# Stakeholder Comments Template

## Subject: SCE Comments on 2011 CRR enhancements Issue Paper, March 4, 2011



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**Introduction**

SCE appreciates the opportunity to address the issues raised in the 2011 CRR Enhancements Issue Paper (CRR Issue Paper). The CAISO clearly states the purpose of the Issue Paper as "to look for opportunities to streamline the current process for both market participants and the ISO". However, the CRR Issue Paper has identified "issues" that go well beyond streamlining the current CRR process. Specifically, the CRR Issue Paper has identified two substantive items for discussion - the movement of CRRs out of the allocation process into the auction and CRR revenue adequacy. While SCE is supportive of considering ways to improve the efficiency of the current CRR process, SCE has significant concerns with potential revisions to the allocation and auction process as well as changes to address CRR revenue adequacy issues.

The CRR Issue Paper has set a schedule for these substantive issues based on submission to the board in June 2011 and implemented for 2012 CRRs. SCE does not believe that the schedule can be kept nor that all of the issues raised are required or desirable in meeting the "streamlining" of the CRR process.

SCE suggests in its comments the issues that can and should be addressed in the CRR process and those it believes would reopen contentious debate in the working group. If these considerations are used to limit the scope of this initiative, leaving aside contentious issues, the Issue Paper's schedule and its streamlining goal may be met.

**Allocation and Auction Issues**

The CRR Issues Paper contains three distinct suggestions for change in the allocation process. The CAISO suggests that in the annual process "it may be more efficient to combine the current Tier LT with a long-term CRR auction"[1]. It goes on to propose that "Tiers 2-3 and the annual auction process can be combined into a single auction step." In the monthly process the CAISO proposes to "consolidate all tiers into a single auction process."[2] The result of this change is that LSEs will lose access to CRRs that are

[1] 2011 CRR enhancements Issue Paper, CAISO March 4, 2011 p. 10
http://www.caiso.com/2b37/2b379e9a574f0.pdf

[2] Ibid at 1 p. 11

currently available to them in the Tier 2/3 allocation and be required to compete for those CRRs in the auction.

SCE is not supportive of any effort to reduce the quantity of CRRs made available to LSEs through the annual or monthly allocation process. Loads receive a hedge against actual congestion costs they incur by holding CRRs for relevant paths used to serve load. Auction revenues do not provide a dollar for dollar hedge against actual congestion charges; such revenues are only a proxy for the CRR itself. This concept is a fundamental interpretation of the function of CRRs as put forward by FERC when it found CRR allocation to load reasonable[3]. FERC goes on to describe an appropriate LSE goal of obtaining “Congestion Revenue Rights that will serve as a hedge against the congestion cost that are actually incurred while serving their load.”[4]

To reiterate, auction revenue does not recover the full value of the CRR. For example, when counter parties judge the risk they are undertaking and their profit requirement when bidding for a CRR, they are by necessity led to discount their offer prices. That discount is part of the loss suffered by ratepayers when accepting auction revenue in lieu of CRRs. Not only is there missing money in pricing, but load then is subject to the volatility of congestion charges more appropriately hedged with the CRR.

Although total credit requirement may not be impacted, there will be additional collateral requirement due to the ESPs auction participation. This cost of collateral for auction participation is even more certain since FERC has ordered that unsecured credit cannot be used in the CRR auction process.

Beyond these arguments the CAISO has asked that market participants provide specific examples of lower benefits to load.[5] It is clear that any example that compares the current process to that proposed must be supported by detailed evaluation of both the existing process and the proposal. SCE does not have the access to data nor the detailed proposal required to perform such an analysis. On the contrary, SCE believes that the CAISO itself is in the best position to accomplish such an analysis and in fact it is their responsibility to illustrate that their proposal will not lower benefits to load. If alternatives to the current allocation methodology are to be analyzed, SCE would propose another scenario where 100% of CRRs are allocated to load. That alternative would conform to the current allocation process, then allocate all remaining CRRs in a manner to be developed. Auctions would then be limited to transactions between willing counterparties and would assure appropriate pricing.

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[3] See October 2003 Order, 105 FERC ¶ 61,140 at P 171. As a general matter the CAISO’s proposal to allocate CRR obligations to all loads not covered by ETC rights within the CAISO control area seems reasonable.

[4] See November 2008 Order, 125 FERC ¶ 61,153 at P 26. Further, the goal of every Load Serving Entity in the allocation process should be to obtain Congestion Revenue Rights that will serve as a hedge against the congestion costs that are actually incurred while serving their load.

[5] Ibid 1 at p. 9

Finally, consideration of changes to the distribution of auction revenues will be complicated and contentious requiring an involved process very similar to that experienced for allocations. Furthermore FERC has previously ruled[6] that the allocation process is reasonable making SCE question why opening such a process is preferable to retaining the current allocation methodology.

**CRR Revenue Adequacy**

SCE is willing to address the CAISO's Revenue insufficiency concerns. However, the CRR process is currently financing that shortfall with auction revenue and only modest near term changes to the CRR process appear to be needed.

Although Operating Transfer Capability (OTC) Breakeven methodology appears on the surface to be useful, that proposal lacks the depth and detail needed to assure its successful application. For example, the methodology does not include treatment for outliers or grid configuration changes. Outliers are likely to be unanticipated and rare events and if included in the analysis have the potential for skewing the OTC Breakeven results. It is therefore necessary to predefine the way in which these outliers can be identified and discarded. In addition, changes to grid configurations and grid topology are not accommodated with the formulaic historical analysis proposed. There must be an alternative developed that will include changes in configuration as they are approved for the grid.

SCE suggests that a substantial analysis is needed, prior to adoption, which details the differences in LT, Annual and Monthly allocations expected under the OTC Breakeven methodology. It is clear that the CAISO has developed its approach in some detail and therefore could simulate its behavior for past periods. SCE is eager to see further detail of the methodology and analysis supporting its utility.

**Streamlining the CRR Allocation and Auction Process**

**Load Migration (Granularity)**

The CAISO suggests that CRRs below .1MW might be aggregated when tracking load migration between LSEs and suggests that the processing requirements would be substantially reduced. SCE is concerned with this approach, because it would aggregate more than half of the Annual CRRs and would require subdividing impacted customer classes by CRR size with the potential for missing small CRR changes. The proposal lacks detail on how accounting for the many small CRRs, not directly considered, would be accomplished. With this method the CAISO estimates[7] that 56%

[6] See September 2006 Order, 116 FERC ¶ 61,274 at P 743. the CAISO's proposed approach to the CRR allocation and auction methodology to be reasonable

[7] Ibid 1 at p. 7

of the LT CRR MW and 62% of the Annual CRR MWs would not be tracked and only aggregated.

Specifically, the proposed granularity change would totally aggregate the Commercial I customer class and partially aggregate Residential, Commercial II, Lighting and Agricultural customers. The remaining large customer classes would remain fully represented. Based on the customer class definitions it appears that the reduction of records could have unintended consequences as CRR tracking would have to accommodate the aggregation process or be skewed by the incomplete consideration of lower usage customer classes.

SCE's experience is that DA expands to the quota limits in segments larger than the .1 MW CRR level and returns to the IOU slowly in smaller segments. In the CAISO's proposed paradigm it is not clear when the IOU would recover the CRRs of returning customers. SCE believes there may be a serious lag in those returning CRRs.

The questions raised by the elimination of records appear to be many and the efficiency benefits may be difficult to quantify or even identify. The extensive number previously migrated 10 year CRRs would appear to be the more important issue and if dealt with regularly, would provide relief from growth in the number of CRRs by providing a soft cap to that CRR count; this without the change in granularity.

SCE believes these questions warrant further CAISO study of the granularity issue which should include the impact and timing of returning loads, labor intensity of the aggregation process and an estimate of the actual savings that may be projected.

**Maintain Annual PNP and Tier LT as Designed**

SCE favors the retention of these features but does not favor a change to incorporate the suggested LT Auction.

**Merge Annual Tier 2 /Tier 3 Allocation and Auction**

SCE can support merging Tier 2 and Tier 3 allocation tiers. However, SCE cannot support the replacement of the allocation process with an auction. That does not preclude a decreased allocation in the annual allocation with a corresponding increase in the monthly allocation in order to develop a more robust monthly program. Such a change would require rethinking the monthly process with discussions of a monthly PNP and a transition plan to accommodate entities that currently acquire CRRs in the annual allocation that would be forced to rely on the monthly process.

Aside from the question of allocation versus auction, SCE is skeptical of the proposal's notion that the CRRs obtained in the proposed auction could be nominated the following year in the PNP. It appears to be an unwarranted complication to price formation giving ESPs a different stake in the auction than other participants. If total allocations remain at current levels, as supported by SCE, this change is superfluous.

**Merge Monthly Tier 1/Tier 2 Allocation and Auction**

SCE can support the merging of Tier 1 and Tier 2 but, as argued in the previous section, SCE cannot support the elimination of allocations in favor of an auction.

**Separate the Balancing Account from the Auction Proceeds.**

The Issue Paper proposes separating auction proceeds from other balancing entries. In SCE's estimation this would exacerbate revenue insufficiency by paying out all auction revenue without consideration of the account balance, thus sacrificing the current buffer to revenue shortfalls. This provision appears to be designed to reallocate auction revenue in a manner that would compensate for moving LSE allocated CRRs to the auction. Furthermore, the proposed DLAP congestion methodology would fall short of providing a reasonable hedge to potential congestion costs and would smear congestion auction revenue across LSEs with little regard for their actual exposure.

SCE opposes the separation of auction revenue from the balancing account and the proposed auction revenue allocation methodology based on DLAP congestion. SCE opposes CRR methodology changes that ignore current allocation precedents and open the potential for an involved negotiation over auction revenue allocations. This is particularly true since the CAISO has a working CRR allocation process in place.

## Conclusion

SCE will work with the CAISO in its efforts to provide CRR revenue sufficiency and process simplification. In particular, SCE is open to the discussion of combining allocation tiers. However, SCE cannot support the increase in risk to customers that would occur when decreasing CRR allocations in lieu of auction participation. SCE opposes any reduction in customer benefits or increases in customer risk undertaken to provide modest increases in efficiency or simplification. In addition, SCE cannot entertain the prospect of changes in allocation arising from issues that have previously been resolved at FERC.

SCE believes that allocation should remain a mainstay of customer protection. Based on that presumption SCE favors only those modest changes to the CRR process which will maintain the current levels of CRR allocations.