

ONTARIO ENERGY BOARD

IN THE MATTER OF sections 18 and 19 of the *Electricity Act*,
1998;

AND IN THE MATTER OF a Submission by the Independent
Electricity System Operator to the Ontario Energy Board for the
review of its proposed expenditure and revenue requirements
and the fees which it proposes to charge for the year 2010 in
connection with the IESO-controlled grid and IESO-
administered markets.

**IESO'S WRITTEN SUBMISSIONS IN SUPPORT
OF SETTLEMENT PROPOSAL
(March 30, 2010)**

March 26, 2010

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A. Overview

1. Further to the Board's Procedural Order No. 2, the purpose of these submissions are to:
 - (a) Submit for Board approval, the settlement proposal (the "Settlement Proposal") entered into between the IESO and intervenors who participated in the February 25, 2010 Settlement Conference; and
 - (b) Update the Board on the IESO's steps to address certain issues relating to congestion management settlement credit ("CMSC") payments identified by the Market Surveillance Panel (the "MSP") in its monitoring report released January 29, 2010.

B. The Settlement Proposal

2. The IESO filed its Fiscal 2010 Fees Submission for Review with the Board on November 2, 2009.
3. The Board issued an approved issues list (the "Issues List") on December 23, 2009, along with Procedural Order No. 1 directing, *inter alia*, that a Technical Conference be held on January 29, 2010.
4. Prior to the Technical Conference, Board staff and certain intervenors (AMPCO, VECC and OPG) delivered written questions to the IESO on matters relating to the Issues List.
5. A Technical Conference was held on January 29, 2010. In addition to the IESO, the Technical Conference was attended by Board staff, the Association of Major Power Consumers of Ontario ("AMPCO"), the Vulnerable Energy Consumers Coalition ("VECC"), Ontario Power Generation ("OPG") and The Society of Energy Professionals of Ontario (the "Society").

6. At the Technical Conference, panels of IESO representatives addressed the written questions submitted by Board staff and intervenors and answered other questions relating to the matters on the Issues List.

7. A Settlement Conference was held on February 25, 2010. In addition to the IESO, the Settlement Conference was attended by Board staff, AMPCO, Energy Probe Research Foundation ("Energy Probe") and VECC. Ms. Gail Morrison acted as facilitator at the Settlement Conference.

8. The IESO and the intervenors who attended the Settlement Conference agreed to a settlement on all of the issues on the Issues List. This settlement was recorded in the Settlement Proposal which was reviewed and approved by the intervenors who attended at the Settlement Conference. The Settlement Proposal was filed with the Board on March 2, 2010. A copy of the Settlement Proposal is attached hereto as Appendix "A".

9. The Settlement Proposal accords with Rule 32 of the Board's *Rules of Practice and Procedure* and the Board's *Settlement Conference Guidelines*. Specifically, the Settlement Proposal provides a direct and transparent link to the evidence in support of each of the settled issues.

10. The IESO, subject to any further questions from the Board, requests that the Settlement Proposal be approved.

C. Update on Steps to Address CMSC Payments

11. At the Technical Conference on January 29, 2010, Board staff submitted questions to the IESO arising from the MSP's January 2010 monitoring report, specifically the MSP's comments and recommendations regarding certain CMSC payments.

12. The IESO filed a written response to Board staff's questions on February 22, 2010 (revised and re-filed February 26, 2010). A copy of the IESO's written response is attached hereto as Appendix "B".

13. In its response, the IESO noted that CMSC payments, though not affecting the IESO's costs and fee submission, are an important component of electricity market design and are a matter that the IESO has addressed and is continuing to address through market evolution activities, including the development of proposed market rule amendments as required.

14. The IESO further stated in its response that the IESO was undertaking work to address the particular concern raised by the MSP regarding certain CMSC payments. Specifically, the IESO raised and discussed this concern with the MSP prior to the release of the MSP's January 2010 report, and the MSP's recommended solution — the limiting of replacement bids for exports and dispatchable loads which bid at negative prices — is in the process of being incorporated in a market rule amendment submission.

15. The following briefly summarizes past steps the IESO has taken to address CMSC payment issues and current steps the IESO is taking to address CMSC concerns raised by the MSP, including the IESO's proposed rule amendment to limit replacement bids for exports and dispatchable loads.

(a) Past Actions to address CMSC Issues

16. As stated in the IESO's written responses to Board staff's questions, the IESO has, in the past, addressed CMSC payment issues through the following steps:

- Limiting generator/import offers for the purpose of CMSC to \$0 (June 2003);

- Introducing dispatchable load “self-induced” CMSC clawback provisions (January 2004);
- Moving the market schedule from 12X ramp rate multiplier to a 3X (September 2007), and
- Transactional coding changes removing CMSC payments for certain causal events (November 2009).

Some of the foregoing changes were made as the result of discussions between the IESO and the MSP.

(b) Present Actions to address CMSC Issues

17. The IESO is currently addressing CMSC issues that were referred to in the MSP’s 2009 and 2010 monitoring reports:

Recommendation 3-2 (from January 2009 MSP Report)

18. In its January 2009 report, the MSP stated:

In an earlier report, the Panel encouraged the IESO to limit self-induced congestion management settlement credit (CMSC) payments to generators when they are unable to follow dispatch for safety, legal, regulatory or environmental reasons. The Panel further recommends that the IESO take similar action to limit CMSC payments where they are induced by the generator strategically raising its offer price to signal the ramping down of its generation.

19. The IESO’s stakeholder engagement working group (SE-84) was formed to consider this recommendation. This working group is composed of the IESO and approximately 20 market participants.¹

¹ All materials, related to this engagement including the current status of this initiative, are located at: http://www.ieso.ca/imoweb/consult/consult_se84.asp

20. The IESO is currently formulating a rule amendment (MR-00252) to limit self induced CMSC payments to generators in the circumstances identified by the MSP. Prior to posting the amendment submission for stakeholder review, the Technical Panel requested that the IESO re-draft the amendment submission to address certain concerns raised by generators.

21. Based on the Technical Panel's advice, the IESO met with generators in December 2009 and January 2010 to identify issues and potential solutions. The IESO's consultation with generators has proceeded well and a third meeting with generators will be scheduled shortly to discuss the IESO's recommendations prior to submitting the revised amendment submission to the Technical Panel in May 2010.

22. The IESO anticipates that this rule amendment will be submitted to the IESO board for approval in September, 2010.

Recommendation 3-4 (from Jan 2010 MSP report)

23. In its January 2010 monitoring report, the MSP stated:

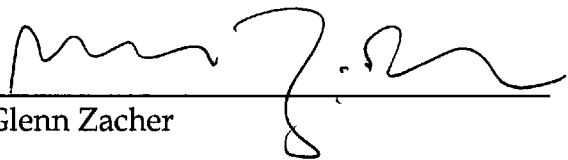
The Panel recommends that, for the purposes of calculating Congestion Management Settlement Credit (CMSC) payments, the IESO should revise its constrained on payment calculation using a replacement bid (such as \$0/MWh) when market participants (both exporters and dispatchable loads) bid at a negative price. This would create more consistent treatment with generators and importers that are constrained off.

24. The IESO agrees with the MSP's recommendation and is in the process of seeking to implement the recommendation through a rule amendment. The current planned timetable for the rule amendment is as follows:

- An efficiency analysis is being conducted to determine the appropriate value to use for a replacement bid. For example, "\$0" may not be the most efficient value; it may be that "\$2" or some other value is more appropriate. Unlike imports, exports are subject to additional transaction costs. These costs in conjunction with a bid floor may, for example, eliminate efficient trade during periods of regional or global surplus. The efficiency analysis will help ensure that no inefficient or unintended consequences result from the amendment.
- The proposed amendment and planned timelines will be identified and included on the Technical Panel's April 14, 2010 Forward Agenda (the Technical Panel's Forward Agenda is revised quarterly - January, April, July, October - and outlines the market rule amendments the IESO plans to bring to the Technical Panel within the next 12 months, including the proposed timetable for rule development and approval).
- The proposed amendment will be introduced at the May 11, 2010 Technical Panel meeting. If the efficiency analysis and any related assessments are complete, the IESO will introduce the amendment rationale and draft rule changes at this meeting. If such analysis is not complete, the IESO will submit the amendment rationale and will seek the Technical Panel's approval that the proposed amendment warrants further consideration and development; draft rule changes would then likely be introduced at the subsequent June 8 Technical Panel).
- Following the May 11 (or June 8) Technical Panel meeting, the proposed rule amendment will be posted for three weeks for stakeholder review and comment.

- Following the period for stakeholder review and comment, the proposed rule amendment (with any revisions resulting from stakeholder feedback) will likely be presented to the Technical Panel at the July 6 or August 17, 2010 Technical Panel meeting.
- The IESO's is targeting September 10, 2010 for IESO board approval of the rule amendment.

ALL OF WHICH IS RESPECTFULLY SUBMITTED



Glenn Zacher

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EB-2009-0377
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INDEPENDENT ELECTRICITY SYSTEM OPERATOR (IESO)
FISCAL YEAR 2010 FEES SUBMISSION FOR REVIEW
SETTLEMENT PROPOSAL
EB-2009-0377

This Settlement Proposal is filed with the Ontario Energy Board ("the OEB" or "Board") for consideration in the determination of the Independent Electricity System Operator ("the IESO") Fiscal Year 2010 Fees Submission for Review, EB-2009-0377 (the "IESO's 2010 Fees Submission"). A Settlement Conference was conducted on February 25, 2010 pursuant to Rule 31 of the OEB's *Rules of Practice and Procedure* (the "*Rules*") and the OEB's *Settlement Conference Guidelines*. This Settlement Proposal arises from the Settlement Conference and was prepared in accordance with Rule 32 of the Rules.

The following parties (the "Parties") participated in the Settlement Conference:

- The IESO;
- Association of Major Power Consumers in Ontario("AMPCO");
- Energy Probe Research Foundation (Energy Probe); and
- Vulnerable Energy Consumers Coalition ("VECC").

This Settlement Proposal addresses all issues on the Board-approved issues list (the "Issues List"), namely:

1. Operating Costs
2. Capital Spending
3. Methodology for Calculating Usage Fee
4. Smart Metering Entity
5. Reliability
6. Green Energy and Green Economy Act (GEGEA) Initiatives

The Parties accept the IESO's evidence on all of the issues and have agreed to a settlement on all of the issues.

OEB Staff is not party to this Settlement Proposal and therefore takes no position on any issue.

A Technical Conference was held on January 29, 2010 and Board Staff and intervenors examined panels of IESO witnesses on the matters contained in the Issues List; the Technical Conference was transcribed. There were no undertakings for the IESO from the Technical Conference.

At the Technical Conference, OEB Staff introduced and marked as an exhibit (TC.1) questions relating to the recent MSP Monitoring Report. Prior to the Settlement Conference, the IESO filed answers to Board Staff's questions stating, inter alia, that the IESO was developing a market rule amendment to address the MSP's specific recommendation relating to CMSC payments to exporters and dispatchable loads. The IESO agrees that it will continue to update OEB Staff and intervenors on the progress of this market rule amendment.

On the basis of the IESO's 2010 Fees Submission, pre-filed evidence, and additional evidence provided at the Technical Conference, the Parties agree to the approvals sought in the IESO's 2010 Fees Submission, including, the IESO's proposed 2010 revenue requirement, capital expenditure requirement, usage fee and application fee.

In accordance with Rule 32 of the Board's Rules and the *Board's Settlement Conference Guidelines*, this Settlement Proposal outlines the Parties' agreement and provides a direct and transparent link between each issue and the evidence in the record. The Parties further agree that the evidence is sufficient to support the Settlement Proposal and that the quality and detail of this supporting evidence will allow the Board to make findings on the issues.

IESO 2010 Revenue Requirement, Proposed Expenditures and Fees

The Parties agree to the IESO's 2010 proposed revenue requirement of \$122.8 million and proposed 2010 capital expenditures of \$21.6 million.

The Parties agree to the continuation of the \$1,000 application fee and proposed IESO usage fee of \$0.822/MWh commencing January 1, 2010 (to be charged in the manner provided in the IESO's 2010 Fees Submission).

The following general evidence, in addition to the specific evidence cited under the issues below, supports this agreement:

- Exhibit A, Tab 1, Schedule 1, IESO's 2010 Fees Submission
- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan
- Exhibit B, Tab 2, Schedule 1, Letter to Minister of Energy and Infrastructure dated October 01, 2009
- Exhibit TC.3, Letter from Minister of Energy and Infrastructure dated November 16, 2009
- Exhibit B, Tab 3, Schedule 1, Supplemental Financial Information
- Exhibit B, Tab 4, Schedule 1, Methodology for Calculating 2010 Usage Fee and Process for Rebating any Revenue Surplus
- Exhibit TC.2, Updated Financial Evidence
- Final Transcript for January 29, 2010 Technical Conference

1.0 Operating Cost

1.1 Are the IESO's projected OM&A Costs appropriate and reasonable?

The Parties accept that the evidence set out below supports the IESO's projected OM & A costs as being appropriate and reasonable:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 10-17, 20-27
- Exhibit B, Tab 3, Schedule 1, Supplemental Financial Information
- Exhibit TC.2, Updated Financial Evidence
- Exhibit TC.6, Answers by IESO to pre-filed Questions of OEB and VECC
- Final Transcript for January 29, 2010 Technical Conference, pages 11-19

1.2 Are the IESO's projected staff costs and strategy for setting compensation levels appropriate and reasonable?

The Parties accept that the evidence set out below supports the IESO's projected staff costs and strategy for setting compensation levels as being appropriate and reasonable:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, page 15
- Exhibit B, Tab 3, Schedule 1, Supplemental Financial Information, page 11
- Exhibit TC.2, Updated Financial Evidence
- Exhibit TC.5, Table of Average Wage Costs
- Exhibit TC.6, Answers by IESO to pre-filed Questions of OEB and VECC
- Exhibit TC.7, IESO Organization Pre-reorganization Chart
- Exhibit TC.8, Current IESO Organization Chart
- Final Transcript for January 29, 2010 Technical Conference, pages 20-33, 44-54

1.3 What are the financial consequences of the IESO's investments in ABCP on the IESO's operating costs and its 2010 revenue requirements and have these costs been appropriately incorporated in the 2010 fees submission?

1.4 Is the IESO's policy for treatment of ABCP investments going forward appropriate and reasonable?

With regards to Issues 1.3 and 1.4, the Parties accept that the evidence set out below confirms that: (i) the financial consequences of the IESO's investments in ABCP on the IESO's operating costs and its 2010 revenue requirements have been appropriately incorporated in the IESO's 2010 fees submission; and (ii) the IESO's policy for treatment of ABCP investments going forward is appropriate and reasonable:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 11 and 13
- Exhibit B, Tab 3, Schedule 1, Supplemental Financial Information, pages 2 and 3
- Exhibit B, Tab 6, Schedule 1, Asset Backed Commercial Paper
- Exhibit TC.6, Answers by IESO to pre-filed Questions of OEB and VECC
- Final Transcript for January 29, 2010 Technical Conference, pages 33-43

2.0 Capital Spending

2.1 Are the IESO's proposed 2010 capital expenditures on the enhanced day-ahead commitment (EDAC) project reasonable?

2.2 Is the EDAC project on budget and schedule?

With regards to Issues 2.1 and 2.2, the Parties accept that the evidence set out below confirms that: (i) the IESO's proposed 2010 capital expenditures on the enhanced day-ahead commitment (EDAC) project are reasonable; and (ii) the EDAC project is on budget and schedule:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 11, 16, 23 and 25
- Exhibit B, Tab 3, Schedule 1, Supplemental Financial Information, pages 16 and 17

- Exhibit B, Tab 5, Schedule 1, Status of Enhanced Day-Ahead Commitment Project
- Exhibit TC.9, Written Response to OEB pre-filed Question 17
- Final Transcript for January 29, 2010 Technical Conference, pages 54-62, 64-65

2.3 Are the IESO's proposed capital expenditures, other than EDAC, appropriate and reasonable?

The Parties accept that the evidence set out below supports the IESO's proposed capital expenditures, other than EDAC, as being appropriate and reasonable:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 16, 23-27
- Exhibit B, Tab 3, Schedule 1, Supplemental Financial Information. Pages 7-10
- Exhibit TC.2, Updated Financial Evidence
- Final Transcript for January 29, 2010 Technical Conference, pages 62-72

3.0 Methodology for Calculating Usage Fee

3.1 Are the methodologies for calculating the 2010 usage fee and process for rebating surpluses appropriate and reasonable?

The Parties accept that the evidence set out below supports the IESO's methodologies for calculating the 2010 usage fee and process for rebating surpluses as being appropriate and reasonable:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 10-13
- Exhibit B, Tab 4, Schedule 1, Methodology for Calculating 2010 Usage Fee and Process for Rebating any Revenue Surplus
- Exhibit B, Tab 3, Schedule 1, Page 1, Supplemental Financial Information
- Exhibit TC.2, Updated Financial Evidence
- Final Transcript for January 29, 2010 Technical Conference, pages 7, 10-11

3.2 Is the forecast Market Demand and methodology appropriate and have the impact of Conservation or Demand Management initiatives been suitably reflected?

The Parties accept that the evidence set out below confirms that the IESO's forecast Market Demand and methodology are appropriate and that the impact of Conservation and Demand Management initiatives have been suitably reflected:

- Final Transcript for January 29, 2010 Technical Conference, pages 6-11

4.0 Smart Metering Entity

4.1 Is the IESO's process for separating costs associated with its role as the Smart Metering Entity from costs associated with its role in operation of the provincial electricity grid and managing the wholesale electricity market reasonable?

4.2 Is the IESO's proposal and timing for recovery of its smart metering costs through a separate regulatory mechanism appropriate and reasonable?

4.3 Has the IESO in its role as the Smart Metering Entity, received Ontario Energy Board approval of a fee mechanism to recover Smart Metering Entity costs incurred, and has the Smart Metering Entity filed a separate fees submission to recover these costs?

With regards to Issues 4.1, 4.2, and 4.3, the Parties accept that the evidence set out below confirms that: (i) the IESO's process for separating costs associated with its role as the Smart Metering Entity from costs associated with its role in operation of the provincial electricity grid and managing the wholesale electricity market are reasonable; (ii) the IESO's proposal and timing for recovery of its smart metering costs through a separate regulatory mechanism is appropriate and reasonable; and (iii) the IESO is preparing applications, including an SME fee proposal, and intends to file these applications with the OEB by the end of the first quarter of 2010:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 9, 18-19, 28-30
- Final Transcript for January 29, 2010 Technical Conference, pages 74-76

5.0 Reliability

5.1 Are the IESO's proposed 2010 measures to address reliability appropriate and cost-effective?

The Parties accept that the evidence set out below supports the IESO's proposed 2010 measures to address reliability as being appropriate and cost-effective:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 1-2, 5, 23-27
- Final Transcript for January 29, 2010 Technical Conference, pages 77-92

6.0 Green Energy and Green Economy Act (GEGEA) Initiatives

6.1 Is the IESO proposal to address GEGEA initiatives appropriate and cost-effective?

The Parties accept that the evidence set out below supports the IESO's proposal to address GEGEA initiatives as being appropriate and cost-effective:

- Exhibit B, Tab 1, Schedule 1, 2010-2012 Business Plan, pages 1-9, 23-27
- Exhibit TC.7, IESO Organization Pre-reorganization Chart
- Exhibit TC.8, Current IESO Organization Chart
- Final Transcript for January 29, 2010 Technical Conference, pages 93-99

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**Questions for IESO at Technical Conference
 Relating to MSP Monitoring Report on the IESO-Administered Electricity
 Markets for the Period from May 2009 - October 2009
 (and previous MSP reports)**

Please find below, the IESO's written responses to the Board's questions concerning the recent MSP report.

It is the IESO's position that Congestion Management Settlement Credits (CMSC) are a component of electricity market design and are not relevant for the purposes of the IESO's current fees proceeding. CMSC payments do not impact on the IESO's costs except indirectly insofar as devoting additional work on the matter of CMSC payments or market evolution in general would require additional resources and costs.

CMSC is an important issue and, as detailed below, it has and is continuing to be addressed through market evolution activities including work with the IESO's Market Assessment Unit (MAU), which assists the MSP, and through the market rule amendment process. It is the IESO's position that these are the most appropriate forums in which to address this issue. That being said, the IESO has addressed Board staff's specific questions and would be pleased to meet with members of the Board to discuss this subject in more detail or other market design issues.

- 1) The MSP has released (or is about to release today) its most recent monitoring report on the IESO administered markets. This report highlights the significant levels of Congestion Management Settlement Credits or CMSC payments which total over \$1 billion since market opening. While CMSC payments are an integral part of the current Ontario market design, the panel reports that many of these are constrained off payments – i.e., payments for generators or importers not to generate or import. In many cases these payments appear to be inappropriate or unwarranted especially in the North West region of the province and particularly as concerns export and import transactions.

Are these issues being addressed in current IESO market evolution and market rule amendment activities? Please provide an update on what actions, if any, the IESO has been taking in this area and what actions it plans to take.

IESO Response

Background— CMSC payments are an integral part of the current Ontario electricity market design which is based on a uniform pricing/two schedule

system in contrast to a locational based pricing model. CMSC payments are paid for numerous reasons including, ramp rate limitations, transmission limitations, locational reserve requirements, and when facilities are dispatched out of merit for regulatory, safety and equipment related concerns.

In the context of the Ontario market design, CMSC payments are integrated with other fundamental components of the market and serve a number of purposes, including

- Pricing (A) — CMSC encourages generators to offer the full capacity of their generation resources notwithstanding transmission constraints that limit the quantity that would ordinarily be scheduled. Without CMSC, these same generators would likely change their offering behavior to offer only the quantities that they would reasonably expect to be scheduled. This would reduce generation supply offered into the market and would have an upward (or in the case of loads and exports downward) pressure on price.
- Pricing (B) — The IESO currently employs a 3X (formerly, 12X) ramp rate methodology. The effect of this is that price is not representative of the marginal cost of certain resources when they are ramping up or down. Constrained-on and off payments are accordingly made to those quick-ramping marginal suppliers (i.e., gas generators, some hydro) whose offer prices are not affected by the 3X ramp rate.
- Resource Funding — CMSC currently provides revenue streams necessary for certain resources to remain commercially viable. For instance, there are certain resources that are located in areas that are bounded by transmission constraints and that frequently experience oversupply/undersupply. The commercial viability of these resources could be jeopardized if they were frequently constrained off/on without any compensation or with reduced compensation. Any reduced compensation would likely need to be replaced through other mechanisms such as OPA contracts.
- Dispatch Compliance — CMSC payments encourage market participants to comply with IESO dispatch instructions. Without CMSC, generators that are constrained off due to transmission limitations would be incented to continue to run in order to receive (higher than cost) uniform market clearing prices. Absent CMSC, compliance with dispatch instructions would need to be regulated through a punitive enforcement system. CMSC therefore contributes to reliability and lower compliance costs.

Given this integration of CMSC with other components of the market, any elimination, reduction or other change in CMSC may have consequences in other areas. Similarly, elimination or reduction in the amount of CMSC paid out could save consumers CMSC-related costs, but add to consumer costs in other areas (e.g., MCP, OPA contract costs). For these reasons, changes to CMSC cannot be addressed in isolation from other fundamental aspects of the market.

It should be noted that the IESO agrees that a locational based pricing system is more efficient than the current uniform pricing/two schedule system and, as the market and sector evolve, the IESO will consider whether transitioning to a locational based pricing system is advisable (see below).

Actions taken and planned to address CMSC— While CMSC is an integral part of the Ontario market, the IESO continually and actively monitors the nature and extent of CMSC payments to ensure that they continue to be appropriate and warranted in light of changes to the market and the sector. The IESO does this through the MAU (which assists the MSP), consultation with the MSP itself, market evolution activities and ongoing stakeholder consultation. Where the IESO identifies problems or improvements that can be made (or problems or improvements are identified and brought to the IESO's attention by others), the IESO makes changes through the market rule amendment process or through changes in its market manuals and/or procedures.

Some of the changes the IESO has made since market opening to address CMSC include:

- Limiting generator/import offers for the purpose of CMSC to \$0 (June 2003);
- Introducing dispatchable load "self-induced" CMSC clawback provisions (January 2004);
- Moving the market schedule from 12X ramp rate multiplier to a 3X. (September 2007); and
- Transactional coding changes removing CMSC payments for certain causal events (November 2009).

Recently, the IESO proposed a generator "self-induced" CMSC claw back initiative. This is currently going through the stakeholder process prior to a planned Market Rule amendment submission. The purpose of this planned amendment is to eliminate CMSC payments currently being made to generators for operating restrictions within their control and not the result of transmission limitations or other intended CMSC casual events.

The MSP, through the IESO's discussions with the MAU is aware of this initiative.

With regard to Board staff's specific question as to whether the IESO is taking steps to address the issues referenced in the recent MSP report, the answer is yes - work is currently being undertaken. Prior to the release of the MSP's recent report, the IESO discussed with the MSP/MAU the specific matter of increasing CMSC payments to exporters and dispatchable loads who bid at negative prices and potential solutions. The frequency and magnitude of these payments in the Northwest has increased as load has declined and Ontario exports have increased. Some of the potential solutions discussed with the MSP/MAU are in the process of being incorporated in a rule amendment submission. Similar to the limitation placed on generators/imports, the IESO intends to bring forward rules that will limit the CMSC calculation for exports and dispatchable loads to \$0.

It should be noted, as discussed above, that CMSC is integrated with other aspects of the market and the proposed changes to CMSC payments to exporters/dispatchable loads may have potentially adverse consequences. These will need to be assessed in considering and formulating the rule amendment in order to ensure that the objective of reducing the magnitude of these specific CMSC payments does not trigger other substantial costs or unduly undermine market efficiency or reliability.

Market Evolution — More generally the IESO will be initiating longer term market evolution considerations during 2011 which, in light of recent changes to the sector, may include consideration of additional changes to CMSC, including constrained off limitations, locational pricing opportunities and other matters.

- 2) Related to the above question, the MSP report indicates that at the Minnesota intertie there are cases where the intertie is import-congested in the unconstrained sequence when in fact there is no actual power being imported. Please explain why this situation is arising and whether or not it is leading to significant costs being borne by Ontario ratepayers. Please also explain any plans or actions, if any, the IESO is taking in regards to the situation.

IESO Response

The above noted references in the MSP report require some background explanation and clarification.

The referenced section of the MSP report describes a condition where the economic offers from Minnesota exceed the transmission interface capability and thus create congestion in the uniform market schedule. Simultaneously the constrained scheduling system recognizes a constrained transmission interface in Ontario and limits actual flows to 0 MW. In these circumstances, the transmission rights (TR) market will pay TR rights holders (TR payouts) when there is congestion in the uniform market schedule regardless of the real-time flows from the constrained sequence. For example, a TR rights holder would be paid even though 0 MW actually flowed. This is how the TR market is designed to function and, in response to Board staff's specific question, this situation has no impact on Ontario ratepayers.

The TR market is a 'closed' design which is entirely funded by TR rights auction proceeds and "congestion rents", and it is designed so that these proceeds and rents are sufficient to fund TR payouts. Specifically, the market is designed so that over time the offset of TR auction proceeds/congestion rents and TR payouts maintains a rolling balance of approximately \$20 million. Over time, non-TR market participants (and ratepayers) are therefore not exposed to TR market costs. Similarly, the reference at p. 96 of the MSP report to "paying less rebate to Ontario consumers" is not a potential consequence of the current TR market design. As noted, the market is designed to maintain a rolling balance of \$20 million and to not rebate any surplus to Ontario consumers.

- 3) The MSP report indicates that at the Manitoba intertie there are significant cases of constrained-off imports Manitoba to Ontario resulting in CMSC payments to Manitoba Hydro totaling approximately \$80 million over the last 7 years — while Ontario has received no power in return. The report also indicates that over the same time frame Manitoba Hydro has been paid about \$3 million for constrained-on exports from Ontario to Manitoba. Please explain how these patterns of payments are arising and any actions or plans the IESO has in this regard.

IESO Response

The constrained-on and off payments referenced above are a result of congestion in Northwestern Ontario — specifically, oversupply that requires constraining-on dispatchable loads/exports or constraining-off generation/imports.

In the circumstances noted, and assuming the export limit on CMSC is \$0, constraining on exports at one cent is, in fact, cheaper for Ontario consumers than paying constrained off payments to generators or importers at an offer price of \$0. The IESO as indicated earlier is expecting to introduce rules limiting the export/dispatchable load CMSC calculation to \$0.

- 4) With reference to the MSP report of November 2008 to April 2009 (released July 31, 2009) Appendix 4A (pages 264-272): This appendix contains a list of recommendations that the MSP has made to the IESO. Please indicate whether the IESO responses therein are still current, and, if not please provide any more up-to-date information.

IESO Response

The IESO formally responds to all MSP recommendations, typically within 4-6 weeks of each report, and at the same time updates the responses to the previous recommendations. The IESO responses to the referenced recommendations are up to date.

Further, all recommendations are considered and, if accepted, prioritized along with all other IESO initiatives. Based on this prioritization and resource availability, the IESO then implements the recommendations.