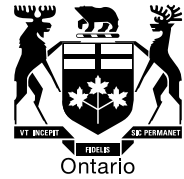


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**BY EMAIL**

July 27, 2017

Ontario Energy Board  
P.O. Box 2319  
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2300 Yonge Street  
Toronto ON M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

**Re: OEB Staff Further Submission on Draft Issues List.  
Independent Electricity System Operator (IESO) Application for Approval of  
2017 Revenue Requirement, Expenditures and Fees  
OEB File Number: EB-2017-0150**

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Pursuant to Procedural Order No. 2, please find attached OEB staff's further submission on the draft issues list prepared by the IESO in the above referenced proceeding.

Yours truly,

*Original Signed By*

Michael Lesychyn  
Project Advisor, Supply and Infrastructure

cc: Parties to EB-2017-0150



# **ONTARIO ENERGY BOARD**

## **OEB Staff Further Submission on Draft Issues List**

**Independent Electricity System Operator's Application for the Approval of  
2017 Expenditures, Revenue Requirement and Fees**

**EB-2017-0150**

**July 27 , 2017**

## Introduction

In Procedural Order No. 2, the Ontario Energy Board (OEB) invited further submissions on the issues list, noting: “Of particular interest is the issue raised by the Association of Power Producers of Ontario (APPrO) on the Wholesale Market Service Charge and the issues on the IESO’s Market Renewal Program raised by Energy Probe and the Vulnerable Energy Consumers Coalition (VECC).”

For the reasons below, OEB staff disagrees with the additions to the issues list proposed by APPrO, and agrees with some but not all of the suggestions made by Energy Probe and VECC.

### **A. OEB staff comments on APPrO’s proposed additions to the issues list**

In its submission dated June 30, 2017, APPrO argued that “an issue in this proceeding should include a review of the terms and conditions of IESO programs, including their cost. These amounts are currently collected by distributors from customers as part of the Wholesale Market Service Charge (**‘WMSC’**).” Specifically, APPrO urged the following additions to the issues list:

1. What are the amounts paid by customers for IESO programs?
2. Should these amounts be categorized as a separate IESO fee?
3. Are the terms and conditions of IESO programs, including their cost, appropriate?

APPrO explained that, although it currently does not propose to challenge the terms and conditions of IESO programs, including the cost, “the public interest is served by having these terms and conditions subject to public oversight,” and should therefore be reviewed “as part of the OEB’s review of IESO fees paid by customers.”

There are two prongs to APPrO’s argument. The first is that the recovery of program costs amounts to “fees” as that term is used in s. 25.1 of the *Electricity Act, 1998*. The second is that reviewing such costs in the context of a fees application would be consistent with the principle of “open and transparent governance in the electricity sector”.

The IESO replied on July 10, 2017. The IESO objects to APPrO’s proposed additions to the issues list. The IESO argues that the costs in question do not relate to the IESO’s costs of operating its business: “These charges are used to pay Market Participants such as generators and loads for services they provide that are necessary to ensure the reliable operation of the electricity system. These are not fees for IESO services rendered such as the registration fees for electricity supply and capacity procurements, the application fee for the FIT program, or the IESO market participation application

fee.” The IESO also disputes that the costs are passed on to consumers without oversight. The IESO argues that the OEB has oversight of the costs, including through the setting of the wholesale market service rate, the IESO’s licence, and the OEB’s role in the Market Rules review process.

In OEB staff’s view, there is no merit to APPrO’s argument. The starting point for the analysis should be the words of the statute that provides the OEB with jurisdiction to approve the IESO’s fees: the *Electricity Act, 1998*. Yet APPrO makes no mention of the definition of “fees” in s. 2(1):

“fees” means, with respect to the IESO, amounts charged by the IESO, or by a predecessor within the meaning of section 4, to recover its costs of operations. [Emphasis added.]

This definition can be contrasted with the definition of “charges”:

“charges” means, with respect to the IESO, amounts charged by the IESO, or by a predecessor within the meaning of section 4, to recover amounts paid or payable by the IESO or the predecessor to another person with respect to electricity. [Emphasis added.]

As can be seen, the difference between fees and charges is that fees are to recover the IESO’s own “costs of operations”, while “charges” are to recover amounts paid or payable to another person.

Section 25 of the *Electricity Act, 1998* provides the OEB with the authority to review and approve the IESO’s fees, but not its charges. Subsection 25(6) refers only to fees:

(6) The IESO shall not, without the approval of the Board,

(a) establish, eliminate or change any fees it has established; or

(b) eliminate or change any fees established by a predecessor that remain in effect. [Emphasis added.]

Moreover, subsection 25(1) requires the IESO to “submit its proposed expenditure and revenue requirements for the fiscal year and the fees it proposes to charge during the fiscal year to the Board for review.” Those three components – the expenditure requirement, the revenue requirement, and the fees – are connected. It is implicit in the language of this provision that the fees must be calculated at a level that would ensure the IESO’s recovery of its expenditure and revenue requirements. That is how the OEB has always read and applied the provision in its previous fees decisions, both before and after the merger of the IESO and the Ontario Power Authority (OPA). For convenience, sections 25 and 25.1 are reproduced in full in the **Appendix** to this submission.

In summary, the statute is clear that only the IESO’s operating costs are to be recovered through fees, which must be approved by the OEB. Thus, for example, the

IESO's expenditures for office space, computers and staff salaries are properly recovered through fees. These are the types of expenditures the IESO has in fact applied to recover in this proceeding. But amounts collected by the IESO to make payments to market participants under the Market Rules cannot fairly be characterized as operating costs, and therefore cannot be considered fees. They are not reflected in the IESO's financial statements, or in its business plan which was approved by the Minister of Energy.<sup>1</sup> The IESO was right to exclude them from its application.

APPrO acknowledges the critical distinction between fees and charges but, in OEB staff's view, misconstrues the implications of that distinction. On page 3 of its submission, APPrO says the *Electricity Act, 1998* "is explicit about IESO costs that are not to be reviewed by the OEB. Specifically, the OEB is not to review IESO 'charges'. 'Charges' relate to the costs of government directed procurement contracts. The costs of these charges are deemed to be approved by the Board" (footnotes omitted). The first half of that passage is correct: the OEB cannot review IESO charges. However, as OEB staff reads the Act, it is not accurate to say that charges "relate to the costs of government directed procurement contracts".

While certainly the IESO's recovery of the costs of government directed procurement contracts is an example of a charge, it is not the only kind of charge. The definition of "charge" is broader than that: it encompasses any charges "to recover amounts paid or payable by the IESO or the predecessor to another person with respect to electricity". Therefore, although APPrO is right that the costs of such procurement contracts are deemed to be approved by the OEB under s. 25.1(3), it does not follow that other types of charges must be reviewed. It is noteworthy that s. 25.1(2) states that "For greater certainty, the IESO may, subject to the regulations, establish and impose charges to recover from consumers its costs and payments related to procurement contracts" (emphasis added). The phrase "For greater certainty" implies that the subsection is not strictly necessary: even without it, the IESO could still impose charges to recover the costs of procurement contracts. That is consistent with OEB staff's understanding of the overall statutory scheme. The IESO can impose fees to recover operational expenses, which are subject to OEB approval, and charges to recover amounts paid or payable to others (under a procurement contract or under a Market Rule), which are not.<sup>2</sup>

The OEB recognized the distinction between fees and charges in its decisions on the OPA's fees before the OPA merged with the IESO. In the EB-2010-0279 case (for the

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<sup>1</sup> The IESO's 2016 financial statements are found in the Annual Report included in its application at Ex A-3-1. The 2017-2019 business plan is at Ex A-2-2.

<sup>2</sup> It might be asked why the drafters of the legislation chose to include a clause deeming the IESO's procurement contract-related charges to be approved by the OEB (s. 25.1(3)), since charges do not require OEB approval in the first place. It appears to OEB staff that this was included, like s. 25.1(2), to provide "greater certainty", that is, to remove any doubt that the OEB has no role to play in reviewing such charges.

OPA's 2011 fees), a similar issue to the issue now raised by APPrO came up. In its decision on the issues list, the OEB explained the issue as follows:

Parties also agreed that the powers of the Board arising from a section 25.21 review is limited to approving or rejecting the OPA's administration costs (i.e. the fees) and that the Board does not have the power to approve or reject the OPA's non-administrative program spending, such as generation procurement and Conservation and Demand Management ("CDM") procurement activities. The costs associated with these procurement programs are recovered through "charges" and not recovered through the OPA's fees that are approved by the Board. This limit to the Board's authority is made clear in section 25.20 (4) of the Electricity Act which states "The OPA's recovery of its costs and payments related to procurement contracts shall be deemed to be approved by the Board."

Where parties differed was regarding the extent to which the Board's approval of the OPA's administrative fees allows for an examination of the OPA's broader program spending.<sup>3</sup>

The OEB confirmed what had been agreed by the parties: that it was not its role to approve or reject the OPA's charges. Its finding was consistent with its decision in EB-2007-0791 (re the OPA's 2008 fees), where it held:

Fees are separate from the OPA's "charges". Charges are the costs associated with the programs that the OPA undertakes or funds in the CDM and other areas of its mandate and are not recovered through the OPA's fees that are approved by the Board. The Board has no role in approving the OPA's CDM charges.<sup>4</sup>

The OEB added in the 2008 fees case that "The Board's role in a fees proceeding is to assess whether the proposed organizational budget is reasonable."<sup>5</sup>

In OEB staff's view, these observations from the 2008 fees case remain apt today. Although changes were made to the *Electricity Act, 1998* to facilitate the merger of the IESO and the OPA, the Act retains the distinction between fees and charges. The OEB's role in a fees proceeding is still to assess the IESO's "organizational budget".

OEB staff submits that the reasons above are sufficient to dispose of APPrO's request. It simply has no foundation in the statute. Nevertheless, OEB staff wishes to add some comments on APPrO's concerns about open and transparent governance.

APPrO is correct that the wholesale market service charges the IESO collects from market participants are passed on to consumers through the wholesale market service rate applied by distributors. When the OEB approves the wholesale market service rate – typically every year – it relies on IESO forecasts and considers the process to be

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<sup>3</sup> EB-2010-0279, Issues Decision and Procedural Order No. 2, January 11, 2011, p. 4.

<sup>4</sup> EB-2007-0791, Decision and Order, May 15, 2008, p. 6.

<sup>5</sup> *Ibid.*, p. 9.

“largely mechanistic”.<sup>6</sup> But that is not to say there is no public oversight of the charges, including the terms and conditions as well as the costs of any programs underpinning the charges. The oversight is mainly through the statutory process for making the Market Rules. The IESO says on page 3 of its reply that all of its wholesale market service charges, including ancillary services, line losses, congestion management, settlement charges and other charges, are governed by the Market Rules. Although OEB staff has not independently verified that assertion, it would appear that all of the charges in question are rooted in the Market Rules or, in some cases, in a regulation under the *Ontario Energy Board Act, 1998*.

The IESO has the authority under s. 32 of the *Electricity Act, 1998* to make and amend the Market Rules. The Act sets out the process for doing so, which includes the right of any person to apply to the OEB for a review of an amendment.<sup>7</sup> Market participants and other stakeholders therefore have the opportunity to challenge any proposed amendment, including an amendment in respect of an IESO charge. As the IESO explains in its reply on page 3, it consults with a Technical Panel of stakeholders when developing Market Rule amendments, and “Any individual with an interest in the operation of the electricity market can request an amendment to the market rules or comment on a rule amendment under consideration.” Many of the charges in question date back to the Market Rules that were adopted on market opening 15 years ago, through a participatory process. They were drafted by the Market Design Committee, which was created by Order in Council and included stakeholders and consumer representatives, and then approved by the Minister of Energy.<sup>8</sup>

It should also be noted that there is oversight of the IESO’s compliance with the Market Rules in calculating these charges, including through the biennial independent audit of the IESO’s settlement operations, as described in Chapter 9, section 6.17 of the Market Rules, and by the Market Assessment and Compliance Division of the IESO, which enforces compliance with the Market Rules.

Even if APPRO or any other stakeholder believes that, despite the Market Rules process, there is a gap in oversight in respect of the IESO charges, it is not one that can be filled by the OEB in this or any fees case. As the OEB noted in its decision on the OPA’s 2008 fees, “the parameters of the OPA’s fees review are not set by the Board; they are rooted in legislation.”<sup>9</sup>

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<sup>6</sup> Letter to all Licensed Distributors, re: Guidance on Wholesale Market Services Accounting for Capacity Based Demand Response (CBRD) and new IESO Charge Type 9920, March 29, 2016, cited in APPRO’s submission on page 2, footnote 2.

<sup>7</sup> Subsection 32(3).

<sup>8</sup> Market Rules, Chapter 1, s. 2.2.

<sup>9</sup> EB-2007-0791, Decision and Order, May 15, 2008, p. 6.

To reiterate, although OEB staff has provided these comments on the Market Rules in an effort to provide some context in respect of the oversight of the IESO's charges, it is not necessary for the OEB to make any findings in this case on the adequacy of that oversight. It would be sufficient to rely on the clear definition of "fees" in the legislation, which is limited to the IESO's costs of operations.

**B. OEB staff comments on Energy Probe's and VECC's proposed additions to the issues list**

Energy Probe proposed a new issue: *Are the cost consequences, scope and timing of the Market Renewal Program appropriate?* The IESO replied that the proposed wording is too broad. OEB staff supports Energy Probe's suggestion. Although the OEB in this case will only be reviewing and approving the IESO's 2017 budget, the Market Renewal Program (MRP) will be a multi-year project costing around \$150-\$200 million overall, according to the IESO's 2017-2019 business plan. It may be helpful to the IESO and its stakeholders for the OEB in its decision to comment on how the IESO has planned the program, for example, how the IESO has determined timing and resource allocation. This issue concerns the reasonableness of the program as a whole. It would supplement the other issue currently on the issues list concerning the focused on the MRP-related costs incurred in 2017 and recovered through 2017 fees (1.6. *Are the IESO's Market Renewal Program 2017 operational costs appropriate?*).

Energy Probe also proposed a new issue under the Deferral and Variance Account heading: *4.4 Should the IESO establish a separate Market Renewal Program Deferral Account (MRPDA)?* The IESO objected, arguing that such an account is unnecessary in light of its plans to track MRP spending. OEB staff supports the addition of this issue. Although the IESO may well be right that the account is unnecessary, given the tracking measures it will implement, that is something the OEB should determine after hearing the evidence. The account might, as Energy Probe says, facilitate the scrutiny of any MRP cost overruns in a future proceeding.

Finally, Energy Probe also proposed the following revision to one issue: *1.4: Are the IESO's projected staffing levels, salaries, wages, benefits and compensation appropriate and reasonable?* (the underlining denotes Energy Probe's suggested revision). The IESO did not object and neither does OEB staff. OEB staff notes, however, that pursuant to s. 25(5) of the *Electricity Act, 1998*, the OEB is precluded from taking into consideration the remuneration and benefits of the chair and other members of the board of directors of the IESO when reviewing the proposed fees.

VECC proposed the following new issue: *1.7 Is the IESO's proposed Market Renewal Program within the mandate of the IESO and, if so, does the program provide sufficient probable benefits to justify its costs?* The IESO replied that "the MRP clearly falls within



the IESO's scope of responsibilities as set out in the *Electricity Act, 1998*," and OEB staff agrees. It is not clear to OEB staff why VECC believes there is any doubt as to the IESO's authority to embark on the MRP. VECC asks, "are these costs contemplated by 25.1(1)(c) of the *Electricity Act*?" but in OEB staff's view, they clearly seem to be contemplated by ss. 25.1(1)(a) and (b):

**25.1(1)** The IESO may establish and charge fees to recover,

(a) the costs of anything done in connection with the IESO-controlled grid or the IESO-administered markets;

(b) the costs of doing anything the IESO is required or permitted to do under this or any other Act; and

(c) any other type of expenditure the recovery of which is permitted by the regulations, subject to any limitations and restrictions set out in the regulations.

According to the IESO's 2017-2019 business plan, which was approved by the Minister of Energy, the scope of the MRP will include:

... improvements to the way the IESO schedules energy, procures supply resources, and manages variability – in particular:

- A single-schedule market;
- A financially binding Day-ahead Market;
- Enhanced real-time unit commitment;
- A capacity auction including the import and export of capacity;
- More frequent intertie scheduling; and
- Other operability enhancements as identified by the IESO and its stakeholders.

Many of these changes will result in increased opportunities for both consumers and generators by introducing stable competitive mechanisms to meet a variety of system needs. These market structures are well-proven in other electricity markets and Ontario will be able to benefit from the best practices that have emerged in those markets over the past two decades. However, there is significant work ahead for the IESO and its stakeholders to design a market that best meets Ontario's needs.

All of those elements would appear to fall squarely within the IESO's statutory mandate as the overseer of the electricity grid and markets.

Further, OEB staff submits that the second part of VECC's proposed issue – *does the program provide sufficient probable benefits to justify its costs* – is unnecessary in light of Issue 1.6 (*Are the IESO's Market Renewal Program 2017 operational costs appropriate?*) and the new issue suggested by Energy Probe (*Are the cost consequences, scope and timing of the Market Renewal Program appropriate?*).

Another new issue proposed by VECC is: *1.8 Are the forecast energy volumes used to calculate the usage fees reasonable and appropriate?* The IESO says this is unnecessary. OEB staff does not support the proposed addition. This was not an issue in the last fees case, or, as far as OEB staff can tell, in earlier fees cases. Forecasting energy volumes is a core function of the IESO, and it is unlikely any other party in this proceeding would be able to come up with a better forecast. More to the point, to the extent any variance between forecast and actual volumes results in an over- or under-collection of revenue through the IESO's approved fees, the variance would be tracked and ultimately reconciled through the existing Forecast Variance Deferral Account. OEB staff notes that this is different than the typical utility rate application, where the utility bears the load forecast risk.

VECC also proposed the following issue: *1.9 Is the allocation of energy volumes and costs as between domestic and export markets used to derive the proposed usage fees reasonable?* The IESO objects because it believes the allocation of costs between domestic and export customers was already addressed in the IESO's 2016 fees case (EB-2015-0275), and because the allocation of volumes is based on its forecast. OEB staff submits that the determination of export and domestic energy volumes is an element of forecasting energy volumes, and as noted above, this is a core function of the IESO that would not benefit from examination in this proceeding. Nevertheless, OEB staff submits that any party that wishes to explore the allocation of costs between domestic and export customers can do so under Issue 2.1: *Is the methodology used to derive the proposed IESO Usage Fees and the resulting Fees of \$1.2187/MWh for domestic customers and \$0.9872/MWh for export customers appropriate?* OEB staff therefore does not support the proposed addition of this issue.

The last new issue proposed by VECC is: *7.0 Are the filing requirements for IESO Fees sufficient?* The IESO does not support this proposal, noting that it has been responsive to the concerns expressed by intervenors about the adequacy of the information filed. OEB staff does not see why this proposed addition is warranted. There currently are no OEB guidelines for the IESO, although the IESO agreed in the settlement approved in the 2016 fees case to include in future applications certain information requested by the parties. VECC acknowledges that "the IESO has taken a number of positive steps to address our concerns"; it is therefore not evident to OEB staff that the formalization of filing guidelines is necessary. If the OEB considers that formal guidelines would be useful, OEB staff submits that they could be developed outside the current application, with input from the IESO and stakeholders.

VECC also proposes a change to another issue: *1.4 Are the IESO's projected staffing levels compensation costs appropriate and reasonable?* OEB staff agrees with the

IESO that this change would be redundant if the OEB accepts the revisions to this issue proposed by Energy Probe which were discussed above.

**All of which is respectfully submitted**

## **APPENDIX: SECTIONS 25 and 25.1 OF THE *ELECTRICITY ACT, 1998***

### **Review of requirements and fees**

25 (1) The IESO shall, at least 60 days before the beginning of each fiscal year, submit its proposed expenditure and revenue requirements for the fiscal year and the fees it proposes to charge during the fiscal year to the Board for review, but shall not do so until after the Minister approves the IESO's proposed business plan for the fiscal year under section 24. 2014, c. 7, Sched. 7, s. 3 (1).

### **Previous fees continued**

(2) Until the Board approves the proposed expenditure and revenue requirements for the fiscal year and the fees the IESO proposes to charge during the fiscal year, the fees approved for the previous fiscal year remain in effect unless the Board orders otherwise. 2014, c. 7, Sched. 7, s. 3 (1).

### **Exception**

(3) Where the IESO is unable to make its submission under subsection (1) within the time required under that subsection, the IESO shall file its proposed expenditure and revenue requirements for the fiscal year and the fees it proposes to charge during the fiscal year to the Board for review as soon as possible after the Minister has approved its business plan under section 24. 2014, c. 7, Sched. 7, s. 3 (1).

### **Board's powers**

(4) The Board may approve the proposed expenditure and revenue requirements and the proposed fees or may refer them back to the IESO for further consideration with the Board's recommendations. 2014, c. 7, Sched. 7, s. 3 (1).

### **Same**

(5) In reviewing the IESO's proposed expenditure and revenue requirements and proposed fees, the Board shall not take into consideration the remuneration and benefits of the chair and other members of the board of directors of the IESO. 2014, c. 7, Sched. 7, s. 3 (1).

### **Changes in fees**

(6) The IESO shall not, without the approval of the Board,

- (a) establish, eliminate or change any fees it has established; or
- (b) eliminate or change any fees established by a predecessor that remain in effect. 2014, c. 7, Sched. 7, s. 3 (1).

### **Hearing**

(7) The Board may hold a hearing before exercising its powers under this section, but is not required to do so. 2014, c. 7, Sched. 7, s. 3 (1).

### **Transition, initial fiscal year**

(8) Despite subsection (1), the IESO shall submit its proposed expenditure and revenue requirements for its first full or partial fiscal year that occurs after subsection 3 (1) of Schedule 7 to the *Building Opportunity and Securing Our Future Act (Budget Measures), 2014* comes into force and the fees it proposes to charge during that full or partial fiscal year to the Board for review not later than 30 days after the Minister approves the IESO's proposed business plan for that full or partial fiscal year under subsection 24 (3), but shall not submit its proposed expenditure and revenue requirements until after the Minister approves the proposed business plan. 2014, c. 7, Sched. 7, s. 3 (1).

#### **Transition, fees**

(9) Until the Board approves the proposed expenditure and revenue requirements for the IESO's first full or partial fiscal year that occurs after subsection 3 (1) of Schedule 7 to the *Building Opportunity and Securing Our Future Act (Budget Measures), 2014* comes into force and the fees the IESO proposes to charge during that full or partial fiscal year, the IESO shall continue to charge the fees that were approved by the Board and that applied to its predecessors immediately before subsection 3 (1) of Schedule 7 to the *Building Opportunity and Securing Our Future Act (Budget Measures), 2014* comes into force. 2014, c. 7, Sched. 7, s. 3 (1).

#### **Transition, orders**

(10) For greater certainty, the Board's orders relating to the predecessors' expenditure and revenue requirements and fees for their fiscal year that applied immediately before subsection 3 (1) of Schedule 7 to the *Building Opportunity and Securing Our Future Act (Budget Measures), 2014* comes into force continue to be in effect until the Board approves the first expenditure and revenue requirement and fees for the IESO. 2014, c. 7, Sched. 7, s. 3 (1).

#### **Fees**

**25.1** (1) The IESO may establish and charge fees to recover,

- (a) the costs of anything done in connection with the IESO-controlled grid or the IESO-administered markets;
- (b) the costs of doing anything the IESO is required or permitted to do under this or any other Act; and
- (c) any other type of expenditure the recovery of which is permitted by the regulations, subject to any limitations and restrictions set out in the regulations. 2014, c. 7, Sched. 7, s. 3 (1).

#### **May recover costs of procurement contracts**

(2) For greater certainty, the IESO may, subject to the regulations, establish and impose charges to recover from consumers its costs and payments related to procurement contracts. 2014, c. 7, Sched. 7, s. 3 (1).

#### **Board deemed to approve recovery**

(3) The IESO's recovery of its costs and payments related to procurement contracts is deemed to be approved by the Board. 2014, c. 7, Sched. 7, s. 3 (1).