CDWR's Comments to CAISO's on 2011 CRR Enhancements Issue Paper

The California Department of Water Resources (CDWR) appreciates the California Independent System Operator's (CAISO) initiative to look for opportunities to improve the current CRR process for both market participants and CAISO. CDWR also appreciates CAISO's decision to allow market participants to post questions and comments regarding the CAISO's 2011 Congestion Revenue Rights (CRR) Enhancements Issue Paper.

First, CDWR would like to emphasize that a timely release (as originally scheduled by the CAISO) of the 2010 CRR Market Performance Report on CRRs would have provided market participants with extremely useful information when preparing their comments. With only the 2009 report available, market participants do not have a complete picture of the CRR process performance for the past two years, which could limit the relevance of market participants' comments. For example, it is possible 2009 CRR performance was influenced by transition to a new market design and, consequently, by market participants' and CAISO's anxiety to commit to a new market design. It's very likely this anxiety would have disappeared in 2010 when market participants and CAISO gained more confidence in the MRTU.

Additional comments by section of the Issue Paper

4.2 Revenue Adequacy Issues

CDWR supports CAISO's initiative to improve CRR Revenue Adequacy. CDWR suggests that, prior to making any recommendations for improving the modeling of the transmission capacity available for CRRs, CAISO perform studies and reports to determine and validate how adopting an Operating Transmission Capacity (OTC) or a median OTC would improve the CRR Revenue Adequacy. CDWR is concerned that, if CAISO's modeling of proposed Available Transmission Capacity (ATC) for CRRs as compared with the current ATC modeled in past years' annual CRR allocation processes resulted in a major reduction, then the existing Long Term Congestion Revenue Rights (LT-CRRs) allocated previously could lock out most of the ATC available for future Tier 2 and Tier 3 CRR annual allocations. In this case, entities such CDWR, that for various reasons[1], would be forced to obtain most of their entire annual CRR needs in Tier 2 and Tier 3 of the annual allocation process. It is possible CDWR and other entities could end up with no CRRs following completion of the annual allocation process and would need to rely only on the annual auction process or monthly CRR allocation and auction processes to obtain any CRR.

Further, CDWR has had numerous discussions with CAISO regarding the impact of auctioned CRRs on the CRR Revenue Adequacy and understood that CAISO's only explanation for not achieving the CRR Revenue Adequacy was due to inaccurate modeling of

[1] For CDWR, some of the reasons that determined a limited participation in the PNP were as follows: undeserved reduction in the On-Peak PNP UB due to ambiguous MRTU-CRR Tariff language, loss of the ability to renew valuable CRR in the 2010 and following years PNP due to CRR FNM modeling error in the Antelope to Vincent transmission line.

outages. CDWR still believe the auctioned CRRs are the main reason CRR Revenue Adequacy was not achieved. For example, the 2009 CRR Performance Report states the average On-Peak CRR auctioned rate was $0.17/MW but the average CRR revenue rate was $0.28/MW. Similarly, the average Off-Peak CRRs auctioned rate was $0.08/MW but the average CRR revenues rate was $0.16/MW. A rough estimate shows the total 2009 On-Peak and Off-Peak annual and monthly processes CRRs were auctioned at $13 million but produced $24 million in revenues. We think that this example alone is enough to explain the decrease in the Revenue Adequacy. We believe the easiest way to fix the CRR Revenue Adequacy problem is to separate the CRR auction monies (proceeds and revenues) from the CRR Balancing Account (BA). As such, a separate balancing account, the Auctioned CRR BA, would be created for the auctioned CRR monies. The auction proceeds would be entered into and the CRR Revenues would be paid out of Auctioned CRR BA. CDWR believes if the Auctioned CRR BA is implemented as described above, auctioned CRR values would closely match CRR revenues as predicted in the CRR Tariff (but not yet validated as presented in the 2009 CRR Performance Report – CRR Auction Results). CDWR also believes that CRR Revenue Adequacy will be met most of the time for the allocated CRRs. To verify the strength or the weakness of this proposal, CDWR recommends CAISO perform a study to evaluate how CRR Revenue Adequacy would have performed for past years if the auctioned CRR proceeds and revenues were isolated from the CRR BA.

4.3 Simplification of the Allocation Process

4.3.3 Merge Annual Tier2 / Tier 3 Allocation and Auction

CDWR is well aware of the burden of having 5 tiers for the annual CRR process and 3 tiers for the monthly CRR process. Internally we find it very difficult to perform timely analysis for participating in multiple CRR processes. However, while we believe CAISO's proposal to merge Annual Tier 2 and Tier 3 Allocation and Annual Auction Tier under one annual auction tier would increase the analysis time available for the remaining tiers, it could tremendously increase the CRR Revenue Inadequacy for the same reasons explained previously in Section 4.2. For example, CAISO's 2009 CRR Performance Report showed a fourfold increase between the auctioned CRRs in 2010 from 2009. This increase was probably due to the fact that 2009 auctioned CRR revenues were almost doubled the price paid to obtain them. This increase also happened when almost no ATC was available for the annual auction assuming that all annual ATC was consumed in the annual allocation process. CDWR believes that the amount of auctioned CRR could increase even more if the currently available ATC for Tier 2 and Tier 3 of the annual allocation process would be opened for auction only; as a result the CRR Revenue Adequacy will decrease sharply.

For various reasons, described in the footnote 1 (page 1 above), entities such CDWR were forced to obtain most of their entire annual CRR needs in Tier 2 and Tier 3 of the annual allocation process. However, CDWR had participated in the previous years' Tier 2 and Tier 3 allocations and had obtained little or no CRR while facing competition only from LSEs. Under CAISO's proposal of merging the Tier 2 and Tier 2 allocation tiers with the auction tier, CDWR would face competition not only from the LSEs but also from all the other market participants

that are allowed to participate in the auction processes; therefore, it would be even more difficult for CDWR to obtain the required CRRs to hedge its congestion rents.

CDWR believes the current burden of having 5 tiers for the annual CRR process could be easily reduced by combining Tier 1 (PNP), Tier 2, and Tier 3 of the annual CRR allocation process under one general annual allocation tier. In this case the priority nomination process can be addressed by assuming priority of nomination within the general annual allocation tier. The LT-CRRs could be allocated at the completion of the general annual allocation tier only from CRRs allocated within the general tier as priority one. Annual CRR auction process would be unchanged from its current design.

4.3.4 Merge monthly Tier 1/ Tier 2 Allocation and Auction

For similar reasons as explained above in Section 4.3.3, CDWR does not believe the merger of the monthly allocation tier with the monthly auction tier to be beneficial.

CDWR accepts merging of Tier 1 and Tier 2 of the monthly allocation under one monthly CRR allocation tier if the market participants agree that it is beneficial and if the current design of maintaining the CRR Revenue Adequacy with a high Global Derate Factor (GDF) is maintained.

4.3.5 Separate the Balancing Account from the Auction Proceeds

CDWR considers this approach to be beneficial only if the CRR auction revenues are also separated from the CRR Balancing Account (see comments in Section 4.2 – last paragraph).

If you have any questions please contact Daniel Cretu at (916) 574-0658.