HQEM-APPRO INTERROGATORY 14

Issue 2.1: Is the IESO's proposal to eliminate the OPA Usage Fee and to charge the proposed single IESO Usage Fee to all market participants (domestic and exporter customers) appropriate?

2-HQEM-APPrO-IR14

INTERROGATORY

Reference: Exhibit B, Tab 1, Schedule 1, page 11, lines 2-11

(i) Can Elenchus clarify what is meant by "somewhat non-standard"?

(ii) If the revenue-to-cost ratios calculated may not be as indicative of a true causal relationship as can be achieved in the typical utility cost model, why it is appropriate to use a zone of reasonableness that was linked to a typical utility cost model?

(iii) Can Elenchus clarify how it was determined that the best indicator available for allocating costs was that which was a manner consistent with the IESO's existing MWh based Usage fee?

(iv) Can Elenchus confirm what the scope of work was as described in its engagement letter with the IESO? Was exploring alternate fee designs part of the scope? Please provide all correspondence on this issue with the IESO.

RESPONSE

(i) The words "somewhat non-standard" appear in the Elenchus Report at page 11, line 6. The words "this approach" in the sentence refer to the approach outlined in the preceding paragraphs, page 10, line 1 to page 11, line 5. The essence of the observation that the methodology that has been adopted is "somewhat non-standard" appears at page 10, lines 4-8: "In conducting this work, Elenchus has observed that the IESO's costs that are recovered through its Usage Fee consist largely of costs that would be treated as operational overhead or administrative and general (A&G) costs in the cost allocation models that are typically used by regulated electric utilities for their rate setting processes." The point being made is that the nature of the IESO's costs is quite different from the bulk of the costs of an electricity transmitter, an electricity distributor or an integrated electric utility. For example, the causal relationship between the capacity-

related costs of a transmission line and customer demand is far more obvious than the causal relationship between the essentially administrative costs incurred by the IESO and the use that is made of the IESO-administered market by customer classes or individual customers. In the absence of a physical cost causality driver equivalent to demand (i.e., kW demand "causes" the need for capacity) or energy (i.e., kWh "causes" the need for energy), the allocators rely much more heavily on assigning costs in an equitable manner than through a physical or engineering relationship. The absence of engineering underpinnings to the causal relationship is the primary basis of the comment by Elenchus that the model is "somewhat non-standard". Additional non-standard features include the absence of a rate base and cost of capital in the IESO's revenue requirement and the absence of non-trivial customer related costs such as customer service, customer meters, etc.

(ii) Elenchus has not asserted that "it is appropriate to use a zone of reasonableness that was linked to a typical utility cost model." The Elenchus evidence states only that "if the OEB were to adopt an R/C ratio range of 80% to 120% for the IESO's usage fee, it would follow that …" (page 15, lines 16-17) In the absence of an OEB approved zone of reasonableness (revenue-to-cost ratio range) for the IESO, Elenchus used the most common OEB approved range for regulated electricity entities for purposes of illustrating the methodology that Elenchus considers appropriate for making a determination about customer classification (one or two classes) based on allocated costs. Zones of reasonableness are generally a matter of the judgment of regulators as there is no generally accepted quantitative methodology for determining an appropriate zone of reasonableness. The selection of an appropriate R/C ratio range is a matter that is appropriately addressed as part of rate design, not cost allocation.

(iii) As Appendix A to the Elenchus evidence shows, a variety of allocators are used in the model developed by Elenchus. One of the allocators used is TWh, which is used for costs for which a volumetric allocator appeared appropriate. There are no IESO costs that appear to be "caused" by demand, as would be common for a transmission company or distributor. Energy (TWh) appears to be a more appropriate volumetric allocator than a demand-related allocator such as TW.

(iv) The scope of work is described in the attached quotation memo. Elenchus confirms that in its view, the scope of work for the filed evidence was consistent with the four tasks as set out in the memorandum dated 24 January 2015 and provided as Attachment 1 to this exhibit. Exploring alternate fee designs was not part of the scope. The rate design matters considered were limited to the first task: "Assess the consistency of the current IESO and OPA fees." Elenchus did not send or receive any correspondence with the IESO on the issue of alternate fee designs.