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COMMENTS OF THE PUBLIC ADVOCATES OFFICE ON THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR'S 2021 REVISED DRAFT POLICY INITIATIVE CATALOG

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The Public Advocates Office at the California Public Utilities Commission is California's independent consumer advocate with a mandate to obtain the lowest possible rates for utility services consistent with reliable and safe service levels, and the state's environmental goals.¹ The Public Advocates Office submits comments and recommendations specific to the following initiatives in the California Independent System Operator's (CAISO) 2021 Revised Draft Policy Initiative Catalog: 1) Congestion Revenue Rights (CRR) Auction Efficiency Track 2,² 2) Allowing Convergence Bidding at CRR Sub-Load Aggregation Points,³ and 3) Implement Point-to-Point Convergence Bids, and general comments and recommendations on initiative prioritization and cost-benefit analysis.

Comments and Recommendations

Congestion Revenue Rights Auction Efficiency Track 2 Initiative

The CAISO proposes to remove CRR auction efficiency Track 2 from its 2021 Policy Initiative. The Public Advocates Office does not support deleting CRR auction efficiency Track 2 at this time because of continued CRR auction revenue inefficiencies, possible undervaluation of CRRs, and overlap with the Extended Day-Ahead Market (EDAM) stakeholder process.

Recognizing that the CRR auction revenues were consistently lower than the payments to CRR holders, the CAISO opened the Track 1 stakeholder process to improve the CRR auction market efficiency⁴. This led to the Track 1A and Track 1B changes to the CRR auction market,

¹ California Public Utilities (Cal. Pub. Util.) Code § 309.5.

² Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, Section 8.1, p. 37.

³ Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, Section 7.1.30, p. 30.

⁴ Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, p. 37.

which included limiting non-delivery source/sink combinations of CRRs⁵ and limiting CRR payments to the actual congestion rents collected on the associated transmission constraints.⁶

The Track 1A and Track 1B changes were formally incorporated in the CRR auction in January 2019.⁷ The CAISO states that in its opinion, CRR auction revenues have improved in sufficiency and efficiency such that it proposes to close the Track 2 CRR auction efficiency initiative.⁸

In its recent report,⁹ the CAISO recognized that although the CRR auction efficiency improved as a result of the Track 1A and Track 1B changes, the CRR auction market still continues to suffer from differences in auction revenues versus payments to CRR holders.¹⁰ While the CRR auction market was 87% and 80% efficient in 2019 and 2020, respectively (up from 47% in 2017 and 2018), the market still experienced shortfalls¹¹ of 14.1 million in 2019 and \$6.7 million in Q1 2020).¹² The CAISO's Department of Market Monitoring (DMM) further states that of the \$22 million ratepayers lost in the CRR auction in 2019, \$16 million was from Q4 2019 alone.¹³ While these losses decreased from the \$860 million in ratepayer losses between 2009 and 2018,¹⁴ there are still losses despite the improvements to the CRR auction efficiency. Given these consistent losses, the Public Advocates Office recommends that the CAISO and stakeholders continue to research, analyze, address, and explore the CRR auction revenue losses and auction inefficiency in Track 2.

⁵ Congestion Revenue Rights Auction Efficiency Track 1A Draft Final Proposal Addendum, California Independent System Operator, March 8, 2018, p. 28.

⁶ Congestion Revenue Rights Auction Efficiency Track 1B Draft Final Proposal Second Addendum, California Independent System Operator, June 11, 2018, p. 28.

⁷ CRR Market Analysis Report, Market Analysis and Forecasting, California Independent System Operator, May 12, 2020, p. 4.

⁸ "Reason for deletion: Analysis shows significant improvement in auction efficiency and revenue sufficiency as a result of the Track 1A and Track 1B market changes. CAISO will continue to review congestion revenue right performance and does not see a need for another initiative at this time." Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, p. 37.

⁹ CRR Market Analysis Report, Market Analysis and Forecasting, California Independent System Operator, May 12, 2020.

¹⁰ CRR Market Analysis Report, Market Analysis and Forecasting, California Independent System Operator, May 12, 2020, p. 1.

¹¹ Shortfalls are the difference between the revenue collected in the CRR auction market versus what the CRR holder paid for it in the Day-Ahead Market. CRR Market Analysis Report, Market Analysis and Forecasting, California Independent System Operator, May 12, 2020, p. 5.

¹² CRR Market Analysis Report, Market Analysis and Forecasting, California Independent System Operator, May 12, 2020, p. 5.

¹³ 2019 Annual Report on Market Issues and Performance, Department of Market Monitoring, June 2020, p. 13.

¹⁴ 2019 Annual Report on Market Issues and Performance, Department of Market Monitoring, June 2020, p. 13.

The CAISO also observed that while negative CRR auction revenues decreased from \$11.9 million (2018 and 2019) to \$7.8 million (2020), 63% of those negative revenues were from load-serving entities (LSEs) selling previously allocated CRRs in the auction.¹⁵ The CAISO states that this demonstrates a significant undervaluing of CRRs from LSEs,¹⁶ which has a growing influence on prices of CRRs in the auction market. While the CAISO proposes to remove the CRR Track 2 auction efficiency initiative from its 2021 Policy Initiatives, it provides no alternative, transparent avenue for stakeholders to offer guidance on this issue, particularly from the LSEs themselves.

Finally, CRRs are currently proposed in the scope of the CAISO's EDAM proposal.¹⁷ Any fundamental flaws or changes in the CRR market would influence the outcome of the EDAM proposal. Given this link between the EDAM proposal and the CRR market, the CAISO should proceed with the CRR Track 2 auction efficiency process to allow for transparency and stakeholder input from stakeholders that may be affected by both the EDAM and CRR market functions..

Therefore, because of the consistent CRR auction inefficiencies, the potential undervaluation of allocated CRRs in the CRR auction market, and the link in scope between the EDAM and CRR market, the Public Advocates Office does not support deleting CRR auction efficiency Track 2 at this time.

Allowing Convergence Bidding at CRR Sub-Load Aggregation Points Initiative¹⁸ and Implement Point-to-Point Convergence Bids Initiative¹⁹

Convergence bids are financial positions taken in the day-ahead market that are paid out in the real-time market.²⁰ It is a purely financial hedge – with no obligation to provide physical power – that allows market participants to limit their exposure to the difference between day-ahead and real-time energy prices.²¹ According to the CAISO's Department of Market Monitoring (DMM) 2019 Report on Market Issues and Performance, 70% of cleared virtual positions in 2019 were held by “financial participants.”²² This means that the actors who dominate this market do not

¹⁵ Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, p. 4.

¹⁶ CRR Market Analysis Report, Market Analysis and Forecasting, California Independent System Operator, May 12, 2020, p. 4.

¹⁷ Extended Day-Ahead Market Bundle One Straw Proposal, California Independent System Operator, July 20, 2020, p. 32

¹⁸ Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, Section 7.1.30, p. 30.

¹⁹ Revised Draft 2021 Policy Initiatives Catalog, Market Infrastructure and Policy, California Independent System Operator, August 12, 2020, Section 7.1.31, p. 30.

²⁰ Convergence Bidding Overview. Presentation by the California Independent System, Operator 2010.

²¹ Mullin, Robert and Sangree, Hudson, CAISO Blames Blackouts on Inadequate Resources, CPUC. RTO Insider, August 18, 2020.

²² Annual Report on Market Issues and Performance, Department of Market Monitoring, June 2020, p. 156.

provide physical generation and are only looking to profit off the difference between day-ahead and real-time energy prices. Overall, virtual bidders had net profits of \$44 million in 2019.²³

The most recent weather conditions (heatwaves) in the western region during the week of August 16, 2020 have led to an increase in load and a reduction in resource availability as all affected areas in the western region were trying to balance their own load. As a result, the CAISO suspended convergence bidding during that time period to give it a “clearer picture of day-ahead market conditions.”²⁴ The CAISO should investigate the role of convergence bidding in promoting energy market efficiency, especially given DMM’s statement that “the degree to which convergence bidding has actually increased market efficiency... has not been assessed.”²⁵ Therefore, Public Advocate Office recommends that before the CAISO acts on its proposed initiatives to allow convergence bidding at sub-load aggregation points and implement point-to-point convergence bids,²⁶ it should open an initiative to address the following questions:

- Did convergence bidding hinder the ability of the CAISO and market participants to adequately prepare for the extreme heat events experienced during the week of August 16, 2020?
- Overall, what role did convergence bidding play in the events of that week?
- Does convergence bidding increase market efficiency?
- Is convergence bidding accomplishing its original goal of making day-ahead and real-time prices more consistent?

The evaluation of these critical questions will inform the value of the CAISO proposed initiative to allow convergence bidding at sub-load aggregation points and to implement point-to-point convergence bids.

General Comments

- *Initiatives Prioritization*

The Public Advocates Office recommends that the CAISO should prioritize its proposed 2021 Policy Initiatives to ensure continued fair and competitive prices for ratepayers and to ensure safe and reliable services to ratepayers. The CAISO’s attempt to complete several initiatives at the same time may compromise the quality of the market design with costs that exceed benefits to ratepayers. The Public Advocates Office recommends that grid reliability and resiliency, market

²³ Annual Report on Market Issues and Performance, Department of Market Monitoring, June 2020, p. 158.

²⁴ Mullin, Robert and Sangree, Hudson, CAISO Blames Blackouts on Inadequate Resources, CPUC. RTO Insider, August 18, 2020.

²⁵ Annual Report on Market Issues and Performance, Department of Market Monitoring, June 2020, p. 154.

²⁶ Revised Draft 2021 Policy Initiatives Catalog, California Independent System Operator, August 12, 2020, Section 7.1.30 and 7.1.31, p. 30.

design quality, fair and competitive prices, and cost effectiveness to ratepayers should continue to be the CAISO's priority focus.

For example, the CAISO needs to further examine the Day-Ahead Market Enhancement (DAME) initiative by conducting a thorough cost-benefit evaluation and analysis. In the DAME initiative, the CAISO proposes to end the Residual Unit Commitment (RUC) procurement process and establish four new products, the Residual Capacity Up/Down (RCU/RCD)²⁷ and Imbalance Reserves Up/Down (IRU/IRD),²⁸ as capacity products like what the RUC process currently provides.²⁹ However, the CAISO's proposal to create RCU/RCD and IRU/IRD products to replace RUC will increase the costs to ratepayers with no additional benefits. Therefore, the cost and benefits of the DAME initiative needs to be further evaluated.

- *Cost-Benefit Analysis*

The Public Advocates Office recommends the CAISO should provide California stakeholders a cost-benefit analysis for its proposed 2021 Policy Initiatives. This recommendation is especially important for complex initiatives such as DAME, EDAM, and Energy Imbalance Market (EIM) Governance Review Committee (GRC). The CAISO should provide the financial and economic impact of its proposed initiatives on ratepayers to enable stakeholders to comprehensively evaluate the implications of these initiatives.

Conclusion

The Public Advocates Office recommends: 1) keeping the CRR Track 2 initiative open and does not recommend its deletion at this time, 2) investigating the convergence bidding practice prior to considering whether to allow convergence bidding at sub-load aggregation points and implementing point-to-point convergence bids, 3) opening an initiative to evaluate and address convergence bidding efficiencies and/or deficiencies, and 4) prioritizing initiatives that provide safe and reliable services to ratepayers and provide stakeholders with cost-benefit analysis, especially on complex initiatives.

If you have any questions regarding these comments, please contact Lina Khoury at either Lina.Khoury@cpuc.ca.gov or 415-703-1739.

²⁷ RCU/RCD is a proposed CAISO market-procured capacity product that would award resources for increasing or decreasing their generation in the real-time market, procured at an amount equal to the difference of bid-in load and CAISO forecasted load. Day-Ahead Market Enhancements Revised Straw Proposal, California Independent System Operator, June 8, 2020, p. 4.

²⁸ IRU/IRD is a proposed CAISO market-procured capacity product that would award resources for increasing or decreasing their generation in the real-time market, procured at an amount to adjust for forecast error and variable resource generation uncertainty. Day-Ahead Market Enhancement Revised Straw Proposal, California Independent System Operator, June 8, 2020, p. 4.

²⁹ Day-Ahead Market Enhancement Revised Straw Proposal, California Independent System Operator, June 8, 2020, p. 13.