Stakeholder Comments on

CRR Issues

Submitted by (name and phone number):	Company or entity:	Date Submitted:
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The CAISO requests additional written comments on the Straw Proposals for various CRR-related issues discussed during the April 21, 2008 conference call. The Straw Proposal Papers and presentations are posted at: http://www.caiso.com/1b8c/1b8cdf25138a0.html

Stakeholder comments should be submitted by close of business on Monday, April 28, 2008 to: CRRComments@caiso.com

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Please offer any comments on the following Straw Proposals:

A. CRR Year 2 Release Process

1. Using Season 1 2007 as the historical reference period for verifying Season 1 source nominations in the next annual CRR release process.

2. Treating CRR Seasons 2 and 3 as "Year 2" seasons that are eligible for the Priority Nomination Process in the next annual CRR release process.

   CPUC staff support the "Year 2" treatment of CRRs for Seasons 2 and 3 of 2008. CPUC staff recognize that some LSEs may have made decisions in the previous allocation under this assumption, and changing the treatment of Seasons 2 and 3 may unfairly punish some LSEs for making decisions under the rules in place at the time of the previous nominations.

3. Confirming that Season 4 CRRs will be eligible for the Priority Nomination Process in the next annual CRR release process.

   Consistent with our response to #2, CPUC staff support the proposal to make Season 4 CRRs eligible for the PNP in 2009.

4. Confirming that Q1 LT-CRRs should be treated under the "Year 1" nomination limit, and Q2-4 LT-CRRs should be treated under "Year 2" nomination limit in the next annual CRR release process.

   CPUC staff support this interpretation. There are requests for clarification and/or rehearing on this subject currently pending at FERC. Lacking a ruling on such requests, CPUC staff believe the CAISO's proposal is a reasonable application of the July 9, 2007 FERC order, which required CAISO to establish the phase-in of LTCRR nominations.

B. CRR MW Granularity

5. Adopt the 0.001 MW level (1kW) for the next annual release of CRRs.

C. 30-Day Rule on Outage Scheduling

6. Modifying the 30-Day Rule so that outages initiated and completed within a 24-hour period are exempt (instead of one day).

   CPUC staff support this proposal. Enacting this change should permit more maintenance during off-peak periods, which in turn promotes reliability.

7. Eliminating the exemption criteria that are detailed in Section 10.3.1 of the BPM for CRRs until actual LMP market experience unfolds.

8. Developing an analytical methodology for assessing the impacts of outages on CRR revenue adequacy, and assessing with stakeholders whether revisions to the 30-day rule exemption policy are appropriate.

D. Monthly CRR Eligibility for LSEs Without Verifiable Load Forecasts

9. In the absence of a verifiable load forecast, using the historical load of the same month from the previous five years.

E. **CRR Credit Policy Enhancements**

10.
    a. Disallow netting between allocated CRRs and auctioned CRRs in the credit holding requirement calculation.

       CPUC staff support this proposal. Obtaining CRRs in the CRR auction that offset CRRs obtained in the CRR allocation is functionally equivalent to selling, through secondary markets, CRRs that were obtained in the allocation. As a result, they should be treated in the same way as allocated CRRs that are sold in secondary markets. Disallowing netting will have the same result as requiring credit

coverage at the time of the sale (CPUC supports part (b) and will explain the reasoning for the credit requirement in part (b)).

b. Require LSEs selling allocated CRRs to maintain sufficient credit coverage to cover the counterflow CRRs that offset the CRRs being sold.

CPUC staff strongly support this proposal. CPUC staff suggested this enhancement to credit policy last fall, and appreciate that the CAISO is willing to consider enhanced credit protections at this time. CPUC staff prefer this method for establishing credit as opposed to prohibiting secondary trading of allocated CRRs because this will permit reasonable uses of the secondary market while protecting the CAISO and ultimately ratepayers from CRR income deficiencies.

CPUC staff believe CAISO's proposed credit requirement will promote fairness and efficient market outcomes

When an LSE elects to sell a CRR, the LSE bears the risk of a potential CRR payment and associated credit requirement should the LSE lose load but remain in business. However, ratepayers ultimately bear the risk that potential payments may be required from load if the LSE folds. CPUC staff believe that this risk-reward balance should be borne entirely by the LSE making the decision whether to sell the CRR.

Ratepayer subsidization of LSE risk creates a market distortion: The act of selling a CRR without a credit requirement to cover the risk of load shift, and allocation to load of counterflow CRRs, transfers the cost of that risk from the LSE to its ratepayers. This cost should be considered part of the financial value of the CRR. The only way to ensure that the value is internalized to the initial CRR holder is to require the initial CRR holder to post credit upon sale of the CRR. An economically rational CRR seller will demand a higher price for its CRR if it is required to pay for credit to cover the CRR. In this way, the cost of credit can be integrated into market transactions in CRR sales. Otherwise, ratepayers are subsidizing part of the cost that a CRR seller should be demanding from a CRR buyer, creating a distortion in the market towards more active selling of congestion hedges. This is bad in principle. An incentive to sell hedges for their long term supply arrangements may exposing the LSE, and ultimately ratepayers, to greater risk.

Establishing a credit requirement at the time of the sale of CRRs establishes a protection against this risk. Rather than ratepayers footing the entire bill, credit will have been posted, from which the CAISO can recover the expected value of the CRR.

CPUC staff believe several objections to CAISO's proposal are misguided

Some stakeholders have suggested that this proposal will decrease liquidity in CRR secondary markets, and some of these stakeholders have proposed that the additional credit obligation should be based on the amount of CRRs that are likely to migrate. CPUC opposes these positions.

First, credit for CRRs is not in place to cover events that are likely; rather, it is in place to cover events that are unlikely, similar to a homeowner's fire or earthquake insurance. Simply because an event is unlikely does not mean that ratepayers should assume the risks associated with the unlikely event.

Second, if the requirement to post credit is a burden the seller is unwilling to accept, it may create an alternative transaction with its intended counterparty to transfer future revenues from the CRR to the counterparty in exchange for the up-front payment. This sort of arrangement will have the same result, except where the CRR seller fails to meet its obligations to the CAISO. As a result, rather than forcing the CAISO (and ultimately ratepayers) to assume risk, the counterparty assumes the risk. If, as some parties have insisted, the risk is minimal, then this arrangement should be attractive to potential counterparties, and should present sufficient liquidity for CRR trading. If the risk is serious enough to deter a counterparty from accepting the risk, then we should also believe that the risk is too serious for the CAISO and ratepayers to take on without any compensation.

Third, if the chances of the LSE losing a substantial amount of load are slim, then the LSE should be able to obtain credit to post to CAISO at a reasonable price, thus enabling the LSE to sell the CRR in CAISO's secondary market at a minimal cost for credit. This would be a transfer of risk from the LSE to a third party. If credit is cheaply available, then there is no need for the CAISO to accept risk on behalf of the LSE, and the credit requirement will not create an excessive burden to liquidity. However, if there are not willing counterparties, the risk may be more serious. If that is the case, then it suggests yet another reason that the CAISO should not take on the risk without compensation.

For all the reasons discussed above, CPUC staff believe that CAISO should impose the credit requirement to cover the risk of load migration at the time of the sale of any CRR that may be transferred due to load migration.

Some stakeholders have noted that there are LSEs have load that cannot migrate, and suggest that these LSEs should not have to post credit to protect against an event that cannot happen. At this time, CPUC staff do not oppose an exemption from the credit requirement for LSEs which serves load cannot migrate.

11. Including historical LMPs (a year after MRTU start-up) to improve the credit requirement for holding short-term CRRs.

CPUC staff support CAISO's proposal to establish a credit requirement based on either the historical LMP or the auction price, which ever results in a higher credit

requirement. Given uncertainty regarding the long-term accuracy of initial CRR auction prices, CPUC staff believe the use of historical LMPs is a viable system to use to assist in establishing credit requirements.

Additionally, CPUC staff believe CAISO should consider methods to implement a similar adjustment to credit requirements for Year 1. Year 1 may have the greatest risk of inaccurate auction prices because market participants will have limited experience with the CRR system. CPUC staff suggest that CAISO consider using the results of the LMP Study 3C Results in the place of historical LMPs in order to implement a comparable adjustment in Year 1. This would mean that credit requirements in Year 1 would be set by the auction price or the estimated price from the 3C study, which ever results in a higher credit requirement.

12. Adding a full credit margin to the bidding requirement for participation in CRR auctions.

F. Other CRR Issues

13. Does your company or entity have further comments on these various CRR issues?