

# Stakeholder Comments Template

## Subject: 2011 CRR Enhancements

Submitted by (name and phone number):	Company or Entity:	Date Submitted:
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DC Energy appreciates the opportunity to provide its insights and recommendations on how we believe the CRR market can and should be improved. While this specific project is intended to examine improvements that can occur in the relatively short-term (i.e., 2011), we recognize some of our comments/suggestions cannot be completed in such time frame. Our intent is to provide CAISO and its stakeholders our holistic view on CRR market enhancements.

Following the agenda from the March 11<sup>th</sup> meeting that discussed the 2011 CRR Enhancements White Paper, we offer the below comments:

### Improve Revenue Adequacy

DC Energy believes there are enhancements that CAISO can and should implement that will have significant improvements in revenue adequacy.

- a- System Capacity Release – The amount of system capability included in the annual product vs. the monthly product will have a profound affect on revenue adequacy. The amount of uncertainty of actual outage conditions is much greater the longer the time step of the product. That is, with the annual product much less is known regarding outage conditions for the coming year. The inverse is true for the monthly product (i.e., much more certainty of outage conditions). It is for this reason that DC Energy recommends that CAISO shift more of the system capability into the monthly auctions. Currently 75% of the system capability is available in the annual product and the remaining 25% in the monthly auctions. DC Energy recommends the annual system capacity be reduced to 50%, with the remaining 50% released in the monthly product. This will lead to a higher degree of revenue adequacy. To be clear, DC Energy is not suggesting less total system capacity be released, simply shifted with negligible affect on auction revenue. DC Energy recognizes this will require a tariff modification, however this current process may result in numerous Tariff modifications and this proposal (shift of system capacity available in the annual and monthly auctions) will be a significant increase in product certainty which will remove some risk from the product and therefore tend to maximize auction revenue which flows back to customers.

- b- Accurate Outage Reporting – Another area that would result in improved revenue adequacy is in the area of outage scheduling and reporting. Currently there is no link between planned outages being scheduled and posted in advance of the annual CRR auction.<sup>1</sup> DC Energy suggests CAISO creates standards that encourage most major transmission outages be planned and posted prior to the development of the model used for the annual CRR auction. This will directly result in greater revenue adequacy. In addition CAISO can create the incentive for Transmission Owners (TOs) by making them accountable for their actions. That is, if revenue inadequacy is created by transmission outages not following such rules, DC Energy suggests they should be held financially responsible for the inadequacy. Also this would not penalize transmission owners who follow the rule in that only the transmission owner in violation would pay, not all TOs. This has worked quite well in NYISO that has had this process in place since the inception of their TCC market (CRR equivalent).
- c- Modeling – As delineated in the White Paper improving modeling to better account for the impact of expected transmission outages and de-rates is one such area. It is DC Energy's understanding that CAISO is considering modeling historical outages during the annual process, rather than selling nameplate capacity, as another step to improve revenue adequacy. We oppose this suggestion and believe this to be a suboptimal solution as the impact will be to sell less capacity in total and thus lower auction revenue allocated to customers. If this approach is pursued, CAISO should distinguish between planned and unplanned outages. As such, historical outages that were known ahead of an auction process should not contribute to future de-rates. While this suggested modification will likely not have much of an impact for annual auctions as most historical outages were not known ahead of the auction, but should result in a more efficient capacity allocation in the monthly auctions where the ISO has a much better view of the planned outages.

DC Energy believes that the above suggestions target the areas that have historically contributed to revenue inadequacy and will also minimize cross-subsidization.

#### Allocation Process Improvements

CAISO has suggested allocation process simplifications in its recent White Paper. DC Energy does not oppose these suggestions. DC Energy would also suggest that beyond allocation process simplification, allocation process improvements are warranted. Specifically the current practice of allocating a valuable commodity, at no cost, is not a market driven process. DC Energy believes ultimately, as suggested on the March 11<sup>th</sup> call, a long-term plan should be to evolve to eliminate the ARR allocation process and instead auction off all CRRs. This will result in maximizing the value to CAISO customers. While this may not be palatable to all CAISO market participants at this time, CAISO can make a change on the allocation process that would be a significant step forward in removing a subsidization that exists today. Currently ARR are allocated based on peak load. DC Energy suggests that using an allocation based on peak load over-allocates ARRs and provides the recipient an over-hedged position to the detriment to the market. Instead of allocating ARRs based on peak load, DC Energy suggests the allocation, if

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<sup>1</sup> DC Energy recognizes CAISO implemented a 30-day rule for the monthly auctions.

continued on an annual period, be based on average load. This will balance the ability for load to hedge congestion risk and a more appropriate market structure that maximizes release of capacity into CRR auctions. If load desires to hedge more of its risk it can enter either the annual or monthly markets to purchase, at market based prices, such hedge. In the alternative of basing the allocation annually on average load, ARRs can be allocated load shaped (i.e., based on monthly peak load).

#### Additional Auction Functionality

DC Energy supports and has been advocating in all ISO/RTO FTR markets, long-term and balancing auctions as added functionality. We believe further that in CAISO's CRR markets Balancing Auctions should be prioritized ahead of long-term auctions as delineated below.

*Balancing Auctions* – The proposal is following the annual auction, in each subsequent monthly CRR auction, market participants (MPs) can bid/offer on any path in any individual month or combination of months (i.e., strips) for the remainder of the annual period. The benefits of Balancing Auctions are they allow MPs to shape and alter their portfolios to a much greater extent and such functionality is specifically useful for responding to changing network or contract situations. In addition the pricing that result from Balancing Auctions provide a much clearer view of updated market value, which can be used to determine mark-to-market collateral requirements in a more robust manner. Some more granular benefits of Balancing Auctions include:

- More flexible time periods would allow load and generators to hedge more effectively (e.g., as load switches participants cannot currently hedge the associated risks)
- Participants will increase participation with reconfiguration capabilities which will likely increase revenue from the auctions
- Participation in OTC markets exhibits interest in bal-year product
- CAISO markets as a whole benefit from additional pricing information
- Existing participants need not participate with limited impact on system capacity
- Some participants may want to only purchase a portion of the year but today cannot
- Enables a straightforward calculation of variance margin (i.e., these additional auctions create a superior forward curve (mark-to-market) to evaluate credit exposure and with each month the credit exposure is continually refined for the balance of the year)
- Create more certainty in the area of liquidating defaulted positions (i.e., more clarity on forward pricing that provides clarity on liquidation pricing).

Balancing auctions have been implemented in PJM in 2006 and participation levels and trading activity in the PJM Balance of Planning Period (“BOPP”) Auction indicates interest in the product. ISO-NE, MISO and NYISO are all in various stages of development, with at least ISO-NE and NYISO planning to implement such in the next year or so.

The structure of the Balancing Auction should co-optimize flexibility and liquidity. DC Energy also recognizes that the impact of the Balancing Auction on sales of existing positions and/or counter-flow will require additional collateral requirement assessment and discussion.

*Long-term Auctions* – DC Energy supports the development of CRR auctions with a duration of more than one-year. DC Energy would like to assert that it believes long-term auctions are but one more evolutionary piece to the mosaic that FERC has crafted with ISO/RTOs utilizing Locational Marginal Pricing (“LMP”). Long-term auctions will benefit customers by providing the ability to hedge transactions of duration greater than one year, which will lead to more efficient and stable electricity markets. We believe the shortage of bilateral energy transactions with a duration greater than one year between market participants exists in these markets because there is no reasonable market driven mechanism to hedge congestion risk. We caution against market structures in which the introduction of long-term auctions would act to remove liquidity in short-term auctions. Specifically, DC Energy suggests only a limited portion of the total system capability should be auctioned off for periods of duration greater than one year. As such, we recommend that initially long-term auctions be limited to a duration of three years and that only a small fraction of total system capacity be included in such auctions. Once the markets in which they are offered begin to gain some liquidity and customers of these markets build comfort around this level of activity, additional years may be added/offered. DC Energy suggests that the risks inherent in the market are more easily determined in the shorter-term, hence our suggestion that 90% of the system capability be reserved for auctions of a duration of one year or less. This provides significant liquidity for market participants to adjust their exposure in light of the most recent market developments. Another reason for the reservation of a significant amount of capacity for the duration of one year or less is the uncertainty of changes to the network topology, including generation dispatch. In the period of one month to one year, the topology is reasonably stable and the risks associated with dramatic changes are low and manageable. Finally DC Energy recognizes that additional credit requirements will be necessary.

*Long-term and Balancing Auction Development Priority* – If CAISO determines that both these enhancements cannot be developed simultaneously, DC Energy suggests that Balancing Auctions be developed first. Balancing Auctions is the next evolutionary step for the CRR markets. Once these auctions develop and provide the benefits delineated above, CAISO can then move to the long-term auctions as the Balancing Auction pricing will provide CAISO the necessary pricing to build suitable collateral policy for the long-term auctions.

#### Load Migration Simplification

DC Energy does not oppose the CAISO suggestion to reduce the number of CRRs tracked as delineated in the CAISO White Paper, including by increasing the minimum size of the product from the current 0.001 MW.

#### Tariff Clarification Issues

DC Energy supports CAISO suggestion to remove mandatory CRR training requirement.