scenario wherein: (1) the Transmission Provider for Unconverted-ETCs (SCE or PG&E) submits CRR allocation requests representing the ETCs; (2) Converted-ETC LSEs (the southern cities) are permitted to request only obligations; (3) all CRR requests are subject to SCE's simple 4-priority approach; and (4) there is one optimization/SFT run for each CRR term with no priorities given to the different CRR types of ETC, Converted Rights, and LSE. Sempra Energy believes this scenario would provide useful information as to what would happen were all LSEs to be equally with respect to their ability to request and obtain CRRs.
- 3. Break down of Large Aggregation Points for Allocation Purposes** – The lower the level of aggregation the better for determining the maximum set of simultaneously feasible CRRs. *See* the Hogan/Harvey paper for a thorough analysis of how large aggregation areas can complicate and even defeat altogether the creation of useful financial instruments to hedge the differences in nodal prices. The CAISO should address directly the problems associated with using large load aggregation zones and only continue with this approach if it can make a compelling demonstration that it has workable solutions to the problems identified by Drs. Hogan and Harvey.
- 4. LMP Calculations / Developing Transaction Data** – Developing "transaction data", determining the resulting LMPs, and then applying the LMPs to the CRRs allocated in each of the scenarios will, no doubt, be an interesting exercise, but it should be a low priority in CRR Study 2. The

CAISO's role is not to evaluate whether or not a particular set of CRRs adequately hedges any particular LSE's exposure to congestion cost uncertainty. Such evaluations are the commercial responsibility of every LSE and their respective regulatory authorities. Similarly, it is not helpful to leave the impression that market participants can (or should) rely on the results of the CAISO's "studies" to establish the market participant's relative commercial position with respect to CRR allocations. Accordingly, Sempra Energy recommends that the CAISO not engage in any CRR scaling or reallocation activities and that these features of CRR Study 2 be eliminated.

- 5. Replace Trading Hub Sources with generator/import Sources / Modeling the results on an auction (e.g., generation/import to Trading Hub) –** Sempra Energy recommends against the CAISO including a scenario that makes *assumptions* about CRRs that are not in fact requested by any LSE, unless the purpose is to understand how the "long term" CRR auction (which will immediately follow the allocation of "long-term" CRRs) could affect the subsequent allocation of "short-term" CRRs. Even if the purpose of such assumptions is an attempt to create a "proxy" for the long-term CRR auction, the results would be highly speculative, so Sempra Energy would urge the CAISO to give a low priority to this effort.