Stakeholder Comments Template

Subject: Convergence Bidding

As a follow-up to the discussion at the August 10 meeting of the Market Surveillance Committee (MSC), the CAISO is requesting additional written comments on convergence bidding, especially the level of granularity at which virtual bidding should be introduced within the CAISO markets.

A number of parties have already submitted comments on this granularity issue, and those comments will remain posted and part of the record for stakeholder process. This template is offered as a guide for any additional comments that participants may have based on the MSC discussion. Documents related to this meeting are posted at: [http://www.caiso.com/1807/1807996f7020.html](http://www.caiso.com/1807/1807996f7020.html).

Comments should be submitted in any format by close of business on Friday, August 24, 2007 to: convergencebidding@caiso.com.

The CAISO offers the following questions as a guide for formulating stakeholder comments:

1. Would convergence bidding enhance your organization’s business needs. If so, how? What does your entity view as the primary benefits of convergence bidding to the CAISO’s energy markets?

   Williams believes that convergence bidding enhances suppliers’ business needs by (1) providing a means to counteract buyer market power and promote a liquid and competitive day-ahead energy market; (2) providing suppliers with a way to access real-time energy prices that still meets the CAISO’s day-ahead reliability needs; and by (3) providing a means to hedge real-time outage risk.
2. What are your entity’s views on the level of granularity at which the CAISO should introduce convergence bidding (LAP-level virtual bidding or nodal-level virtual bidding)?

Williams strongly supports nodal-level convergence bidding for these reasons:

- LAP-level convergence bidding cannot serve as a fully effective hedging tool for generators, which are settled at nodal prices. The CAISO has provided load with point-to-point CRRs to hedge price risk; supply equitably should be provided a comparable tool to hedge its price risk.

- NYISO’s LAP-level convergence bidding has been shown to produce inferior price convergence in load pockets\(^1\), and this even with eleven zones (as compared to the three zones proposed for LAP-level convergence bidding for the CAISO).

- Implementing convergence bidding on a LAP-level wastes CAISO staff effort on a “throwaway” product and creates unnecessary uncertainty about when nodal-level convergence bidding will be implemented.

- There is nothing unique about the CAISO’s MRTU design that renders the significant experience gained by all ISOs in nodal-level convergence bidding inapplicable. Thus there is no need for the CAISO to engage in an unbounded trial period for LAP-level convergence bidding prior to implementing a proven and well-functioning product, i.e., nodal-level convergence bidding.

3. What are your entity’s views on position limits (limiting virtual bidding to a percentage of the MW volume at each node)?

Williams believes the CAISO’s initial suggestion – position limits of 10% of the physical supply or demand at each node – is far too conservative, as it would only allow hedging an outage of 10% of a unit’s capability. Imposing severe position limits in response to concerns about bidding competitiveness seems certain to become a self-fulfilling prophecy that will deter participation in the virtual market.

4. What are your entity’s views on allocating costs to virtual bids?

Williams appreciates that the CAISO and its Market Surveillance Committee understand the benefits of a deep and liquid virtual market and do not wish to discourage participation by saddling virtual bids with punitive uplift charges. Williams supports assessing charges to virtual bids based on cost causation, not some asserted costs.

“symmetry” between physical and virtual supply and demand. For example, it is rational to allocate RUC charges to virtual supply that displaces physical supply in the day-ahead market, but not rational to allocate RUC charges to virtual demand if that demand merely raises day-ahead unit commitment to levels that would occur if demand had been fully bid into the day-ahead market.

5. What are your entity’s views about the optimal number of LAPs in California?

Nodal prices are intended to serve as an indicator of the value of supply and the cost of demand at individual locations on the grid. Paying nodal prices to supply in constrained areas but not allocating those costs to demand in those same areas shifts costs and may not best target investment which would address the constraints in these areas. The more granular the load settlement, the better, but the primary hurdles to be overcome to implement nodal settlement of load stem from politics, not market design or system limitations.