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DOCKET NO. 24770

REPORT OF THE ELECTRIC
COMMISSION
RELIABILITY COUNCIL OF TEXAS
(ERCOT) TO THE PUCT REGARDING
IMPLEMENTATION OF THE ERCOT
PROTOCOLS

§ PUBLIC UTILITY
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§ OF TEXAS

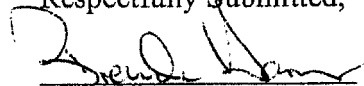
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**RELIANT RESOURCES, INC.'S
SUBMISSION OF MAY 14, 2003 PRESENTATION**

Pursuant to Order No.19, a technical conference was held May 14, 2003 to discuss Staff's modified competitive solution method. Reliant Resources, Inc. (RRI) made a presentation at that technical conference entitled "Mitigation Methods for the ERCOT Balancing Energy Market."

RRI now submits a copy of that presentation for the record.

Respectfully Submitted,


Brenda Harris

Mitigation Methods for the ERCOT Balancing Energy Market

Docket No. 24770

***Report of the Electric Reliability Council
of Texas (ERCOT) to the PUCT
Regarding Implementation of the ERCOT
Protocol***

May 14, 2003 Technical

Parties That Generally Support the Proposal

- *City of Austin*
- *City Public Service San Antonio*
- *CenterPoint Energy*
- *Dynegy*
- *Lower Colorado River Authority*
- *AEP*
- *Mirant*
- *TXU*
- *Reliant Resources Incorporated*

Desired Market Model

- *Stability and Clarity of Market Rules*
- *Prices Result from Competitive Market Dynamics*
- *Less Regulatory Intervention*
- *Unrestricted Opportunities to Contract and Manage Market Risk*
- *Timely Investment*

Current Balancing Energy Market Structure

- *ERCOT procures balancing energy to cover real-time differences between load and supply*
- *All balancing energy obtained by ERCOT is paid out at the price of the highest bid accepted*
- *On average, balancing energy represents less than 10% of the energy supplied in the ERCOT region*

Mitigation Issue

- *Infrequently, the highest bid accepted is at or near the \$1,000 bid cap*
 - *From market opening through March 27, 2003, the bid stack was exhausted 512 times out of 58,000 intervals, approximately 0.9% of the time, according to ERCOT*
- *The highest accepted bid sometimes is based on a bid of only a few megawatts*
- *MOD seeks mitigation rules to prevent this result, which is generally characterized as “hockey stick” bidding*

Competition Provides the Most Effective Price Discipline

- *Allows proper response to scarcity*
- *Disciplines both the supply and demand sides of the market*
 - *Retail providers are incented to control around price uncertainty*
 - *Suppliers can provide additional resources in response to price signals*
- *Competitive markets can respond without the need for regulatory intervention*

Adverse Effects of MOD MCSM 95% Mitigation Proposal

- *Different bidding approach by resources as they react to the new rules, which may lead to less effective market outcomes*
- *Greater use of balancing energy market with its artificially depressed prices*
- *Corresponding decrease in independent risk management*

Adverse Effects of MOD MCSM 95% Mitigation Proposal

- *Reduced capital investment as price investors respond to dampened price signals*
- *Accelerated unit retirement/move to RMR*
- *Difficulty of creating and applying a “verifiable cost” methodology*

Adverse Effects of MOD MCSM 95% Mitigation Proposal

- *Scarcity only occurs due to short-term and usually random events*
 - *Long-term scarcity in balancing energy stack has little meaning*
- *Scarcity usually occurs in the last 2-3% of the bids*
 - *MCSM's cut off of 5% of the bid stack either eliminates scarcity or forces the market to bid higher overall, which raises the average MCPE*

Any Mitigation Methodology Has Unintended Consequences

- *Rules that are overbroad will lead to unintended consequences and result in inefficient markets that require regulatory intervention*
- *Implementation of a mitigation methodology will not necessarily result in lower average prices*
- *If ERCOT systems do not synchronize mitigated zonal MCPs and shadow prices, arbitrage opportunities will be created*

Mitigation Proposal

- Define a “hockey stick” bid as:
 - the last price/volume pair:
- has a volume less than 3% of the QSE’s total volume included in the bid curve, and
- is greater than three times the price of the immediately preceding price/volume pair in the bid curve

Mitigation Proposal

- *ERCOT has not declared an EERC event when it selects the volume of energy from the balancing energy stack, and*
- *No more than one independent bid by an unaffiliated QSE has already been declared hockey stick bid or the sum of hockey stick bids is not greater than 25 MW*
- *ERCOT evaluates bid stack and excludes hockey stick bids*

Implementation

- *No proposal offered to date can be fully implemented by ERCOT in time for the summer peak (ERCOT May 8 filing)*
- *Target system implementation date of November 2003 (subject to completion of ERCOT system changes)*

Certificate of Service

I hereby certify that a true and correct copy of the foregoing document was served on all parties of record in this proceeding by hand delivered, courier, certified mail (return receipt requested), registered mail, facsimile, electronic mail or sent by overnight delivery or United States first class mail on this 16th day of May 2003.

Shirley A. Myers