

**Comments of Powerex Corp. on  
Congestion Revenue Rights Auction Efficiency: Track 1B Draft Final Proposal  
Addendum**

Submitted by	Company	Date Submitted
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Powerex appreciates the opportunity to submit comments on CAISO’s May 25, 2018 Congestion Revenue Rights Auction Efficiency Track 1B Draft Final Proposal Addendum (“Addendum”). In the Addendum, CAISO retains its proposal to reduce payments to CRR holders after the close of the day-ahead market to reflect constraints that result in revenue inadequacy due to discrepancies between the amount of transmission available in the day-ahead market and the amount of transmission modeled in the CRR auction. CAISO does, however, propose two changes from previous iterations of its proposal:

- First, CAISO proposes to only reduce payouts to CRRs in the prevailing flow direction in the event of an over-subscribed constraint (*i.e.*, CAISO will not make adjustments to counterflow CRRs).
- Second, CAISO proposes to allow surpluses on one constraint in one hour to offset deficits on the same constraint in another hour over the course of the month. More specifically, CAISO will allow netting on a daily basis and then resettle CRRs at the end of the month, effectively allowing inter-day surpluses on one constraint to offset deficits on the same constraint on another day.

Powerex applauds the significant progress that CAISO has made in addressing the inefficiencies of the existing CRR framework. In particular, Powerex believe that the proposals developed and implemented as a result of Tracks 1A and 1B of this proceeding will provide material benefits in the form of reduced CRR revenue inadequacy and improved efficiency of the CRR auction process.

As Powerex has noted, Powerex believes that CAISO effectively has three options available to address the potential that changes in topology between the CRR model and day-ahead market will create CRR revenue inadequacy:

1. reduce the amount of transmission capacity sold on a forward basis;
2. socialize the costs of de-rates by allocating any resulting shortfalls to load on a load ratio share basis; or
3. allocate the costs and risks associated with de-rates to entities holding CRRs on the affected transmission paths.

Powerex believes that CAISO's decision to adopt an approach that allocates the costs and risks associated with de-rates to CRR holders on the affected paths represents an important step forward in terms of addressing the issue of CRR revenue inadequacy and a material improvement over the existing framework. By reducing payouts to CRR holders on affected paths, CAISO's proposal will ensure that the costs of CRR revenue inadequacy are allocated equitably to CRR holders and will protect load from being forced to bear costs that it neither causes nor has any ability to prevent.

Powerex believes that the Addendum proposal is an appropriate interim approach that addresses CRR revenue inadequacy in a more equitable manner than occurs at present. Powerex notes, however, that the proposed adjustment to financial settlement of CRRs introduces new risk and uncertainty for CRR holders, who will no longer be able to rely on those CRRs to provide a complete hedge against day-ahead market congestion charges on the designated path. As discussed further below, Powerex is highly supportive of CAISO pursuing a design that involves an ex ante volumetric de-rate to CRR holdings on affected paths, and communicates these reductions to CRR holders ahead of the day-ahead market. While CAISO agrees that such a design would be preferable, Powerex acknowledges CAISO's concern that it could not be implemented in time for application to the settlement of CRRs in 2019. Powerex does believe, however, the CAISO should provide additional information to CRR holders that could be used to develop more accurate estimates of the potential financial adjustment that certain CRRs are likely to experience. Specifically, Powerex believes that this can be achieved by CAISO publishing a table each day, prior to the day-ahead market bid submission deadline, that identifies:

- Each constraint that will be modeled in the day-ahead market run with a rating that differs from the rating used in the CRR model;
- Total CRR-settled flow on the constraint, broken out by prevailing and counterflow CRRs and by time-of-use period; and
- The expected capacity of the constraint in the day-ahead market run, broken out by hour.

Powerex believes that implementation of this proposal will enhance the ability of market participants to determine whether their CRR holdings will hedge their exposure to congestion charges when submitting bids and offers in the day-ahead market.

Powerex also supports the changes to CAISO's proposal outlined in the Addendum. As an initial matter, Powerex agrees with CAISO's proposal to limit any reduction to CRR holders' payouts to CRRs in the prevailing flow direction only. In particular, Powerex believes that CAISO's original proposal to reduce the payments received from counter-flow CRRs had the potential to exacerbate, rather than resolve, CRR revenue inadequacy. Powerex agrees that "[r]educing payments from counter-flow congestion revenue rights actually makes revenue insufficiency worse on the constraint by increasing the amount by which payments to positively valued congestion revenue rights might be reduced."

Powerex believes that CRRs should only experience a de-rate or financial adjustment to the minimum extent necessary to address revenue adequacy and that it is both inequitable and

inefficient to de-rate CRRs or reduce payments associated with CRRs that do not contribute to revenue inadequacy. For this reason, Powerex believes it would not be appropriate to de-rate or apply charges to CRRs on paths that do not have a material shift factor to the de-rated constraint, nor would it be appropriate to do so on counterflow CRRs. De-rating or applying a financial charge to counterflow CRRs exacerbates revenue inadequacy, while de-rating CRRs on other paths merely socializes the cost of revenue inadequacy to participants that neither contribute to, nor benefit from, the applicable de-rated constraint.

Powerex also supports CAISO's proposal to permit monthly netting of revenue shortfalls and surpluses on a constraint. In practice, the quantity of transmission that is available over a particular path is likely to vary on an hour-to-hour and day-by-day basis. For instance, where CAISO has auctioned off 1,000 MW of CRRs on a particular path, the actual capacity available over that path may be higher than 1,000 MW in some hours (e.g., 1,200 MW) and lower than 1,000 MWs in others (e.g., 800 MW). Powerex believes that it would be inappropriate to require CRR holders to bear the risks and costs of transmission de-rates without allowing CRR holders to offset those costs with surplus congestion revenues that occur when the transmission available in the day-ahead market over a particular path exceeds the quantity of capacity modeled for CRR purposes. For that reason, Powerex supports CAISO's proposal to allow surpluses collected on a constraint in one hour to offset shortfalls incurred on the same constraint in a different hour.

Powerex agrees that the above netting should be performed on a constraint-by-constraint and month-by-month basis. This is necessary to avoid cost-shifting or cross-subsidization of revenue shortfalls on one constraint in one month through application of surplus congestion revenues collected on a different constraint or in a different month. Powerex believes that one additional limitation is necessary to give full effect to the intended design of the netting mechanism, however. Specifically, surplus congestion revenues should only be used to reduce revenue shortfalls on the same constraint, in the same month, *and in the same time of use period*. That is, surplus congestion revenues realized during on-peak hours should only be used to reduce CRR shortfalls during on-peak hours (on the same constraint, within the same month). This is necessary because CRRs are defined for (1) a source/sink pair; (2) a calendar month; and (3) a time-of-use period (on-peak versus off-peak). If netting is allowed across different time-of-use periods, one group of CRR holders stands to benefit at the expense of other CRR holders, or at the expense of load customers that are the ultimate recipients of surplus congestion rents. Powerex requests that CAISO clarify this additional limitation of the netting mechanism in the next version of its proposal.

While Powerex supports CAISO moving forward with implementation of the Track 1B proposal, Powerex believes that CAISO should move forward with development and implementation of more comprehensive long-term changes to the CRR framework as part of Track 2 of this proceeding as soon as possible. As Powerex has explained, Powerex believes that Track 2 of this initiative should focus on two primary issues:

- **Implementation of an ex ante approach that de-rates CRRs in advance of the day-ahead market:** As CAISO has acknowledged, one shortcoming of CAISO's current proposal is that it does not provide notice to market participants in advance of the

submission of bids into the day-ahead market whether their CRR holdings will effectively mitigate their exposure to congestion charges. In order for CRRs to achieve their purpose of allowing market participants to hedge their exposure to congestion associated with physical deliveries, it is important that market participants receive notice of any potential de-rates or reductions to their CRR portfolio in advance of the day-ahead market. Although Powerex supports CAISO moving forward with its Track 1B proposal as an interim measure, Powerex believes that CAISO should immediately move forward with efforts to establish an ex ante approach that more fully aligns with the core purpose and function of CRRs in an organized market.

- **Phasing out the CRR allocation process:** As explained in detail in Powerex's earlier comments in this proceeding, Powerex believes that the existing CRR allocation framework is a significant and growing source of inefficiencies in the CAISO markets. More specifically, the existing allocation of CRRs to load-serving entities ("LSE") on a load ratio share basis disadvantages small LSEs and other market participants, effectively stranding intertie capacity and artificially constraining the ability of California LSEs to purchase RA from external suppliers. In addition, the existing framework effectively has rendered large LSEs physical intermediaries between external suppliers and the CAISO grid, which has increased the use of self-scheduling at the CAISO interties and reduced operational flexibility for CAISO.

Powerex believes that each of these issues should be addressed as soon as possible and encourages CAISO to move forward with Track 2 of this initiative without delay.