



# Memorandum

**To:** ISO Board of Governors and Western Energy Markets Governing Body

**From:** Eric Hildebrandt, Executive Director, Market Monitoring

**Date:** June 12, 2025

**Re:** Department of Market Monitoring report

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***This memorandum does not require ISO Board of Governors or WEM Governing Body action.***

## EXECUTIVE SUMMARY

This memo provides comments by the Department of Market Monitoring (DMM) on Management's extended day ahead market (EDAM) congestion revenue allocation proposal.<sup>1</sup> The current FERC-approved EDAM design would allocate congestion revenue to the balancing authority area where the transmission constraint creating the congestion is located. Management is proposing an alternative congestion rent allocation method to use on a transitional basis. The alternative method would allocate the congestion rent like the current FERC-approved EDAM design, except that rent associated with balanced self-schedules on long-term firm and network integration transmission service rights would be allocated to the balancing area where the energy is scheduled, rather than where the constraint is located.

Management's proposal is likely to create economic incentives for some inefficient self-scheduling of resources. While this will reduce the efficiency benefits from managing congestion over an expanded EDAM footprint relative to the currently approved design, DMM believes there would still be significant benefits from an expanded market relative to the current pre-EDAM market. The ISO has provided data showing there is reasonable hope that the potential for inefficient self-scheduling would be limited in the PacifiCorp balancing areas.

The ISO also proposes to seek to implement another change within the first year of EDAM operation that would extend the proposed congestion rent allocation to cleared balanced schedules that submitted price-based bids. This change is intended to reduce incentives to self-schedule and to allow users of network integration transmission service (including future potential EDAM participants) to receive parallel flow congestion revenues associated with economic schedules. However, DMM believes that such a change would distort bid prices and result in inefficient scheduling of a much wider range of resources submitting price-

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<sup>1</sup> *Extended Day-Ahead Market Congestion Revenue Allocation Final Proposal*, California ISO, June 6, 2025: <https://stakeholdercenter.caiso.com/InitiativeDocuments/FinalProposal-EDAMCongestionRevenueAllocation-June62025.pdf>

based bids. This change could also have significant impacts on holders of congestion revenue rights in the ISO system.

While DMM recognizes the importance of this issue to potential EDAM participants, DMM believes efforts to implement this additional change within the first year of EDAM should be abandoned in favor of shifting efforts toward reaching a more effective and complete solution, such as flow entitlements. A well-designed flow entitlement approach has the potential to provide a similarly valued allocation of congestion rent to economic schedules, but without the inefficiencies of linking cleared schedule quantities with the congestion rent allocation.

DMM views Management's proposal as an acceptable alternative transitional measure. However, DMM believes any commitment to extend this transitional approach to economically cleared schedules should be abandoned. DMM believes that the ISO and stakeholders should instead focus immediately on development of an approach that decouples congestion rent allocation from cleared schedules, such as flow entitlements.

## COMMENTS

DMM views Management's proposal as a reasonable alternative transitional measure to allocation of EDAM congestion revenues. While the proposal may create increased incentives to self-schedule that would reduce market efficiency benefits relative to the approved EDAM design, the implementation of EDAM with this allocation will still create market benefits relative to the current pre-EDAM market. The sub-sections below highlight some points for consideration when evaluating Management's proposed allocation.

### ***Self-scheduling issues***

As highlighted in detail during the May 2 Market Surveillance Committee (MSC) meeting, the rule changes included in the draft final proposal—and ultimately in Management's final proposal—may create economic incentives for significant inefficient self-scheduling of resources relative to the approved EDAM design. DMM previously commented that the initial straw proposal would also create incentives for self-scheduling.<sup>2</sup>

DMM initially envisioned that, in practice, self-scheduling incentives would be limited primarily to import and export schedules that were wheeling power through EDAM areas. However, based on ISO presentations and discussions at the MSC meeting, it appears the incentives to self-schedule may apply to a much broader set of resources, including resources of load serving entities in each area that utilize network integration transmission service.

In response to requests by DMM and other stakeholders, the ISO provided data on the distribution of firm rights holders in the PacifiCorp balancing areas. According to the ISO, about 88 percent of eligible rights—including about 95 percent of network integration transmission service—are held by PacifiCorp Merchant. Based on this data and public

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<sup>2</sup> *Comments on Extended Day-Ahead Market Congestion Revenue Allocation Issue Paper*, Department of Market Monitoring, April 7, 2025: <https://www.caiso.com/documents/dmm-comments-on-edam-congestion-revenue-allocation-mar-17-2025-issue-paper-apr-07-2025.pdf>

statements by PacifiCorp, the ISO believes the total amount of rights that would self-schedule in order to receive congestion rent would likely be limited. As the ISO states:

*PacifiCorp has publicly stated that the economic dispatch and commitment of resources that result from economic bidding in the market will create significant customer benefits. Additionally, PacifiCorp has stated that it believes the risk of congestion costs does not outweigh the benefits of economic bidding. With this context, it is assumed that PacifiCorp's market participation will not be driven solely by the ability to self-schedule the exercise of transmission rights to derive a congestion hedge.<sup>3</sup>*

DMM agrees these points provide some reassurance that self-scheduling for the purposes of parallel flow congestion hedging may be limited in the PacifiCorp balancing areas. However, such data and statements should not take the place of a more efficient market design that will ultimately extend across multiple balancing areas. DMM recommends the ISO work to address such self-scheduling incentives more broadly by decoupling congestion rent allocation from cleared schedule quantities.

### ***Opting in and out of allocation to avoid counterflow payment “claw backs”***

To be eligible for the proposed congestion rent allocation, holders of firm rights outside the ISO balancing area would be required to submit balanced self-schedules and a contract reference number. If the energy is not self-scheduled or a contract reference number is not submitted for an hour, the schedules would not receive a congestion rent allocation. After the local balancing area passes the allocation to the firm rights holder, the allocation will fully offset the congestion costs associated with binding constraints in other EDAM balancing areas for the firm rights holder.

In cases where scheduling of firm rights provide counterflow to ISO constraints, the rent allocation would actually be a charge that offsets the counterflow payments the schedule receives in the market. A firm rights holder could avoid this charge and keep their counterflow payments by simply not submitting a contract reference number for hours in which they will be net counterflow. Thus, firm rights holders will have an incentive to opt in to the allocation to avoid charges by submitting a contract reference number when they think they will create flows, but will have an incentive to opt out by not submitting a contract reference number when they think their schedules will create counterflows.

The ISO has clarified that rights holders can opt to not submit a contract reference number when they think schedules will create counterflows for which they may receive congestion payments, and that this will be allowable and expected under EDAM market rules. However, DMM notes that DMM would not view it as acceptable to utilize various types of circular schedules to receive such congestion payments while avoiding congestion charges. For example, this could involve submitting a contract reference number for one set of schedules in the congested direction, while also submitting an offsetting (or circular) set of schedules in the counterflow direction without a contract reference number.

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<sup>3</sup> *Extended Day-Ahead Market Congestion Revenue Allocation Revised Draft Final Proposal*, May 19, 2025, p 19: <https://stakeholdercenter.caiso.com/InitiativeDocuments/Revised-Draft-Final-Proposal-EDAM-Congestion-Revenue-Allocation-May-19-2025.pdf>

### ***Transitional nature and sunseting of the proposed allocation***

In response to earlier stakeholder comments and questions on whether the approach described in Management's proposal will sunset in three years or not, the ISO stated:

*The ISO and market participants will continue to work together, through stakeholder working groups, to evaluate and consider a spectrum of potential near-term enhancements and long-term congestion revenue allocation or congestion hedging mechanisms that could be considered after the launch of EDAM.<sup>4</sup>*

DMM understands this to mean that the proposal does not have an explicit sunset provision and that the proposed allocation will continue unless and until replaced by future design changes.

### ***Additional proposed changes within first year of EDAM***

Management's proposal does not provide the possibility that balanced economic schedules on network integration transmission service rights could receive congestion rent from parallel flows. This feature is consistent with the approved EDAM design but represents a change from the ISO's first straw proposal in this initiative. DMM understands that this design feature has raised concerns for some potential future EDAM entities.

To address this concern, the ISO proposes to implement another change within the first year of EDAM operation that would extend the proposed congestion rent allocation to cleared balanced schedules that submitted price-based bids. This additional change is also intended to reduce incentives to self-schedule and to allow users of network integration transmission service to receive parallel flow congestion revenues associated with economic schedules.

However, DMM believes that such a change would result in inefficient scheduling of a much wider range of resources submitting price-based bids. Even if resources do not self-schedule, the fact that resources receive a full or partial rebate of congestion costs if scheduled will distort bidding incentives. Resources receiving congestion rent rebates if scheduled will have an incentive to lower their bid prices to receive congestion rent rebates, which could have the effect of increasing congestion costs. This change could also have significant impacts on holders of congestion revenue rights in the ISO system.

### ***Recommended direction for longer-term approach***

DMM recognizes that the additional change the ISO has indicated it will pursue within the first year of EDAM is important from the perspective of potential EDAM participants with network integration transmission service rights. However, DMM believes efforts to approve and implement this additional change should be abandoned in favor of shifting efforts toward reaching a more effective and complete solution, such as flow entitlements.

A well-designed flow entitlement approach has potential to provide a similarly valued allocation of congestion rent to economic schedules, but without the inefficiencies of linking cleared schedule quantities with the congestion rent allocation. As noted in numerous filings and comments on this issue, the most efficient longer-term approach would be one that is

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<sup>4</sup> Revised Draft Final Proposal, May 19, 2025, p, 28.

decoupled from bidding and scheduling. For example, as highlighted by the MSC, long-term options may include flow entitlements and/or financial approaches.

Regardless of which approach is adopted initially, the ISO should closely assess the differences, keep stakeholders informed, and be prepared to develop other transitional and longer-term options. DMM will also monitor and report on the congestion rent allocation and scheduling within the EDAM. The additional data and experience from actual EDAM operations will help inform stakeholders for future design changes.