

Comments of Financial Marketers Coalition Regarding Congestion Revenue Rights Auction Efficiency Draft Final Proposal

Submitted By	Companies	Date Submitted
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The Financial Marketers Coalition¹ (“Coalition”) appreciates the opportunity to comment on the California Independent System Operator’s (“CAISO”) February 8, 2018 “Track 1” Congestion Revenue Rights (“CRR”) Auction Efficiency Draft Final Proposal, as discussed in the CRR Auction Efficiency stakeholder meeting held on February 13, 2018 (“February CRR Meeting”). The Coalition supports CAISO’s goal to improve CRR auction efficiency, but has concerns with some aspects of the current proposal, and with the expedited timeline CAISO has set for filing and implementation of the proposal.

CAISO’s proposed Track 1 package to address CRR auction efficiency contains four policy proposals. Two of those proposals are aimed at enhancing auction competitiveness consistent with the use of CRRs as a hedge for supply delivery, and the other two proposals are aimed at improving the release of system capacity consistent with the actual transmission that will be ultimately available.

The Coalition generally supports the aspects of CAISO’s proposal that are designed to improve the CRR auction modeling and release of system capacity. In particular, the Coalition supports CAISO’s proposals to (i) create an additional annual outage reporting deadline to be aligned with the annual CRR allocation and auction process; and (ii) lower the percentage of system capacity available in the annual CRR allocation and auction to more accurately model the transmission that will ultimately be available. The Coalition agrees that improving outage information and attempting to provide a better match between system capacity in the annual allocation and auction and the capacity that will actually be available, will improve CRR Auction efficiency. However, the Coalition is not convinced that these measures are needed on an expedited basis in the short term. Instead, they should be considered as part of the upcoming Track 2 comprehensive policy review.

¹ The Financial Marketers Coalition is an industry trade group made up of independent power marketing companies that trade electricity at wholesale in all of the organized ISO and RTO markets. The coalition is an active participant in many ISO/RTO stakeholder proceedings as well as in proceedings before the Federal Energy Regulatory Commission. Many of the coalition members currently trade in the CAISO market, or are interested in doing so.

The Coalition has significant concerns with CAISO's proposals to enhance the competitiveness of the CRR Auction, as discussed in more detail below. The Coalition also expresses support for the comments filed in this issue by DC Energy, with which these comments are aligned.

A. The Coalition has Significant Concerns with Components of the Draft Final Proposal.

1. CAISO's Proposal to Limit Source and Sink Pairs in the CRR Auction Will Lead to Inefficiency

CAISO proposes to restrict eligible source and sink pairs in the auction, by limiting pairs to generator and intertie nodes to trading hubs, loads and interties (only those pairs needed for hedging supply delivery). CAISO posits that node pairs not associated with supply delivery ("non-delivery pairs") do not add counter-flow or competitive flow value to the CRR Auction, hinder the ability of "delivery pairs" to clear the auction, and add to net payment deficiencies. The Coalition disagrees with CAISO's conclusions, and submits that, rather than achieving CAISO's objective of minimizing net payment deficiencies, this proposed restriction would erode competition, result in fewer CRRs being awarded, and decrease realized revenues from the CRR Auction.

CAISO offers a simulation in which it removed non-delivery pair CRR bids from the auction as support for its argument that this restriction will increase competition and increase net auction revenues. However, the Coalition's analysis of CAISO's data reaches a different conclusion. Although CAISO notes that its simulation resulted in an increase in CRR average clearing price (*i.e.*, \$113 to \$117), it fails to acknowledge that the simulation resulted in a significant decrease in overall auction revenue. Despite the apparent increase in CRR clearing price, cleared volume decreased by almost 75% while prices increased by only 30%, resulting in an overall decline in auction revenues by 65%. Eliminating awarded transactions from the CRR auction removes competitively-awarded flow, which is not a reliable means of increasing competition in a network of related transactions. Restrictions on CRR pairs will result in a transfer of congestion rents from CRR holders to Load Serving Entities, ultimately serving to further reduce auction revenues and efficiency. The Coalition believes that CAISO should shift its focus away from reducing net payment deficiency, towards measures intended to improve auction modeling and the release of system capacity, so that cleared CRR pairs accurately reflect the actual capacity available in the market.

The Coalition strongly disagrees with CAISO's conclusions regarding which kinds of transactions are needed to efficiently hedge forward contracts for physical supply delivery. Many of CAISO's stakeholders currently use non-delivery pair transactions to efficiently manage their physical supply risk – CAISO's conclusions appear to ignore the realities of the market. Among the CRRs CAISO proposes to eliminate are pairs where both the source and sink are resource nodes. These transactions are used within a portfolio of resources to move supply from one resource to another for things like maintenance, forced outages, fuel supply risk and weather deviations. For example, financial entities use CRRs within a portfolio of products to provide risk management and hedging services to other market participants.

CAISO's proposal also would disrupt well-established risk management practices that have developed under the current market framework. This portion of CAISO's proposal has drawn significant stakeholder opposition, which to date, CAISO has failed to acknowledge. CAISO should refrain from pushing an agenda that is inconsistent with the needs of market participants, especially when such an approach will lead to unintended consequences and undermine competition in the wholesale and retail power markets.

2. CAISO Should Eliminate Electrically Equivalent CRRs

The Coalition agrees that electrically equivalent CRR pairs should be eliminated from auction clearing because those transactions serve no purpose and ultimately contribute to net payment deficiency. Other ISOs already either remove such pairs or prohibit their submission. CAISO should consider removing electrically equivalent CRRs in isolation, as part of its Track 1 implementation, before considering any further limitations to the availability of source and sink pairs. The Coalition believes that removing electrically equivalent CRR pairs would effectively address CAISO's issues with net payment deficiency and improve CRR auction efficiency, without the need to remove a larger subset of eligible source and sink pairs.

The benefits of removal can be observed in the ERCOT, SPP and PJM markets, which have all experienced quantifiable efficiency benefits from restricting electrically equivalent pairs. CAISO should move forward with implementing this restriction in Track 1 and conduct further analysis to assess the efficiency benefits of the change in isolation before significantly limiting additional source and sink locations with no analysis supporting such a change.

3. Elimination of Modeling Information Disclosure is a Step in the Wrong Direction

The Coalition views CAISO's proposal to eliminate the disclosure of certain modeling information used in the CRR Auction as a step in the wrong direction. CAISO proposes to provide modeled outage information and a list of all possible constraints and contingencies, but will no longer disclose which outages are modeled out-of-service and constraint/contingency enforcement status. CAISO proposes not to release the exact CRR market model, instead only providing the basic information needed to model congestion in the Day-ahead. The premise of the proposal is that CRR bids should be based on the expected grid condition of the day-ahead markets, and not the congestion revenue rights model itself.²

Rather than proposing to adopt a restrictive and opaque model disclosure practice, CAISO should be working to ensure that its practices are moving towards increased transparency, in order to ensure proper price formation and an efficient, well-functioning market. Increased granularity with regard to operator actions and real-time transparency in ISO/RTO markets is a priority for the Federal Energy Regulatory Commission (the "Commission"). In a pending Notice of Proposed Rulemaking ("NOPR") on uplift and transparency practices, the Commission proposes that each ISO/RTO be subject to additional reporting and data granularity

² Servidio, P., CAISO CRR Auction Efficiency Presentation at 15 (Dec. 19, 2017), available at <https://www.caiso.com/Documents/Presentation-CRRAuctionEfficiencyPolicyDiscussion-Dec192017.pdf>.

requirements, including improvements to the accessibility of transmission outage data and network model availability.³

CAISO's proposal will impede appropriate price formation and undermine the objective of minimizing net payment deficiencies in the CRR auction. Eliminating the proposed disclosures will undermine CAISO's objective of minimizing net payment deficiency by impairing market participants' ability to value future congestion outcomes. The artificial uncertainty created by this inability would translate to higher forward risk premiums, which would then be reflected in CRR bids. The Coalition submits that the proposed reduction in transparency could also make it challenging to understand auction results. This could, in turn, erode ability to detect market clearing errors, reducing confidence in the auction's clearing outcomes.

B. The Expedited Timeline for CAISO's Track 1 Process Has Not Been Justified

In addition to the substantive concerns with CAISO's proposal described above, the Coalition is also concerned with the proposed timeline. CAISO has made clear that the Draft Final Proposal is intended as an interim solution to auction inefficiency, with plans to explore comprehensive changes in an upcoming Track 2 policy review process. However, CAISO has not demonstrated that the Track 1 proposal, which has drawn significant opposition from stakeholders during the meetings, should be rushed through the stakeholder process so that CAISO can file a proposal with FERC prior to July 1, 2018.

CAISO's Draft Final Proposal, published on February 8, 2018, has evolved significantly from the proposal submitted by the Department of Market Monitoring in a November 2016 whitepaper, to modify the CRR auction into a market based on bids submitted by entities willing to buy or sell CRRs. The Congestion Revenue Rights Auction Efficiency Working Group has only met on December 19, 2017 and April 18, 2017. During those meetings the Working Group discussed overall policy goals and provided a forum for individual stakeholder presentations, but no draft proposals were presented for stakeholder review. The current Draft Final Proposal was presented to stakeholders for the first time during a Working Group meeting on February 13, 2018.

Stakeholder comments on the proposal are due to CAISO on February 28, 2018, and CAISO intends to seek Board of Governors approval at the March 2018 meeting, which is scheduled for March 21-22, 2018. This expedited timeline does not provide an adequate opportunity for CAISO to review and consider stakeholder comments and suggestions before presenting to the Board for approval. To date no additional Congestion Revenue Rights Auction Efficiency Working Group meetings have been scheduled prior to the March 21-22 Board of Governors meeting. Given the significant opposition voiced by various Working Group participants, stakeholders should be afforded an additional opportunity to voice their concerns and modify the proposal prior to presenting the proposal for endorsement by the Board of Governors.

³ See *Uplift Cost Allocation and Transparency in Markets Operated by Regional Transmission Organizations and Independent System Operators*, 158 FERC ¶ 61,047 at P 82 (2017) ("Uplift NOPR").

CAISO has provided no explanation as to why this expedited timeline is necessary, and has not presented data and evidence that supports the need to move this quickly. As discussed above, the Coalition does not agree with CAISO's conclusion that restricting eligible source and sink pairs in the auction will reduce CRR net payment deficiencies. The Coalition is concerned that, in its haste to implement stopgap measures to address auction inefficiency, CAISO will implement policies that exacerbate the problem.

Instead of rushing to implement interim measures, CAISO should focus on developing, with stakeholders, a comprehensive proposal to enhance CRR Auction efficiency in the upcoming Track 2 policy review process.

If you have further questions or would like to discuss these comments, please do not hesitate to contact Ruta Kalvaitis Skučas at (202) 530-6428 or RSkucas@pierceatwood.com, or Maeve Tibbetts at (202) 530-6435 or MTibbetts@pierceatwood.com.

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