COMMENTS OF THE
ALLIANCE FOR RETAIL ENERGY MARKETS
ON THE CAISO's APRIL 15, 2011
2011 CRR ENHANCEMENTS STRAW PROPOSAL
Submitted to: 2011CRREnhancements@caiso.com

On April 15, 2011, the California Independent System Operator (CAISO) released the "2011 CRR Enhancements Straw Proposal," which significantly modifies its March 4, 2011 issue paper on this topic. The Alliance for Retail Energy Markets (AReM)[1] supports the CAISO's decision to defer discussion of changes to the current load migration process for allocating congestion revenue rights (CRRs) to a working group and plans to participate in that effort. However, after further review, AReM has significant concerns about the CAISO's proposals for improving revenue adequacy. AReM presents its concerns on each element of the proposal below.

A. Proposals To Address Issues With Revenue Adequacy

The CAISO proposes using historical hourly Operating Transfer Capability (OTC) data to select the break-even point on an OTC duration curve for each transmission element as a way to improve revenue adequacy for CRRs.[2] AReM believes that basing CRR release on historical data is not the preferred approach. The quantities of CRRs calculated by looking at previous forced outages have no relationship to future conditions and only ensure inaccuracies – either in revenues or CRRs available for hedging. Rather, AReM prefers that the CAISO explore using a forward-looking CRR model on the interties to the extent possible that addresses the probability of outages and derates. Further, rather than seek to reduce revenue shortfall to zero, the CAISO

[1] AReM is a California non-profit mutual benefit corporation formed by electric service providers that are active in the California's direct access market. This filing represents the position of AReM, but not necessarily that of a particular member or any affiliates of its members with respect to the issues addressed herein.
[2] Straw Proposal, pp. 6-7.

should consider using some of the auction revenues to fund CRRs rather than leaving LSEs unable to hedge their congestion risk because last year there was a forced outage on a particular intertie.

Nonetheless, AReM agrees that the CAISO's OTC proposal is an improvement over the current process, but only if, the CAISO eliminates or *significantly lowers* the use of the Global Derate Factor (GDF) in the *monthly* CRR process.[3] If the CAISO has no such plan, or even worse, plans to introduce the use of the GDF in the *annual CRR process,* then AReM cannot support this proposal.

In fact, the Straw Proposal includes just such a proposal for the use of a GDF in the annual CRR allocation process.[4] In a short paragraph, the CAISO presents additional modifications to "ensure there is sufficient capacity remaining for stakeholders to true up their CRR holdings in the monthly process."[5] Specifically, the CAISO proposes either: (a) reducing capacity released in the annual process to 65% (from 75%); or (b) introducing a Global Derate Factor in the annual process.

As noted in our March 21 comments, AReM supports changes that would *reduce* the use of the GDF or otherwise improve the accuracy of the quantity of CRRs made available in the monthly process. AReM notes that the use of a GDF in determining the quantity of monthly CRRs released has severely limited the ability of load-serving entities (LSEs) to obtain the necessary CRRs to adequately hedge congestion costs. Electric service providers (ESPs) obtain the vast majority of their CRRs in the annual allocation process and cannot support any proposal that would introduce the use of the GDF into this process. The GDF is a broad-based de-rate

[3] The March 4 issue paper (p. 8) stated that one of the benefits of this OTC approach was to lower the GDF in the monthly allocation process, but the Straw Proposal was silent on that point.
[4] The GDF has only been used in the monthly CRR process thus far.
[5] Straw Proposal, p. 7.

across the network rather than a local de-rate factor being applied to those paths that cause revenue inadequacy, thereby reducing all CRRs.

In fact, AReM does not support either proposed modification at this time, but recommends that the CAISO adopt the capacity reduction proposal as an *option* to be implemented only if required. Specifically, AReM recommends that the CAISO first implement the OTC method and evaluate its results. If significant issues with revenue adequacy remain, and after adequate notice to market participants, the CAISO could implement the proposal to reduce the capacity released in the annual process to 65%.

Further, because these steps to improve revenue adequacy reduce CRRs available in the annual process, AReM proposes to introduce a Priority Nomination Process (PNP) in the CRR monthly allocation process, as discussed below, to improve a LSE's chances of obtaining the CRRs they need to hedge their congestion costs. In particular, the CAISO must ensure to the extent possible that all available CRRs are released through either allocation or auction, both to meet hedging needs and to ensure that longer-term commitments undertaken to meet the renewable portfolio standard (RPS) obligations are not impaired. The CAISO's own planning efforts (*e.g.,* RETPP) have been directed toward meeting the 33% RPS; permitting an enhanced PNP in the monthly CRR process is a way to harmonize those efforts with the CAISO's CRR program.

Accordingly, it may not be at all appropriate for the CAISO to adopt the supposedly "standard" rules of the other ISOs for congestion hedging, as suggested on the April 22nd call, given California's unique and challenging LSE requirements.

B. Relaxing Full Funding Requirement for CRRs

AReM opposes any relaxation of the full funding requirement for CRRs.[6] The impact of changing this requirement would fall disproportionately on ESPs, which may be unable to recover the increased costs from their customers. The utilities, on the other hand, would not be significantly harmed due to their typically full cost recovery of CAISO charges. Consequently, reducing the full funding requirement would provide a competitive advantage to the utilities and harm retail competition. Unlike a utility's bundled customers, direct access customers have the opportunity to hedge basis risk between a liquid trading point (SP15, PV, NOB, COB) and the LAP with their ESPs. If the ESP were to offer that product to the customer and then the path became underfunded, the ESP may not have a way to recoup those costs. This is a significant issue in PJM, where the underfunding of FTR's is harming retail competition.[7].

C. Merging Tiers 1 and 2 in Monthly Allocation Process

The CAISO proposes "merging" the two tiers in the current monthly process into one to provide additional time to refine the model used each month.[8] As noted above, AReM has an alternative proposal. AReM requests that the CAISO introduce a PNP tier in the monthly allocation process. This approach would mitigate, to some extent, the expected reduction in annual CRRs released when the CAISO implements its OTC method (or if it subsequently implements the capacity reduction proposal) to improve revenue adequacy. In that event, there would be a PNP Tier and a Tier 1 – in effect, still two Tiers. AReM understands that this proposal does not address the CAISO's goal for more time to "refine" the model. Nonetheless, AReM believes that the need for additional and valuable CRRs that could be obtained by LSEs

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[6] Straw Proposal, p. 7.
[7] All AReM members currently serve retail load in PJM.
[8] Straw Proposal, p. 7.

though a monthly PNP outweighs the benefits that would be expected from a few more days to "refine" the model.

D. Proposed Tariff Clarifications

The issue paper proposes several new tariff clarifications, in addition to those proposed in its March 4 issue paper.[9] AReM supports the following additional clarifications:

- Clarifying credit requirements related to load migration and bilateral trades.
- Clarifying that auction participants submit a portfolio of bids.
- Implementing a "sell" feature.

AReM does not support the CAISO's proposal to modify the retirement process for disconnected Pnodes so that the closest "biddable" Pnode is used.[10] AReM believes that using the closest biddable location for replacing retired nodes, instead of the closest electrically, will exacerbate revenue inadequacy. As an alternative, AReM proposes that the CAISO make the electrically closest location biddable for the duration of outstanding CRRs.

E. Additional Auction Functionality

AReM has no further comments on the proposal at this time.[11]

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[9] Issue paper, pp. 8-11.
[10] Straw Proposal, p. 11.
[11] Straw Proposal, p. 10-11.