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March 20, 2018

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Ashutosh Bhagwat, CAISO Board of Governors
Mark Ferron, CAISO Board of Governors
Angelina Galiteva, CAISO Board of Governors
David Olsen, CAISO Board of Governors - Chair
California Independent System Operator
P.O. Box 639014
Folsom, CA 95630

CAISO Governors,

As load serving entities (LSEs) and representatives of millions of impacted customers within California, we respectfully request the Governors instruct the CAISO to take swift action to remedy systemic problems in the Congestion Revenue Rights (CRR) auction process. According to the CAISO's Department of Market Monitoring (DMM), these structural CRR auction flaws cost California customers \$100 million in 2017, and total costs to California now exceed \$750 million, an average of \$82 million a year.¹

Specifically, the Governors should instruct CAISO management to remedy core structural issues by immediately moving forward with the stakeholder process to discuss the proposal supported by the signatories of this letter as well as the DMM, the so-called "SCE proposal". Moreover, given the significant dollars at stake, such changes should be effective before the 2019 annual CRR auction process commences.

The signatories actively participated in the current stakeholder process and appreciate the CAISO's attention to the issue. Unfortunately, the CAISO has failed to recommend adequate changes, proposes to further delay discussions on structural remedies, and despite a clear and timely written request of the signatories (attached), has declined to move forward with developing a comprehensive solution. In order to stem the ongoing financial harm, the signatories make the well-considered request that the Board instruct immediate action to move forward with a stakeholder process to create a comprehensive proposal that would implement the SCE proposal.

¹ http://www.caiso.com/Documents/Decision_CongestionRevenueRightsAuctionEfficiencyProposal-DMMMemo-Mar2018.pdf

Specifically, the CAISO should change the CRR auction process such that auction transactions only occur between willing counterparties. The Governors should instruct the CAISO to file, if necessary, any tariff changes needed for implementation once the proposal to accomplish this principle has been fleshed out.

This is a significant and ongoing cost for California customers, especially load customers who have unjustly and unreasonably become “default sweepers” paying for a faulty CRR market design and its “inefficiencies”. And as the CAISO contemplates expanding the Energy Imbalance Market to include Day-Ahead functionality in many other states, the harm is likely to increase and impact even more customers in the region unless effective solutions are implemented now. The signatories therefore request that the Governors instruct CAISO management to make all necessary reforms and implement a workable comprehensive resolution implementing the SCE proposal prior to the commencement of the 2019 annual CRR auction process.

Sincerely,



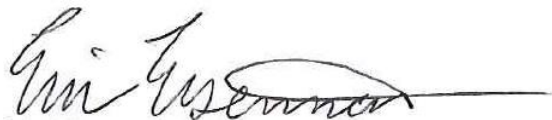
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Enclosure

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An EDISON INTERNATIONAL® Company

March 6, 2018

Steve Berberich, President and CEO
Keith Casey, Vice President, Market and Infrastructure Development
California Independent System Operator
P.O. Box 639014
Folsom, CA 95630

Mr. Berberich and Mr. Casey,

As load serving entities (LSEs) and a representative of end users within the CAISO, we write to you to encourage the CAISO to take immediate action to remedy problems with the Congestion Revenue Rights (CRR) auction that already have cost electricity consumers hundreds of millions of dollars. Specifically, as allowed under the existing tariff, the CAISO immediately should revise the quantity of CRRs held for the auction to zero. This will ensure that auction transactions occur only between willing counterparties, that electricity consumers receive the actual value of congestion, and that revenue shortfalls (and associated costs the CAISO allocates to load) from the auction process will be eliminated.

While we appreciate the CAISO's willingness to propose Track 0 and Track 1 modifications to the current process as shared with the Market Surveillance Committee (MSC) on February 2, 2018 and the stakeholder process meeting on February 23, 2018, these incremental proposals still do not address the fundamental auction design issues. Too much time has passed and too many dollars already have been misappropriated; now is the time to fix the underlying problem.

Through the CAISO's own work and its Department of Market Monitoring (DMM) research, you are well aware that load in the CAISO has lost over \$730 million since 2009¹ – or about \$81 million per year. During original development of the CRR structure, stakeholders believed that competitive forces would produce efficient auction results. The CAISO's own studies have proven otherwise. Auction participants do not face the competition necessary to produce prices that approach the expected value of congestion between the CRR source and sink. Yet the CRR is sold regardless of how far from that expected value the bid price may be.

Since the transmission grid is paid for by electricity consumers, associated congestion rents should rightly flow to those consumers. Indeed, the primary purpose of providing CRRs is to allocate them to consumers via their LSEs, and the process for doing such is to offset consumers' exposure to congestion. In the original CRR auction design, the notion of auctioning CRRs was acceptable to the utility LSEs and customer representatives only on the basis that the price of a competitive auction would yield revenues to

¹ California ISO Department of Market Monitoring Q4 2017 Report on Market Issues and Performance.

consumers consistent with the associated congestion costs. However, based on the analysis performed by the CAISO and DMM, this has not happened, and instead consumers have been deprived of hundreds of millions of dollars of value. This situation has persisted far too long and must be addressed immediately.

LSEs and end user representatives appreciate that other parties also may reasonably seek CRRs to hedge their own congestion risk. However, a hedge in congestion is designed to provide certainty for the delivered price of energy and not to provide a profit on the difference between the auction value and the actual congestion value. This difference occurs because the CAISO auction process forces consumers – through the actions of the CAISO acting as their mandatory agent – to sell CRRs at any price without the right to decline the sale. This is not a competitive market. A competitive market consists of a mechanism in which willing buyers and willing sellers agree to a mutually acceptable price, and this simply does not exist under the current construct. Since there are only willing buyers, and the primary seller is the CAISO selling at any price (with consumers bearing the net costs), there is no competitive market.

Southern California Edison (SCE) has developed a proposal in which the CRR auction would be a true competitive market. It would be conducted between willing buyers and sellers producing prices agreed to by both parties rather than forcing compulsory sales on behalf of consumers. This mechanism would allocate available CRRs requested by LSEs or other eligible entities (after a reasonable derate as determined by the CAISO) as a first step and would not withhold any CRRs for the auction process. This approach is already contemplated and allowed under existing CAISO Tariff and Business Practice Manual authority². LSEs would continue to receive the property rights of their customers through this process. While this allocation may still result in revenue inadequacy, only the LSEs as a whole would receive the benefits and bear the burdens of the revenue inadequacy, so the CAISO would return to consumers the maximum CRR revenues possible. The CAISO would conduct an auction as is done today except that the auction would only clear to the extent that parties bid a flow and an equal and opposite counter-flow. Those wishing to purchase CRRs either to hedge a physical risk or to speculate on value would be able to do so in the auction. This approach completely eliminates revenue shortfalls in the auction since payments to one party will be matched by revenues due from its counterparty. In addition, consumers would receive the actual value of congestion through the allocation process, and LSEs could continue to participate in the auction at their discretion and by acting as their own agent, rather than relying on the CAISO to make the sales on their behalf. In addition, marketers/financial entities and generators would still have all other options of hedging or eliminating congestion risk, including participation in the CRR auction.

Finally, it has often been argued that the ability of any entity to obtain CRRs in the auction adds liquidity to the market. However, liquidity in the CAISO CRR auctions has been provided only by forcing consumers to rely on the CAISO as their mandatory marketing agent, and this liquidity has come at a significantly unreasonable cost of \$730 million. Under the SCE proposal, liquidity will be provided if there are willing counter-parties to provide it. If not, it is an indication the market does not demand the liquidity. Within the SCE-proposed CRR framework supported by the signatories to this letter, we remain open to exploring other mechanisms to encourage liquidity, such as a pre-auction bulletin board

² This approach can be implemented very swiftly and effectively using the existing Auction CRR Full Network Model (FNM) and setting all the line capacities to zero by applying a 100% Global De-rate Factor (GDF) for the seasonal and monthly auction CRR processes. Currently the CAISO derates the CRR FNM by a GDF each month for the allocation and auction CRR processes to account for expected outages that will remain in service within the CRR FNM or expected outages with short duration that are not studied in a power flow analysis. See the CAISO CRR Business Practice Manual, Section 10.3.2.B

where auction participants could disclose potential interest in buying or selling specific CRRs. Such advance information might help focus auction activities on CRR source sink pairs where liquidity might be valued. In addition, the signatories are open to monitoring mechanisms that will ensure the effectiveness and performance of the proposed CRR framework.

In conclusion, the signatories respectfully ask the CAISO to take immediate action to remedy the current CRR auction process and reduce the ongoing harm to electricity consumers based on the current CRR auction implementation. Specifically, management should commit to implementing the willing buyer/willing seller framework such that consumers receive the full value of congestion, the auction no longer creates revenue shortfalls, and most importantly the auction functions as a true competitive market wherein transactions only occur if willing buyers and willing sellers agree to mutually acceptable prices.

Sincerely,



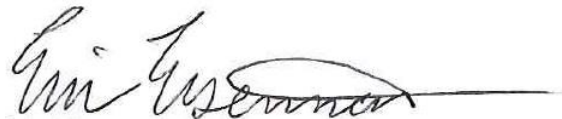
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