Delivered by email: (to boardsec@ontarioenergyboard.com)

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
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2300 Yonge Street, Suite 2700
Toronto, Ontario M4P 1E4

Dear Ms. Walli:

Re: Consultation on the Effectivenss of Part II of the Energy Consumer Protection Act, 2010
Board File Number EB-2010-0245
General comments and comments on questions posed in OEB's letter of October 23, 2014

I am writing to provide general comments on the ECPA and related questions posed by the OEB in its October 23, 2014 letter.

I have worked in the Ontario energy industry for twenty-seven years and have a background in power generation, energy management, industrial natural gas utilization, energy marketing and energy consulting. I have also been an expert witness in OEB proceedings and in other legal proceedings. I currently work in the Ontario energy industry as a consultant. My employer does not represent residential consumers and so is not participating in this process. I am participating because I have the required knowledge and expertise and also a strong sense of social justice and interest in leveling playing fields that are not level. Ontario energy retailing – particularly for smaller consumers – is a playing field tilted strongly in retailers' favour.

While the Ontario natural gas retailing market has its warts, in this submission I will focus on Ontario electricity retailing aimed at smaller consumers.

In 2010, my ECPA participation included submitting comments to the Ontario Environmental Registry (EBR-0110-8556) and participating in the OEB's initial ECPA consultations. Most recently, in April 2014 I had an op-ed piece published in the Hamilton Spectator that looked at Ontario natural gas and electricity retailing.

Central premise

A review of Part II amounts to checking in on and optimizing the Act itself. The problem is that doing so is like perfecting a life jacket made of cement – the process may make sense in a very narrow quality sense but the product is ultimately very bad for the consumer. The prime question is "Why do we have at all an electricity retailing market for Ontario's smaller consumers ?"

Summary of my comments

1. The Ontario retail electricity market suffers from an asymmetry of information and so is dominated by unsavoury sellers and gullible buyers.
2. The Global Adjustment or GA – paid for by customers on regulated rates and those on retail contracts – already provides protection against varying spot prices.
3. Ontario retail electricity contracts duplicate what is already being done by the GA, causing consumers to effectively speculate on the spot market price of electricity. These contracts are therefore very unnecessary.

4. The extreme profit margins embedded in retail electricity contracts virtually guarantee a homeowner will incur an added cost. This cost can be $ 200 or more per year.
5. If we must improve the cement life jacket, side-by-side bill comparisons should be proactively audited and verification scripts should be modified such that the retailer clearly identifies for the customer the option costs, the higher cost option and magnitude of the differential.

(My full comments follow.)

The Market for Lemons

In 1967, American economist George Akerlof wrote the paper The Market for Lemons: Quality Uncertainty and the Market Mechanism. His paper was published in 1970 and in 2001 led to him being the co-winner of a Nobel Prize in Economics.

In his book The Signal and Noise: Why So Many Predictions Fail – but Some Don't, famed forecaster Nate Silver described the main idea behind The Market for Lemons (paraphrasing):

> *"a market characterized by asymmetry of information sees a reduction in the quality of goods and becomes dominated by crooked sellers and gullible or desperate buyers"*

As well, in his paper Akerloff noted that:

> *"The cost of dishonesty, therefore, lies not only in the amount by which the purchaser is cheated; the cost must also include the loss incurred by driving legitimate business out of existence".*

These thoughts unfortunately but neatly describe much of the Ontario retail electricity market – particularly for smaller consumers.

The Global Adjustment

The Global Adjustment ("GA") is a market mechanism and charge that is paid by all consumers, whether they are on the Regulated Price Plan or served by an electricity retailer. One problem is that in the former case, the GA is buried.

The GA primarily pays for the above-market (contract price less spot market price) costs related to generation supply arrangements entered into by the Ontario government and its agencies. These arrangements are in many cases very similar to or behave like what occurs when individuals sign retail electricity contracts.

Coverage from non-market supply and other dynamics

The purpose of hedging or entering into a fixed-price arrangement is to make one's price or cost predictable, i.e. to make one's budget as stable as possible.

Non-market (contracted and prescribed) supply at prices that are fixed or behave much like fixed prices provide protection or coverage against varying electricity spot prices. Up until April 2013, Regulated Price Plan ("RPP") Reports issued by the OEB contained references to the proportions of RPP energy coming from non-market and market based generation sources. The April 2013 report stated that for the period of May 2013 – April 2014, 91% of RPP energy would come from non-market (contracted and prescribed rates) sources and 9% from market-based sources. Put another way, 91% of RPP supply was paid via the spot market plus GA and 9% by the spot market only.

Since May 2014, the quantity of non-market based supply has increased, mainly due to wind and solar contracts that have been and continue to be added to the province's supply portfolio. Also, a significant step increase in the quantity and RPP percentage of non-market based prescribed-rate supply is likely to materialize – in the form of providing Ontario Power Generation with fixed pricing on output from its currently-unregulated hydraulic (hydro) generating stations.

There are other dynamics involved but the last that bears consideration is one that serves to increase the effective GA Class B coverage provided by non-market supply. In January 2011, the previously-single class of GA customers was split into two Classes – Class A (very large consumers) and Class B (the remainder, including residential consumers). The allocation of GA costs between the two group changed, with Class B thereafter paying a higher share of costs than it would otherwise. In 2014, the transfer of GA costs (relative to what they would have been had no change occurred) from Class A to Class B will be in the order of $ 500 million while in 2015 it could be in the order of $ 800 million. This reallocation of GA costs effectively shifts a portion of the total Ontario non-market supply to the GA Class B.

In total, smaller Ontario electricity consumers already have total coverage from GA-related supply arrangements in the order of 100% of their consumption. This offsets their consumption and so they have very little or no remaining exposure to variations in spot market electricity prices. Signing a typical retail electricity contract increases a consumer's fixed-price coverage to 200%. Rather than making a homeowner's electricity budget more stable, the exact opposite occurs as the consumer's budget becomes highly unstable – due to the homeowner's excess coverage that causes them to effectively speculate on the spot market price of electricity.

Retail electricity contracts that fix prices for residential and other small Ontario electricity consumers are therefore unnecessary.

Financial impact of signing a retail electricity contract

The vast majority of Ontario residential electricity contracts are for 100% of a customer's consumption. In the absence of the GA and its underlying non-market supply arrangements and resulting coverage, a fixed price contract might make sense for an extremely risk-adverse homeowner.

However with 100% coverage already provided by the GA, signing a retail contract results in the now consumer speculating on the price of electricity -- an activity recommended only for those seeking to do so and that understand what they're doing.

The problem with the speculation is that Ontario electricity retailers are typically seeking a gross profit of $ 200 per year on a contract; for the average home, this works out to 2 cents/kWh. In a falling electricity spot market, the additional cost will then exceed $ 200 per year. In a rising market, this additional cost will decrease but has very little likelihood – especially in the near term – of becoming a benefit.

It's no surprise then that when I'm asked whether or not one should sign a residential electricity contract, I explain the market coverage one already has and offer the advice to stick that $ 200 per year in one's "energy price risk mattress".

In my opinion, most unfortunate in all of this is that those likely to sign a retail electricity contract are often those who can least afford the virtually-guaranteed additional cost.

Improving the cement life jacket

The OEB states that 6% or roughly 300,000 of Ontario's 4.9 million residential and small business consumers are currently in retail electricity contracts. Arguably, that number should be zero; certainly none of these customers should be renewing a contract nor should new customers be entering into new contracts.

In 2013, the Ontario New Democratic Party introduced a private member's bill (Bill 182) that would have outlawed renewed or new contracts. Unfortunately, this bill died with the call of the election earlier this year. In the absence of another such bill, the only hope for reducing the financial damage done by most retail electricity contracts is that renewing or prospective consumers will not re-sign or sign contracts.

It's not at all realistic for most consumers to understand the market coverage provided by the GA and resulting inappropriateness of signing a retail electricity contract. The last line of defence against signing a contract is therefore the side-by-side bill comparison. If the retailer honestly presents the cost of their option – including the forecast GA – and the almost-inevitable added cost of the retail option registers with the homeowner, then the homeowner will not sign the renewal or new retail contract.

There are ways for retailers to dishonestly present the cost of their option and so that possibility warrants additional investigation – through a proactive audit process (if one doesn't already exist), rather than simply reacting quite narrowly to specific, individual complaints. As for the likely added cost of a retail offer registering with a customer, retailers should be required at the verification stage to clearly restate to customers the costs of the retailer and regulated commodity options, identify which one has a higher cost and by how much.

This completes my comments. I hope to and if able look forward to participating in the stakeholder forum scheduled for December 8 and 9.

Yours truly,

Bruce Sharp, P. Eng.