

MEMORANDUM

TO: UTILITIES ADVISORY COMMISSION

FROM: UTILITIES DEPARTMENT

DATE: MAY 2, 2007

**SUBJECT: APPROVAL OF CONGESTION REVENUE RIGHTS
PRODUCT TO MITIGATE ELECTRIC TRANSMISSION
CONGESTION COST**

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REQUEST:

Staff requests that the UAC recommend that City Council: 1) Approves changes to Section XI of the City's Energy Risk Management Policy to allow Congestion Revenue Rights (CRRs) to be included in the list of approved electric portfolio products; and 2) Authorizes the City Manager to sign a contract with the California Independent System Operator (CAISO) or to authorize Northern California Power Agency (NCPA) to execute the necessary agreements to request CRRs from the CAISO on behalf of the City and to manage the CRR for the purpose of mitigating the potential electric transmission congestion costs' impact of the City's retail electric customers.

BACKGROUND:

Following the 2000-2001 electricity market crisis in California, the CAISO, under the direction and approval of the Federal Energy Regulatory Commission (FERC), has been developing a new transmission market design. The stated objective of the new design is to increase electricity and transmission market efficiencies and improve transmission grid reliability. This new market design, officially named Market Redesign and Technology Upgrade (MRTU), is planned to start on January 31, 2008.

Implementation of MRTU will bring about many changes in scheduling and settlements of loads and generation over the CAISO controlled transmission grid. One of the key changes will be an explicit charge to users of the electricity grid for the cost of congestion associated with delivering energy to meet loads. As part of the new market design, the CAISO has also developed a tool named Congestion Revenue Rights (CRR), an insurance-like product designed to mitigate transmission congestion costs that Load Serving Entities (LSE) like the City will be subject to upon the implementation of MRTU in January 2008.

DISCUSSION:

The CRR product and the allocation process have been designed by the CAISO to protect and compensate loads (customers) from the new incremental congestion costs of the market redesign. These CRRs will be allocated free of charge to LSEs to hold and to manage for their customers. Based on the studies undertaken by Northern California Power Agency

(NCPA) on behalf of its members, the value of CRRs that the City has the right to obtain from the CAISO is expected to be positive, though the exact value is highly uncertain. At this time there are no alternative products available to manage this new congestion cost exposure under MRTU. A more complete discussion and the rationale for seeking approval to request and manage CRRs through NCPA to reduce the impact of transmission congestion costs on the City's retail electric customers is provided in Attachment A.

POLICY IMPLICATIONS

CRRs are a form of 'financial product', a class of product that is currently prohibited under Section XI of the Energy Risk Management Policy approved by Council in February 2006 (Resolution No. 8591). The prohibition was designed mainly for financial derivative products which have considerably more risks, compared to a CRR product which is allocated free of charge to LSEs to protect against congestion costs. Based on this analysis, the Utilities Risk Oversight and Coordinating Committee (UROCC) voted to approve the CRR product on April 16, 2007 and has recommended it for Council approval. Proposed changes to the Risk Management Policy are highlighted in Attachment B.

RESOURCE IMPACTS

The CRRs the City expects to request through NCPA are expected to have a positive value and are expected to reduce the City's congestion costs. Participation in the CRR requesting and management process is expected to reduce the cost of serving the City's retail electric load.

ATTACHMENTS:

- A. Presentation - Requesting the UAC to recommend the CRR Product for Council approval
- B. Proposed Changes to Section XI of the Energy Risk Management Policy

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