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May 23, 2008

BY COURIER (3 COPIES) AND EMAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
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Dear Ms. Walli:

Re: Pollution Probe – Written Comments on Staff Discussion Paper
EB-2007-0672 – RPP – Time-of-Use Pricing Consultation

We are writing to provide Pollution Probe's written comments to the *Staff Discussion Paper: Regulated Price Plan – Time-of-Use Prices: Design and Price Setting Issues* dated April 17, 2008. For your reference, Pollution Probe's comments are organized as responses to certain emphasized Board Staff summaries/questions in the discussion paper as detailed below.

Board Staff Summary/Question #1 at page 11:

Board [S]taff's initial view is that the three period design should be retained. The hourly variations in the cost of RPP supply referred to in section 2.1.1 continue to support this structure and, based on the results of the OSPP, the structure does not appear to be so complex from a consumer perspective as to require change. However, Board staff would be assisted by comments from stakeholders on whether and how a two-period pricing structure might better support load shifting and conservation.

Pollution Probe agrees that the three period rate structure should be retained. Ontario experiences sharp needle-like peaks in demand for four to six hours during a very limited number of hot summer days, and the cost of meeting these demands with peaking supply-side infrastructure is very high. Accordingly, Pollution Probe submits that a third critical peak-pricing period that provides a strong financial incentive for consumers to reduce their consumption during these highest demand hours is in the overall public interest.

Board Staff Summary/Question #2 at page 13:

Board [S]taff's initial view is that seasonal variations may remain appropriate, but that there is merit in revisting the issue. Board staff would be assisted by comments from stakeholders on whether seasonal variations should be retained and, if so, whether the seasonal variations should be retained in their current form or whether they should be adjusted such that the differences between the summer and winter pricing structures are reduced.

In short, Pollution Probe agrees that seasonal variations are appropriate in general since they permit rates to better reflect the costs of providing electricity supply.

Board Staff Summary/Question #3 at page 15:

Board staff's initial view is that critical peak pricing options – whether CPP or CPR – should be developed, and mandated for all consumers, only after consumers have greater experience with TOU pricing. Atlernatively, consideration could be given to providing for critical peak pricing to be offered initially at the discretion of the distributor rather than being mandated for all consumers. Board staff would be assisted by input from stakeholders in relation to critical peak pricing generally, and to the manner and timing of implementation.

Pollution Probe agrees that critical peak pricing ("CPP") should ultimately be mandatory for at least all of the consumers in southern Ontario. However, Pollution Probe also agrees that CPP needs to be skillfully implemented in order to ensure that its rationale is widely understood and supported by the general public. In addition, Pollution Probe believes that some (but not all) of Ontario's electric utilities already have the ability to successfully implement CPP now, and they should implement CPP as soon as possible. Pollution Probe also submits that CPP is most urgently needed in the transmission constrained regions of the province (e.g. Toronto, Mississauga, Northern York Region, and the Kitchener-Waterloo-Cambridge and Guelph area), and it should be implemented on a priority basis in these regions.

Finally, Pollution Probe submits that it is important to note that a local CPP programme provides benefits to *all* of Ontario's electricity consumers similar to the OPA's demand response programmes (e.g. reduced need for peaking electricity generation and transmission infrastructure as well as lower peak hour commodity costs).

Pollution Probe thus submits that that the OPA should pay LDCs for each incremental MW of demand reduction that their CPP programmes provide in order to encourage Ontario's finest electric utilities to voluntarily develop and implement innovative and effective CPP programmes as soon as practically possible. Furthermore, Pollution Probe specifically submits that the OPA should pay the LDCs the same price for CPP demand reductions that it pays large electricity consumers and aggregators for demand reductions pursuant to its DR3 programme.

Board Staff Summary/Question #4 at pages 18/19:

Board [S]taff suggests that the threshold question for revising the TOU price setting methodology to reduce price convergence among the TOU pricing periods is whether the hours for each price period should be adjusted or whether the principle of supply cost recovery within each TOU pricing period should be relaxed.

If hours are to be adjusted, should they be adjusted to restore the 1:2:3 ratio in the original design?

If the principle of supply cost recovery within each TOU pricing period is to be relaxed, then Board staff notes that the following additional issues may arise:

- *Should the Board focus on maintaining the 1:2:3 ratio and, as a result, recover supply costs across more than one TOU period if needed?*
- *Should the Mid-peak price be adjusted, perhaps closer to the midpoint between the Off-peak and On-peak prices? For example, by basing the Mid-peak price on the "average" RPP price?*
- *Should the range of Off-peak to On-peak prices be "stretched", perhaps by including forecasts or estimates of segmented uplift costs in the price setting process?*
- *Should multi-period cost of supply recovery be examined to provide more flexibility in setting prices? Should a reduction in the cost recovery period to six months be considered for consistenency with the frequency of price changes?*
- *Assuming that a price ratio methodology is retained by the Board, should the Board consider price ratios as a variable, changing from one RPP period to the next to reflect changes in the policy priorities and/or cost recovery concerns?*
- *Should the Board adopt an "avoided incremental cost of supply" methodology for On-peak prices and then adjust Mid-peak and Off-peak prices to recover total supply costs, regardless of the resulting price ratios?*

As the Board is aware, it has a broad public interest mandate with respect to electricity due to section 1(1) of the *Ontario Energy Board Act, 1998*.[1] Pollution Probe thus submits that the Board's primary objective, at least with respect to rate design, should be to establish prices that will ensure that consumers' electricity service needs are met at the lowest possible total ***societal*** cost ***including externalities***. In a practical sense, this means that prices would ideally allow consumers to do much of they want to do (such as being able to have a hot shower or a cold refreshment), but the price must reflect the realities of the ***entire*** cost of that consumption.

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[1] According to s. 1(1) of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sched. B:
The Board, in carrying out its responsibilities under this or any other Act in relation to electricity, shall be guided by the following objectives:

1. To protect the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service.
2. To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.

This reality in turn requires that electricity prices be based, to the fullest extent practical, on the ***marginal*** cost of supply ***including externalities***. As the Board knows, these marginal costs vary by season and by time of day, and the greatest disparity between electricity prices and marginal costs occurs during peak demand hours. In fact, according to one study, the cost of supplying electricity during the top 88 demand hours of the year is approximately ***16 times greater*** than the average residential price of electricity.[2]

Pollution Probe thus submits that the link between a utility's costs on an annual accounting basis and the marginal costs of electricity supply can be very weak. As a result, while a utility's costs on an annual accounting basis are essential for establishing a utility's overall annual revenue requirement, they are not a rational foundation for rate design.

Pollution Probe accordingly submits that, to promote overall economic efficiency in accordance with the Board's mandate, the Board should instead adopt an "avoided incremental cost of supply" methodology for On-peak prices. Pollution Probe further submits that the Board should then adjust Mid-peak and Off-peak prices to appropriately recover total supply costs. Pollution Probe submits that this proposed approach is in the best overall interests of all consumers since it will minimize average electricity rates and average electricity bills over time and the long-term.

Conclusion

We trust these comments have been of assistance to the Board, and please do not hesitate to contact the undersigned if you have any further questions or clarifications.

Yours truly,

Basil Alexander

BA/ba

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[2] Ontario Clean Air Alliance Research Inc., *Tax Shift: Eliminating Subsidies and Moving to Full Cost Electricity Pricing*, dated March 3, 2008, at pg. 11. Available online at http://www.cleanairalliance.org/files/active/0/taxshift.pdf.