NPRR 140

DC Energy Comments

September 16, 2008

DC ENERGY

QUANTITATIVE TRADING

NPRR 140
– DC Energy Comments –

- **Auction credit constraint should mirror post auction credit requirements**
  — There are valid concerns for wanting auction adders greater than post auction adders
  — However, in using the FMM (forward mark-to-market) view in addition to ACPE (Auction Clearing Price Exposure) for PTP obligations, we have accepted the possibility that at some point a collateral call to cover delta between FMM and ACPE might be needed
  — We should seek alternatives that could allow for covering of FMM without penalizing bids that are not in violation

- **Negative bids should not require collateral beyond the additional credit requirement for awarded PTP obligations**
  — Negative bids self fund the clearing price component of the credit requirement
  — Participants can circumvent existing rule by bidding zero or positive for negative CRRs

- **Credit requirements are an important part of these market**
  — They also have a negative impact on liquidity, transparency, and cost of doing business
  — The safest level of credit requirement is infinite: no one participates and there is no default risk

Agenda
– DCE Comments NPRR 140 –

→ • **Auction Credit Constraint Changes**

• **Negative CRR Bids**

The FMM component of FCE makes it difficult to predict FCE with certainty

CRR Ongoing Credit Requirement

$$FCE = max(ACPE, -FMM)$$

Future Credit Exposure for PTP Obligations

Auction Clearing Price Exposure for PTP Obligations

Forward Mark-to-Market Obligations (the weighted average of different recent time periods)

Scenarios where FMM exceeds ACPE after the auction and during the auction are comparable; there is no need to have more stringent auction requirements

Changing Auction Credit Constraint
– Credit Requirements –

Illustrative
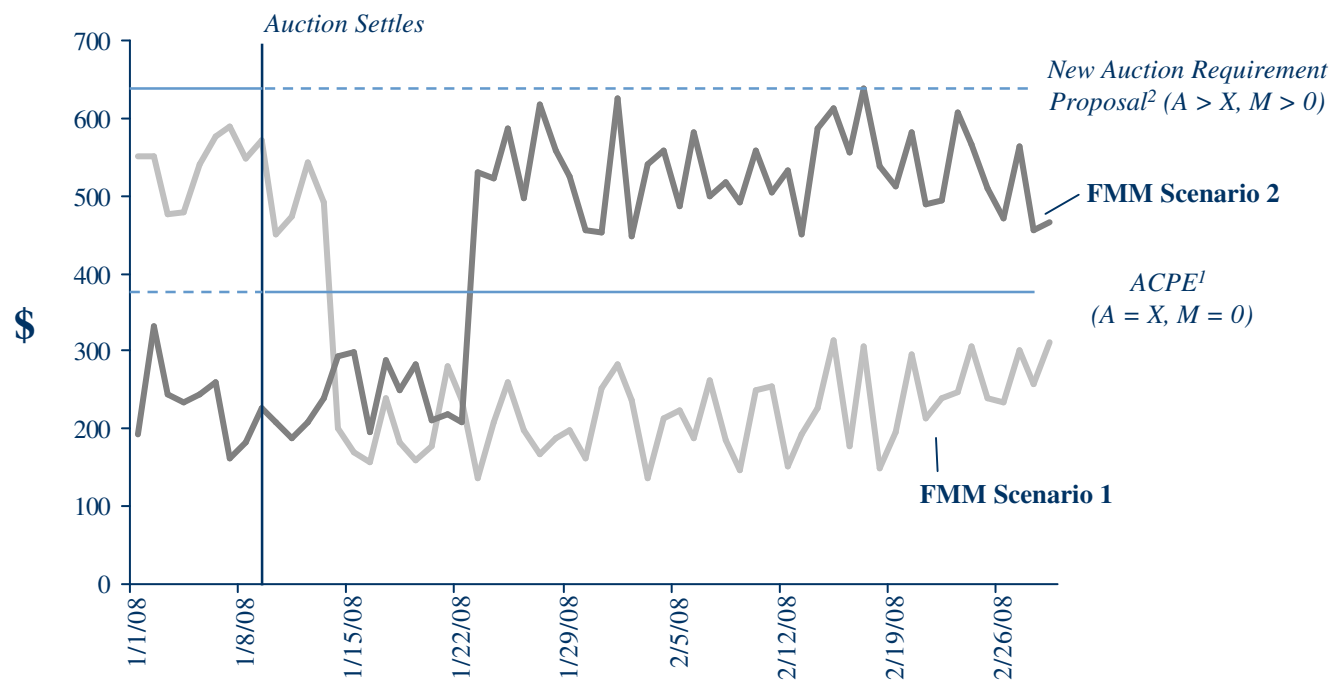
Assuming A = X and M = 0, the collateral call ERCOT has to issue under FMM scenario 1 is equivalent to that in FMM scenario 2. Given we are willing to tolerate scenario 2 we should tolerate scenario 1.

[1] Auction Clearing Price Exposure for PTP Obligations; A is additional requirement for bids, X is additional requirement for holding; M is percent of clear price to be added to requirement for bids as per ERCOT comments to NPRR 140

[2] There is no guarantee A > X and M > 0 will ensure Auction requirement is sufficient to cover FCE

- We recommend that the auction credit adder be the same as the post auction credit adder (i.e. A = X)

- We recommend that the multiplier to bid price requirement be kept at zero (i.e. M = 0)

- Alternatively, develop system that requires collateral to comply with FMM for only those paths that have an FMM exceeding ACPE
  — Lookup tables? – likely implementation difficulties at this stage

Agenda
– DCE Comments NPRR 140 –
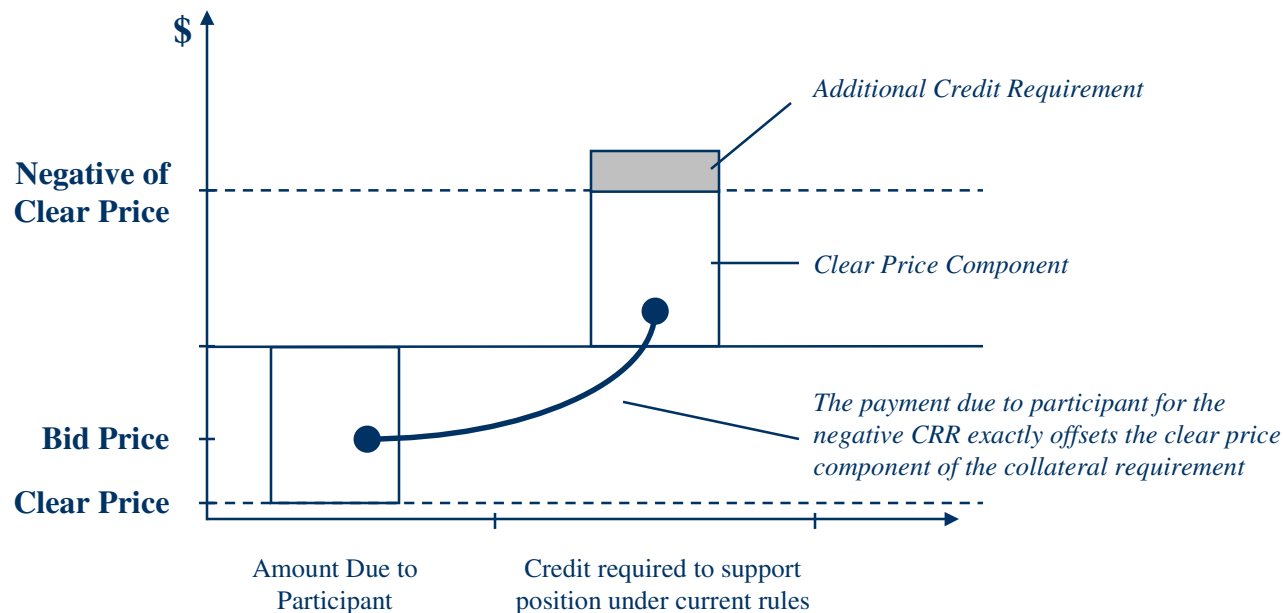
- **Auction Credit Constraint Changes**

- **Negative CRR Bids**

Since negative CRRs self-fund the clearing price component, it is unnecessary to ask the holder to cover the absolute value of negative bids

Credit Requirement & Cash Flow
– Negative Price Cleared CRR –

Illustrative

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Additional Credit Requirement

Negative of Clear Price

Clear Price Component

Bid Price

The payment due to participant for the negative CRR exactly offsets the clear price component of the collateral requirement

Clear Price

Amount Due to Participant

Credit required to support position under current rules

> *ERCOT can guarantee that a participant clearing a negative CRR will have funds to cover that CRRs clearing price credit component; only the additional credit requirement needs to be provided*

DC Energy proposes modifying 7.5.5.3(1)(a)(i) from the nodal protocols because it results in unnecessary collateralization of negative bids

Credit Auction Credit Constraint
– Nodal Protocols –

7.5.5.3 Auction Process

(1)   (a) …The credit constraint for each Counter-Party ensures that the following sum for all of the Counter-Party's CRR Account Holders is less than or equal to the Counter-Party's CRR Auction credit limit:

(i) all awarded CRR Auction Bids multiplied by the absolute value of the corresponding bid price; plus

Suggested change >   **(i) all awarded CRR Auction Bids with a positive bid price multiplied by the corresponding bid price; plus**

(ii) all awarded CRR Auction Offers with negative offer prices multiplied by the absolute value of their corresponding offer price; plus
(iii) the additional credit requirement for all awarded PTP Obligations.

Collateralizing negative bids does not provide protection to the market because a participant can circumvent that requirement by offering at zero or positive.
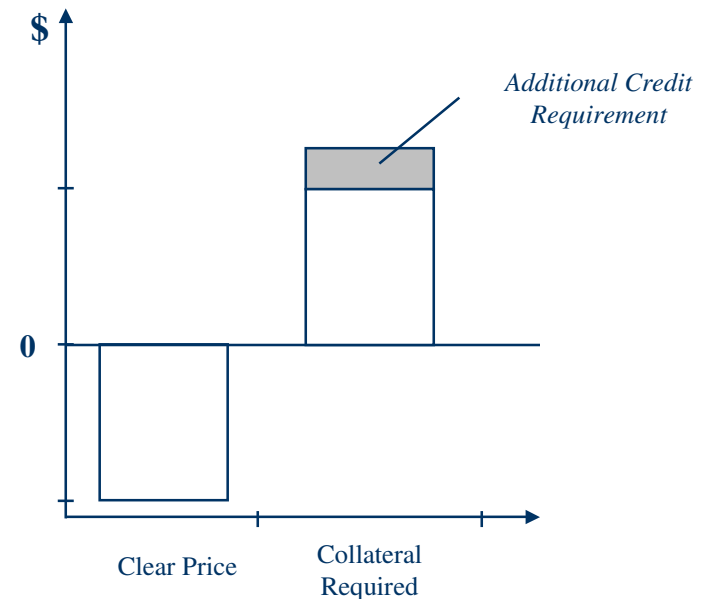
Zero Price Bids
– Credit Requirements –

Illustrative

Requirements for Auction

Additional Credit
Requirement

Bid Price   Collateral
Required
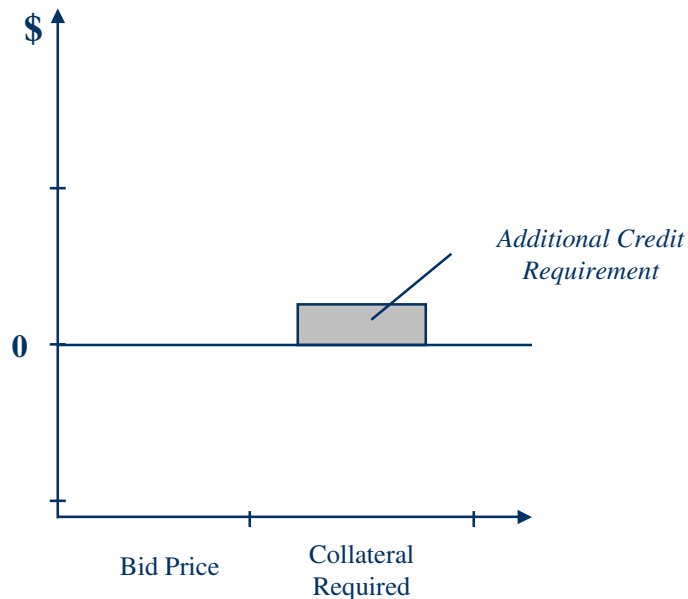
Requirements for Holding

Additional Credit
Requirement

Clear Price   Collateral
Required

A participant offering its CRRs at zero, will not have to post any bid price based credit. Thus, demanding it from other participant unnecessarily penalizes participants willing to bid at true value.