EB-2012-0031

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sch.B, as amended;

AND IN THE MATTER OF an Application by Hydro One Networks Inc. for an Order or Orders approving just and reasonable rates and other service charges for the transmission of electricity, effective as of January 1, 2013 and January 1, 2014.

FINAL ARGUMENT OF THE SCHOOL ENERGY COALITION

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1 INTRODUCTION AND SUMMARY

1.1 *Introduction*

1.1.1 On May 28, 2012, Hydro One Networks Inc. ("HONI") filed an Application for transmission rates, effective January 1, 2013 and January 1, 2014. A settlement was reached among the parties on all issues with the exception of Issue 23.

1.1.2 The Independent Electricity System Operator ("IESO") was required by the Ontario Energy Board ("OEB") in its Decision in HONI's 2011-2012 transmission rate application (EB-2010-0002) to undertake a comprehensive Export Transmission Service ("ETS") rate study, which would identify a range of proposed ETS rates and the pros and cons associated with each. The Board ordered the IESO to consult with stakeholders on the terms of reference for the study. The study was to be filed in HONI's next transmission rate application. The IESO retained Charles River Associations ("CRA") to undertake the study and the results ("CRA Report") were filed by HONI.

1.1.3 In this proceeding, expert evidence was filed by Cliff Hamel of Navigant Economics on behalf of Association of Power Producers ("APPrO"), Elenchus Research Associates ("Elenchus") on behalf of Hydro Quebec Energy Marketing ("HQEM"). Evidence was filed by Marc-Andre Laurin, a senior trader at Brookfield Energy Marketing LP, on behalf of APPrO.

1.1.4 An oral hearing was held on February 25th and 26th, 2013.

1.1.5 This is the Final Argument of the School Energy Coalition ("SEC") on Issue 23.

1.1.6 The ratepayer groups who intervened in this proceeding have followed their normal practice of working together throughout the hearing to avoid duplication.

1.2 *General Principles and Position Summary*

1.2.1 The transmission system is different than the distribution system; customers are not differentiated by customer class and charged different rates for service. This principle recognizes that the transmission system is a shared asset, and the costs should be borne by all system users, no matter the purpose, path of travel or the final destination. This is the "postage stamp" method of transmission rate-setting.

1.2.2 This principle should only be deviated from in two circumstances. First, if different customer types are shown to have different transmission rights so that they do not have similar access to the system. This is similar to the fairness criteria set out in the CRA Report. Second, if it can demonstrated that there are *significant* system benefits that would warrant another rate-setting approach. These system benefits may include the

efficiency and simplicity criteria set out in the CRA Report.

1.2.3 In this proceeding, there is no evidentiary basis to conclude that the export customers are treated fundamentally different than domestic customers. Further, the evidence also does not demonstrate that there are significant system benefits from a reduction in the ETS rate. SEC submits that the Board should set the ETS rate at the Equivalent Average Network Charge. This would recognize that export like domestic customers utilize the transmission system in a similar manner. While export customers do use the system significantly less than domestic customers, that difference is recognized by the variable rate nature of transmission rates. Customers are only charged when they use the transmission system.

2 FAIRNESS

2.1 ***Fairness***

2.1.1 CRA evaluates fairness on two basis, i) ensuring customers pay like charges (horizontal fairness), and ii) ensuring customers who impose different costs and derive different benefits are treated in a way that reflects those different costs and benefits (vertical fairness).[1]

2.1.2 CRA evaluated each option with the view that domestic loads and exporters impose different costs on the Ontario transmission system and receive different benefits. Elenchus on behalf of HQEM took a similar view in its evidence. They recommended that exporters be considered a separate customer class and a cost-allocation study be undertaken to determine the ETS rate.[2] Mr. Hamel's evidence is that exporters do not create incremental costs on the transmission system, but he did recognize that there was a basis for them paying out of a sense of fairness.[3]

2.1.3 The distinction between domestic and export load has been overstated, particularly by Elenchus. While it is true that the transmission system was designed to service domestic and not export load, the only difference in transmission treatment is capacity restrictions which may cause congestion to arise, such that, export customers transactions can be limited.[4] Even then they are not full curtailed but reduced on a pro-rata basis. Besides this distinction, export transactions are considered 'firm' for the purposes of transmission service by the IESO. There is no significant difference between domestic and export transmission service as claimed by Elenchus.

2.1.4 While the risk of curtailment may be greater due to non-transmission considerations (generally generation issues), the same issue of intertie congestion does create exporter benefits as it leads to price differentials between neighbouring markets which can be turned to an advantage. Exports also have the ability to hedge against congestion risks by purchasing Transmission Rights through the IESO's auction process.

2.1.5 Elenchus' comparison with Ontario's natural gas cost allocation for interruptible service is flawed. As the IESO's witness Mr. Finkebeiner repeatedly pointed out during HQEM's cross-examination, the interuptability of export transactions is almost always due to generation not transmission domestic priority.[5] The ETS rate is a transmission not a generation rate. It is not comparable to a natural gas interruptible service.

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[1] *Export Transmission Service (ETS) Tariff Study*, Charles River Associates, Ex.H1/5/2/Appendix B [*CRA Report*]at p.39
[2] *Ontario Cost Allocation and Export Tariff Service*, Evidence Prepared by Elenchus Research Inc at pp.1,6
[3] *Hamel Evidence* at p.3, Tr.2:124-125
[4] Tr.3:9,106-10, Tr.2:143
[5] Tr.3:14

2.1.6 While the transmission system was not designed for the purposes of export customers, it should not be a reason for not paying for their usage now. A similar circumstance occurred in the RP-1999-0044 proceeding. In that preceding the Board had to determine how to allocate sunk costs of certain network transmission assets. The Board adopted a net over gross billing approach which recognized that all customers should pay for the services used not just those whom the assets were built for.[6] SEC submits the same principle applies in this proceeding. Export customers should be required to pay for their use of the transmission system, regardless of whom the assets were built for**.**

[6]Decision with Reasons, dated March 26, 2000 (RP-1999-0044) at paras 3.4.12-30

3 SYSTEM BENEFITS

3. Consistency with Neighboring Jurisdictions

3.1.1 SEC submits that the consistency with neighboring jurisdiction criteria favors the Equivalent Average Network Service Rate. As the CRA Report recognizes, the Equivalent Average Network Service Rate is consistent with the methodology used by most other jurisdictions.[7]

3.1.2 While some neighbouring jurisdictions have eliminated their export rate, it is on the basis of reciprocal arrangements, and not a unilateral decision by one jurisdiction.[8][9] The Board should not consider the agreements between those jurisdictions in determining the appropriate ETS rate for Ontario. While a bilateral agreement between the IESO and neighbouring jurisdictions may be preferable, it is not what is being proposed, nor would it seem to be a near-term possibility. The IESO in the past has sought reciprocal ETS rate agreements with the neighbouring jurisdictions, but has not received much interest and because of that this approach was not considered an as option for the study.[10]

3.2 *Simplicity*

3.2.1 As set out in CRA report, besides the tiered tariff options, all of the ETS rate options are easily implementable by the IESO.[11] Even the tiered rate options would only require a seemingly non-controversial IESO market rule amendments to implement differentiation of rates by time-period.[12]

3.3 *Efficiency*

3.3.1 CRA's calculation of efficiency is based on the total change in consumer and producer benefit (surplus), the Net Ontario Benefit for each of the five ETS rate scenarios modeled using their North American Electricity and Environment Model ("NEEM"), over a three time periods (2013, 2015 and 2017).[13] Additional runs were later undertaken based on feedback from participants that Ontario would likely not join the Western Climate Initiative (WCI) by 2015 and that no carbon pricing will be implemented.[14] SEC agrees with the IESO in this regard, the Board should only consider the non-WCI results.[15]

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[7] *CRA Report* at.p.42-46
[8] There are reciprocal agreements in place between NYISO and ISO New England, and MISO and PJM,
[9] *Evaluation of Export Tariff by Cliff W. Hamel* [*Hamel Evidence*] at p.11
[10] Ex. I/23/1/02 Staff 85(b)
[11] *CRA Report* at.p.42-46
[12] *CRA Report* at p.45-46
[13] *CRA Report* at p.3, 40
[14] *CRA Report*, Appendix B
[15] IESO Argument-in-Chief at p. 7 footnote 20

3.3.2 Below are a number of concerns with the IESO's position, and evidence presented by various parties.

3.3.3 ***IESO Analysis.*** The IESO in its Argument-in-Chief has presented its own approach to measuring efficiency. It has calculated the changes in surplus of the electricity commodity which measures efficiency from a generation perspective only.[16] Separately, it has reviewed transmission efficiency by measuring the intertie and regional efficiencies. The IESO measures these transmission efficiencies by looking primarily at the marginal cost of the system to exporters.[17] SEC has concerns with this approach.

3.3.4 There is no reason to separate transmission and generation efficiency and then use separate measures for each. Both are integral components of the Ontario power system that should be measured on the same basis. Further, in calculating the change in consumer surplus, the IESO removed ETS revenues but still included Uplift revenues. Uplift charges are similar in nature to the ETS rate. Both are primarily charges for non-commodity costs. The IESO has provides no rationale for removing the ETS revenue but not the Uplift revenue in its calculation of the total surplus of electricity commodity. By leaving Uplift revenue in the calculation, it overstates the benefits of increases exports.

3.3.5 ***Uplift Revenue.*** The CRA Report assumes that the Uplift rate will remain constant with a change in the ETS rate. SEC submits that this is unlikely since the Uplift rate is designed to collect revenues for costs that are generally not connected to the volume of exports.[18] If exports increase due to a reduction in the ETS rate, then the Uplift charges will likely decrease as a result since the total Uplift 'revenue requirement' would remain roughly the same. This leads to the benefits of increases exports to be overstated in the CRA Report.

3.3.6 ***Change in Producer Surplus.*** Mr. Hamel, drawing from the CRA Report, argues that since almost all the change in net income to generators resulting for a decrease in the ETS rate will flow to OPG's non-prescribed hydro-electric assets, in the long-run the benefit will accrue to consumers. This is because since OPG is owned by the province, an increase in net income will either pay down stranded debt or may benefit the fiscal balance of the province.[19]

3.3.7 While are it is true that OPG is owned by the province, it should have no bearing on the Board's determination of this issue. For the purposes of the Board, consumers – that is ratepayers – are distinct from taxpayer or general provincial residents. The

[16] IESO Argument-in-Chief at paras 22-26
[17] IESO Argument-in-Chief at paras 27-30
[18] Vol.2:186-189
[19] Tr.2:35-36, *CRA Report* at p.23

objectives for electricity under the *Ontario Energy Board Act* require the Board to protect the interests of consumers with respect to price, not to protect the interest of taxpayers.[20] Not all consumers are taxpayers, as an example schools do not pay taxes in Ontario. Further, the Board cannot with any precision draw the necessary line from increases in OPG net income to increases in consumer's pocket.

3.3.8 ***Effect on Trading.*** Mr. Laurin of Brookfield Energy Marketing LP provided evidence, which was also relied upon by Mr. Hamel, that the NEEM model used by CRA was flawed since it does not take into account actual trader behavior. SEC submits that while this is true, all models are imperfect.Modeling trader activity is virtually impossible and as Mr. Laurin admitted, individual traders will have different risk tolerances.[21]

3.3.9 ***Intertie Congestion Revenue.*** A significant portion of the oral hearing was dedicated to the issue of the allocation of the Intertie Congestion Revenue ("ICR"). CRA did not take a position on to whom changes in ICR would accrue to, but did agree that it is a net benefit to Ontario. Mr. Hamel took the view that it would accrue entirely to consumers.[22]

3.3.10 As pointed out during the cross-examination, it is not clear that all of the changes in ICR do accrue entirely to parties in Ontario. This is because the yearly total Intertie Congestion Rents have historically been less than the yearly total Intertie Congestion Payments made to holders of Transmission Rights.[2324] Since Transmission Rights can and are held by a variety of parties, including those outside of Ontario, some portion of the ICR will not flow to consumers (or even traders). With more than 80% of the of the Intertie Congestion Rents flowing to Transmission Rights holders, the Board should not assume that the change in ICR will accrue fully to the Net Benefit of Ontario.[25]

3.3.11 ***Surplus Baseload Generation.*** One of the expected benefits of the two-tiered scenarios was that it would increase exports during off-peak hours to help reduce Surplus Baseload Generation ("SGB"). However, the results of the CRA modeling of the various scenarios showed that this was not ultimately the case. All four scenarios showed no change in the amount of SGB.[26] This is because there is still a large separation in prices between the HOEP, the wholesale market price, and the neighbouring market price.[27]

3.3.12 ***Efficiency Calculations.*** Since it is likely, and due to the cost of the undertaking probably preferable, that the IESO not be required to do a full review the ETS rate before 2017, the Board should look not just to the impact on the change rates for the Test Years but also for subsequent years. While there are increases in the Total

[20] *Ontario Energy Board Act, 1998* at ss.1(2)(1)
[21] Tr.3:66,131
[22] *Hamel Evidence* at p.15

Ontario Net Benefit by implementing the Unilateral Elimination scenario, most of the benefits accrue in the Tear Years and then significantly decrease by 2017. They are likely to decrease even further if projected past 2017.

Summary of Change in Total Consumer Net Benefit by Scenario (C$2011 Millions)[28]			
Scenario	2013	2015	2017
Unilateral Elimination	*-$16.1*	*-$31.2*	*-$18.5*
Equivalent Average Network Charge	$24.1	$57.1	$24.9
Two-Tiered Scenario A ($5.80 on-peak/$0 off-peak)	$0.6	$7.5	$14.7
Two-Tiered Scenario B ($3.50 on-peak/$1.00 off-peak)	$10.3	$4.4	$13.4

Summary of Change in Total Ontario Net Benefit by Scenario (C$2011 Millions) [29]			
Scenario	2013	2015	2017
Unilateral Elimination	$17.6	$4.0	$6.1
Equivalent Average Network Charge	*-$22.8*	*-$0.6*	*-$10.5*
Two-Tiered Scenario A ($5.80 on-peak/$0 off-peak)	$4.1	$2	$7.3
Two-Tiered Scenario B ($3.50 on-peak/$1.00 off-peak)	$11.7	$2.9	$11.2

3.3.13 ***Summary.*** Ultimately, SEC submits that there are no efficiency reasons that would warrant departing from the general transmission rate-making principle. The change in the Total Net Ontario Benefit of a reduction in the ETS rate is not significant enough as compared to the overall cost of the electricity system. Further, as the CRA noted, no scenario has an effect on SGB. A change in the ETS rate will have no impact one of the Ontario'slargestelectricity system concerns.

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[23] Tr.2:111,175 Tr.3:27
[24] For the difference between Intertie Congestion Revenue (ICR) versus Intertie Congestion Rent see Ex. I/23/10.04 Staff #87
[25] *Monitoring Report on the IESO-Administered Electricity Market for the Period From November 2011-April 2012,* Market Surveillance Panel at p.155 (Exhibit K1.5)
[26] Vol.2.27
[27] Vol.2:27
[28] *CRA Report*, Table 12
[29] *CRA Report*, Table 13

4 SUMMARY

4.1 *Conclusion*

4.1.1 SEC submits that the Board should raise the ETS rate to the Equivalent Average Network Charge. This recognizes that the transmission system is a shared asset and export customers utilize the system as do domestic customers. The evidence in this proceeding does not warrant deviation from this principle. Export loads are treated similarly to domestic loads with respect to the transmission system and there are no significant system benefits that will occur from a change in the ETS rate.

4.2 *Costs*

4.2.1 The School Energy Coalition hereby requests that the Board order payment of our reasonably incurred costs in connection with our participation in this proceeding. It is submitted that the School Energy Coalition has participated responsibly in all aspects of the process, in a manner designed to assist the Board as efficiently as possible.

All of which is respectfully submitted.

Originally signed by

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