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BY EMAIL AND COURIER

October 15, 2010

File No.: 101926.1007

Kirsten Walli
Board Secretary
Ontario Energy Board
PO Box 2319
2300 Yonge Street
Toronto, Ontario
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Dear Ms. Walli:

Re: HONI 2010/2011 Transmission Rate Case, EB-2010-0002

I enclose the Written Submissions of the IESO which are also being filed through RESS.

Yours truly,



for: Glenn Zacher

/sc
Encls.

cc: Registered Intervenors

TORONTO

MONTREAL

OTTAWA

CALGARY

VANCOUVER

NEWYORK

LONDON

SYDNEY

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998, S.O. 1998, c. 15, (Schedule B)*;

AND IN THE MATTER OF a review of an application filed by Hydro One Networks Inc. for an order or orders approving a transmission revenue requirement and rates and other charges for the transmission of electricity for 2011 and 2012.

**SUBMISSIONS OF THE INDEPENDENT
ELECTRICITY SYSTEM OPERATOR
(October 15, 2010)**

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AND TO: ALL REGISTERED INTERVENORS

A. EXPORT TRANSMISSION SYSTEM TARIFF

1. The Independent Electricity System Operator (IESO) recommends that the export transmission system (ETS) tariff of \$1.00/MWh be maintained through the current planned transformation of the Ontario electricity sector.

Exhibit H1, Tab 5, Schedule 2, p. 7

2. Specifically, the IESO recommends that the current tariff be maintained until the *Green Energy and Economy Act* (GEA) has been further implemented – and in particular, Ontario gains sufficient experience integrating large volumes of “intermittent” renewable resources (e.g., wind, solar energy) into the electricity system and addressing the operational, reliability and economic challenges that the addition of these resources introduces.

3. Once the electricity system has evolved and requisite operational experience has been gained, it may be appropriate to further study a new ETS tariff design. The IESO is not the appropriate entity to carry out a rate design study, but the IESO will participate and provide input on any continuing operability or reliability impacts.

a) Background

4. The ETS tariff of \$1.00/MWh was established by the Board in 1999; at the time, it was approved as an interim solution and compromise amongst numerous competing interests.

Exhibit H1, Tab 5, Schedule 2, p. 1

5. In Hydro One’s 2007/08 transmission rate application (EB-2006-0501), the Board approved a settlement under which it was agreed that the IESO would undertake a study of an appropriate ETS tariff design, while at the same time working towards reciprocal elimination of the tariff with Ontario’s neighbours.

Exhibit H1, Tab 5, Schedule 2, pp. 1-2; and Attachment 1, pp. 3-4

6. The IESO initiated a stakeholder engagement process (SE-78) in December 2008 for the purpose of carrying out the ETS tariff study and making a recommendation to the Board. This process provided interested parties with an opportunity to provide

input on the ETS tariff study, including on the study methodology and scope. Participants in SE-78 included Board staff and a number of the intervenors in the current proceeding (e.g., AMPCO, VECC, CCC, Bruce Power, Hydro Quebec, Brookfield, Energy Marketing).

Exhibit H1, Tab 5, Schedule 2, p. 2; and Attachment 1, pp. 3-4 and Appendices B and C

7. Based on initial stakeholder consultation, the IESO agreed to carry out a “qualitative” (i.e., reliability, operational and legal/regulatory impact) and “quantitative” (i.e., market impact) assessment of the three ETS tariff options identified in Hydro One’s 2007/08 rate case.

Exhibit H1, Tab 5, Schedule 2, pp. 2-4; and Attachment 1, pp. 4-6

8. Charles Rivers & Associates (CRA) was retained to carry out the quantitative analysis. This included assessing the impact of the ETS tariff options on export and wheel-through volumes, ETS tariff revenues, the Hourly Ontario Energy Price (HOEP), and market efficiency. IESO staff carried out the qualitative assessment, which included assessing potential legal/regulatory impediments and operational/reliability impacts.

Exhibit H1, Tab 5, Schedule 2, pp. 2-4; and Attachment 1, pp. 4-6

9. The IESO agreed that after carrying out the foregoing quantitative and qualitative assessments, it would make a recommendation on an appropriate ETS tariff based, in part, on the ETS tariff design principles articulated by Hydro One in its 2007/08 rate case (i.e., simplicity of implementation; consistency with rates in neighbouring markets; fairness and equitableness; and net Ontario benefit).

Exhibit H1, Tab 5, Schedule 2, pp. 2-4; and Attachment 1, pp. 4-6

10. In the spring of 2009, at the request of SE-78 stakeholders, the IESO, amended the scope of the study to include consideration of a fourth ETS tariff design option (i.e., Ontario unilateral elimination of the ETS tariff in all hours and off-peak hours only) and to consider the potential impact of the various ETS tariff options on the emerging issue of “surplus baseload generation” (SBG).

Exhibit H1, Tab 5, Schedule 2, p. 3; and Attachment 1, pp. 3-4
Oct 4, 2010 Transcript, Vol 9, pp. 53-55

11. SBG is a condition that occurs when Ontario's electricity production from baseload resources such as nuclear, wind, non-utility generators (NUGs) and must-run hydro facilities is greater than market demand. SBG conditions typically occur when there is low demand coincident with certain other conditions — i.e., spring freshet, high production from intermittent resources (e.g., wind, solar), low export demand in adjacent markets.

Exhibit H1, Tab 5, Schedule 2, Attachment 1, pp. 21-22

12. Following commencement of the ETS tariff study, Ontario began to experience unprecedented levels of SBG. For example, SBG hours for the months April to August 2009 totalled approximately 451 hours as compared to less than 100 hours for all of 2008.

Exhibit I, Tab 4, Schedule 16 (d), Revised October 6, 2010

b) The IESO's August 2009 Recommendation

13. The IESO filed its ETS tariff report and recommendation with the Board on August 29, 2009. While staff review and analysis indicated that Option 2 (i.e., a tariff based on average embedded network transmission cost) best satisfied the ETS tariff design principles, the IESO recommended maintaining the status quo (i.e., \$1/MWh) due to changes that had occurred since commencing the ETS tariff study — i.e., load deterioration due to declining economic conditions, projected increases in intermittent renewable resources due to the FIT program and increased occurrences of SBG.

Exhibit H1, Tab 5, Schedule 2, pp. 4-6; and Attachment 1, p. 9

14. In accordance with the ETS tariff study, the IESO observed that exports could help alleviate surplus conditions caused by low load periods and increased amounts of renewable baseload generation. On this basis, the IESO recommended against changing the ETS tariff to a higher amount that would place downward pressure on exports, especially, given the relatively small incremental economic benefits offered by Option 2. The IESO therefore recommended maintaining the current ETS tariff until system conditions had further evolved.

Exhibit H1, Tab 5, Schedule 2, pp. 1-2; and Attachment 1, pp. 3-4

c) ETS Tariff Panel Evidence

15. Darren Finkbeiner, Manager of Market Development for the IESO, confirmed that between commencement of the ETS tariff study in early 2009 and the IESO's recommendation in August, system conditions changed significantly. Specifically, Mr. Finkbeiner stated that:

- The CRA quantitative analysis had relied on a load forecast for 2010 of 159 TWh. By August 2009, the IESO's load forecast had materially dropped.
- SBG conditions had increased to a level "never seen before by the IESO". During the period April – August 2009, the IESO started to see the "first major wave of surplus conditions.
- The *Green Energy Act* received first reading in early 2009, however, it was not until later in the year that the IESO began to appreciate the magnitude of renewable resources that were likely to be added to the system pursuant to the OPA's FIT program. Mr. Finkbeiner stated that the IESO is currently anticipating that 6,000 or more MW of renewable resources will be added to the system over the next two to three years.

Exhibit H1, Tab 5, Schedule 2, Attachment 1, pp. 22
Oct 4, 2010 Transcript, Vol 9, pp. 34-35, 62-64

16. Mr. Finkbeiner stated that low load periods, coupled with the addition of increased amounts of OPA-contracted renewable generation, may continue or exacerbate SBG conditions. These surplus conditions – which confront operators with the choice of dispatching down/off nuclear units or "spilling" water/wind – have potentially adverse operational, reliability and economic consequences, for example:

- Nuclear units are designed to operate as baseload resources and are not designed to be frequently dispatched up/down and on/off. When surplus conditions require the IESO to dispatch nuclear units in this way, there are short and long-term adverse effects to these units.
- Similarly, some hydroelectric facilities that are governed by safety and other regulatory requirements concerning spilling, spill inspection, river levels and volume, etc.; these regulatory requirements impose operational limitations on how these facilities may be dispatched.
- There are potentially significant costs implications that arise from dispatching resources to meet surplus conditions. For example, if a nuclear unit is dispatched off to respond to surplus conditions, the unit may be unavailable for a period of days. This can result in the need to

replace the foregone nuclear generation with higher priced resources (e.g., gas or coal), not to mention cost implications that this can give rise to under OPA contracts (e.g., contractual payments owed to generators when they are curtailed). These factors can add to consumer cost through increases in HOEP, global adjustment and IESO-uplift charges, thereby eroding any consumer surplus benefits that might otherwise be realized by increasing the tariff.

Oct 4, 2010 Transcript, Vol 9, pp. 44-45, 70-71, 91-92

17. Surplus conditions can be mitigated by exports, which increase demand for surplus baseload generation and demand for other marginal resources (e.g., gas, hydro) that can be called upon by operators to more flexibly adapt to real-time surplus/demand variability. Conversely, by increasing the ETS tariff, export transactions become more expensive thereby dampening their ability to respond to and alleviate surplus conditions.

Oct 4, 2010 Transcript, Vol 9, pp. 45-46, 71-77

18. Mr. Finkbeiner further noted that the IESO is working on developing tools and processes to help better integrate increased intermittent resources on the system, but it will be sometime before the necessary processes/rule changes are made. The IESO also does not expect the first major wave of FIT wind resources to come on line until mid-way through 2012.

Oct 4, 2010 Transcript, Vol 9, pp. 42-43, 96

d) Summary of IESO Recommendation

19. Based on the foregoing, it is the IESO's view that it would prudent to maintain the current \$1.00/MWh ETS tariff until Ontario has integrated more intermittent renewable resources into the electricity system and the IESO has developed new tools/processes and has gained requisite experience operating the system under these dramatically transformed conditions.

20. Given the anticipated in-service dates for the first major tranche of FIT intermittent generation resources, the IESO recommends that the current ETS tariff be maintained at least until the spring of 2013.

B. HIGH FIVE PROPOSAL

21. The IESO takes no position on the merits of AMPCO's proposed new methodology for determining the Network service charge determinant. The IESO, however, was asked to review the implementation considerations, and provide an estimate of the timeframe and costs for implementing and administering the Network charges based on the proposed methodology.

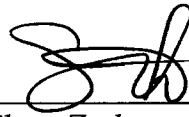
22. As earlier stated, it is not possible for the IESO to implement the necessary tools, market rule amendments and business process changes for a January 1, 2011 effective date.

July 20, 2010 Motion Hearing Transcript, Pages, 2, 14-15
Exhibit I, Tab 4, Schedule 63 (c), Page 30 of 30

23. Furthermore, the IESO noted that based on past experience in dealing with matters of this nature, more detailed review of the proposal will be necessary to ascertain the full extent of the implementation requirements and impacts; as well, in some cases further input from the Board may be necessary.

Exhibit H1, Tab 3, Schedule 1, Page 5-6

All of which is respectfully submitted, this 15th day of October, 2010.



for: Glenn Zacher,
Counsel for the IESO