EB-2019-0002
ONTARIO ENERGY BOARD

IN THE MATTER OF subsection 25(1) of the *Electricity Act, 1998*;

AND IN THE MATTER OF a Submission by the Independent Electricity System Operator to the Ontario Energy Board for the review of its proposed expenditure and revenue requirements for the fiscal year 2019 and the fees it proposes to charge during the fiscal year 2019.

REPLY ARGUMENT OF THE INDEPENDENT ELECTRICITY SYSTEM OPERATOR

1. Introduction

1. On September 30, 2019, the Board issued Procedural Order No. 7 (PO#7) in this proceeding which provided for the Independent Electricity System Operator (IESO) to file Argument in Chief by October 11, 2019, OEB Staff and intervenors to file submissions, if any, by October 25, 2019 and the IESO to file reply argument by November 6, 2019.

2. In accordance with PO#7, the IESO filed its Argument in Chief on October 11, 2019 and subsequently the IESO received the following submissions:

(i) OEB Staff Submission;
(ii) Association of Major Power Consumers in Ontario (AMPCO) submissions (AMPCO Submissions);
(iii) Association of Power Producers of Ontario (APPrO) submissions (APPrO Submissions);
(iv) Building Owners and Managers Association, Greater Toronto (BOMA) submissions (BOMA Submissions);
(v) Canadian Manufacturers & Exporters (CME) submissions (CME Submissions);
(vi) Energy Probe Research Foundation (Energy Probe) submissions (Energy Probe Submissions);
(vii) School Energy Coalition (SEC) submissions (SEC Submissions);

(viii) Society of United Professionals (SUP) submissions (SUP Submissions); and

(ix) Vulnerable Energy Consumers Coalition (VECC) submissions (VECC Submissions).

3. This is the Reply Argument of the IESO filed in accordance with PO#7 and in response to the submissions listed above. The submissions made by OEB Staff and intervenors fall generally into a number of areas, namely, Market Renewal Program (MRP) expenses, employee compensation costs, operating reserve and materiality threshold. These areas, as well as a number of questions raised by OEB Staff, will be addressed under the headings that follow.

2. Expenditure and Revenue Requirements and Usage Fees

4. OEB Staff says that it has no concerns with the majority of the IESO's proposed revenue requirement and indeed notes that the resulting fee is actually lower for domestic customers than the current fee, although slightly higher for export customers.[1] Aside from arguments about the MRP, many of the intervenor submissions do not raise any specific issues with respect to the IESO's 2019 expenditure and revenue requirements and usage fees.[2]

5. Submissions by OEB Staff and intervenors about the MRP are addressed separately below. Other than these submissions about the MRP, the issues raised in argument that bear on the IESO's expenditure and revenue requirements and usage fees fall into two main areas: OEB Staff questions and the IESO's employee compensation costs.

[1] OEB Staff Submission, page 5.

[2] For its part, VECC submits that, given the time remaining to the end of 2019, there is little value in arguing about minor changes to the revenue requirement and that the Board should approve the fees as applied for in 2019; accordingly, VECC limits its submissions to "matters affecting the future impact on consumers": VECC Submissions, paragraph 4, page 4.

(a) OEB Staff Questions

6. Much of the OEB Staff Submission consists of questions that OEB Staff has put forward for the IESO to answer. OEB Staff says that, to the extent these questions can be addressed by the IESO in its reply submission without introducing new evidence, “this will inform the OEB to what extent the IESO should be required to further substantiate its position on these matters in the next fee application”.[3]

7. Of course, when making its final submissions in this proceeding, OEB Staff did not know to what extent its questions would be answered in the IESO’s reply submission. Nevertheless, the OEB Staff Submission recommends that the 2019 revenue requirement be approved on an interim basis to allow OEB Staff’s questions to be addressed “while avoiding having two revenue requirement applications before the OEB at the same time”.[4]

8. The OEB Staff questions that relate to the MRP are addressed under the Market Renewal Program heading below. OEB Staff’s other questions relate to staffing impacts on revenue requirement, the wind-down of the Green Ontario Fund and the activities of the IESO’s Market Assessment and Compliance Division (MACD).

(i) Staffing Impacts on Revenue Requirement

9. OEB Staff questions what the IESO has done to make room for 111 incremental staff in 2019 while maintaining the same revenue requirement as 2017 and 2018. OEB Staff says that at least some of the incremental headcount is being capitalized, but it is not clear to OEB Staff how many of the incremental staff are being capitalized and how many are full-time permanent and will be continuing even after the end of capitalized projects.[5]

[3] OEB Staff Submission, page 5.
[4] OEB Staff Submission, pages 5-6.
[5] OEB Staff Submission, page 16.

10. In response to a question from OEB Staff about "staff migration", the IESO provided a table comparing the breakdown of staff across the IESO's business units in the 2018 and 2019 budgets. This table shows the staff changes across the business units that result in the 111 incremental FTEs referred to the OEB Staff Submission.[6]

11. The IESO's response to the question from OEB Staff also explained that the increase of 111 FTEs was mainly due to increased support for the MRP, in that additional resources were required to support the detailed design of the program and additional staff were required in legal resources for the legal and market rule advisory support needs of the MRP.[7] As for the capitalization of costs, the IESO's evidence is that a significant portion of the 2019 FTE increase is related to MRP resources whose costs will be primarily capitalized as part of MRP detailed design work,[8] including the legal support costs required in the development of the detailed design.[9]

12. The evidence also makes clear that the $12 million reduction in capital costs[10] for the Capacity work stream is due to the cancellation of planned hiring that would have supported the detailed design phase.[11] Incremental staffing resources for the Capacity work stream were originally budgeted at 55, but were reduced to an average of 27 as a result of the revised approach. The evidence is that this reduction will occur gradually through 2019, with further reductions occurring in 2020.

13. As to the extent to which full-time regular staff will be continuing after the end of the capitalized projects, the evidence is that there are no regular Capacity work stream positions.[12] Further, the IESO indicated in response to a question from OEB Staff that

[6] Response to OEB Staff Interrogatory 9a)i. (OEB Staff 9a)i. Response), Exhibit I, Tab 1.3, Schedule 1.09 OEB Staff 9, page 3.
[7] OEB Staff 9a)i. Response, page 2.
[8] Response to PWU Interrogatory 3, Exhibit I, Tab 1.3, Schedule 7.03 PWU 3.
[9] Response to VECC Interrogatory 15, Exhibit I Tab 6.0 Schedule 3.15 VECC 15.
[10] The $12 million reduction in capital costs is explained in Argument in Chief, at paragraph 52, page 15.
[11] Exhibit C-2-2, page 4 of 5.
[12] Response to OEB Staff Interrogatory 40, Exhibit I, Tab 6.0, Schedule 1.40 OEB Staff 40.

only positions with enduring work "post-MRP" will be converted to regular employment.[13] Of course, to the extent that there are costs included in a future IESO revenue requirement for employees who convert from MRP work to regular employment, those costs will be subject to review at the time when the associated revenue requirement is reviewed.

(ii) Green Ontario Fund

14. OEB Staff questions how the IESO's work on the Green Ontario Fund does not impact the 2019 revenue requirement given that IESO staff were hired to support Green Ontario Fund activities, which are now winding down.[14]

15. Activities and costs of the IESO in support of the Green Ontario Fund have never been included in the revenue requirement submitted for review by the OEB and thus the winding down of these activities and costs has no impact on the revenue requirement. The evidence specifically confirms that all of the work done by the IESO for the Green Ontario Fund does not impact the IESO's revenue requirement and is funded separately and that this includes reimbursement of all of the IESO's termination and wind-up costs.[15]

(iii) MACD Activities

16. OEB Staff notes that the OEB has not expressed an interest in prior revenue requirement submissions about gaining more clarity with respect to MACD activities, but suggests that, given recent changes, it would be helpful if the IESO provided further explanation in future applications about MACD activities, budgets and spending.[16] It is not clear what OEB Staff means by its reference to "recent changes", because OEB

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[13] Response to OEB Staff Interrogatory 14, Exhibit I, Tab 1.3, Schedule 1.14 OEB Staff 14. In this response, the IESO identified Market Power Mitigation (incremental roles in MACD) as a potential area for employees engaged in MRP work to convert to regular employment.
[14] OEB Staff Submission, page 17.
[15] Response to BOMA Interrogatory 11(b), Exhibit I, Tab 0, Schedule 2.11 BOMA 11.
[16] OEB Staff Submission, page 17.

Staff's comments about MACD activities essentially just summarize evidence about the way in which MACD activities are funded.[17]

17. The IESO funds MACD through both the IESO fee and a separate Market Rule prescribed Adjustment Account. The IESO deposits penalty payments and other prescribed funds such as payment adjustments arising from resolution of settlement disputes and negotiated settlements into the Adjustment Account. The Market Rules prescribe that certain expenses associated with those outcomes are to be reimbursed from the Adjustment Account.[18]

18. While the IESO does not seek fee recovery for expenses reimbursed via the Adjustment Account, the IESO accepts OEB Staff's suggestion for enhanced clarity around the IESO's Adjustment Account to the extent that such clarity will advance an understanding of costs included in the OEB-approved fees. Accordingly, in the IESO's 2020 Revenue Requirement Submission, the IESO will file evidence that will delineate spending between the Adjustment Account and the IESO's OEB approved fees.

(b) Employee Compensation Costs

19. As set out in Argument in Chief, the IESO filed a study completed by Mercer (Canada) Limited (Mercer) to fulfill its agreement that it would hire a third-party consultant to conduct a total compensation study of represented and non-represented staff, excluding executives.[19] OEB Staff says that it does not object to any of the findings in the study,[20] but concludes from the study that compensation for IESO staff is higher than energy sector peers.[21] Energy Probe makes a similar argument and goes on to propose that the OEB indicate that the IESO should amend its total compensation practices and

[17] *Ibid*.
[18] OEB Staff Interrogatory 10a), Exhibit I Tab 1.3, Schedule 1.10 OEB Staff 10.
[19] Argument in Chief, paragraphs 38-40, page 11.
[20] No intervenor raised any issue about the IESO's fulfilment of its commitment in relation to the compensation study.
[21] OEB Staff Submission, page 24.

direct another benchmark study to be provided in the 2021 revenue requirement submission.[22]

20. As a result of the unique nature of the IESO's operations, the organization includes many jobs that are not commonly found in other organizations, or are single incumbent positions. This reduces the number of positions, and the number of employees in particular positions, that can be accurately matched to market.[23]

21. The Mercer study indicates that the IESO's total cash compensation, on an aggregate organization basis, is positioned within the market competitive range for the energy sector.[24] Thus, on a total cash basis, the IESO's employee compensation is aligned with the energy sector, which is the IESO's main peer group.[25] The IESO primarily competes within the energy sector labour market and must offer compensation packages comparable to those in its sector.[26]

22. The Mercer study also indicates that, on an overall organization basis, the IESO's total remuneration, including the value of all cash compensation, benefit and pension plans, is positioned above the market 50th percentile for the energy, public and private sector peer groups.[27] According to Mercer, positioning above the 50th percentile on a total remuneration basis is primarily a result of the high employer provided value of pension plans in place at the IESO for represented jobs.[28]

23. Pension changes have been negotiated for the IESO's represented employees, to become effective in 2025, which will better align the IESO with its peer group comparators

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[22] Energy Probe Submissions, page 5.
[23] Response to SUP Interrogatory 7, Exhibit I, Tab 5.2, Schedule 9.07 SUP 7.
[24] Exhibit C-4-1, Attachment 1, page 1.
[25] Response to Energy Probe Interrogatory 18 (Energy Probe 18 Response), Exhibit I, Tab 5.2, Schedule 4.18 ENERGY PROBE 18, page 1.
[26] Energy Probe 18 Response, page 2.
[27] Exhibit C-4-1, Attachment 1, page 3.
[28] *Ibid*.

in the energy sector.[29] These changes are outlined in the evidence in this proceeding,[30] and successor organizations of Ontario Hydro have made essentially the same changes, also to become effective in 2025.[31]

24. The IESO will continue its efforts to control pension costs in future collective bargaining meetings.[32] More particularly, in future collective bargaining sessions, the IESO will table increasing employee pension plan contributions and cost-saving pension plan proposals.[33]

25. In light of this evidence, it is unnecessary for the Board to indicate, as Energy Probe has submitted, that the IESO should amend its total compensation practices. Except for pension benefits, the IESO's employee compensation is aligned with its peer group comparators in the energy sector and the IESO has made, and will continue to make, efforts to address pension costs through the collective bargaining process.

26. The OEB Staff Submission notes the evidence that the IESO has negotiated significant plan changes that will better align the IESO with its peer group comparators effective in 2025.[34] OEB Staff goes on to suggest that the IESO provide a report on progress in future revenue requirement submissions, recognizing the 2025 timeline.[35] The IESO submits, however, that it provides information about staffing costs in each revenue requirement submission and this provides the means for monitoring trends in staffing costs and that a specific requirement for progress reports is not necessary.

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[29] Energy Probe 18 Response, page 1; Response to OEB Staff Interrogatory 13b) (OEB Staff 13b) Response), Exhibit I, Tab 1.3, Schedule 1.13 OEB Staff 13, page 1; Response to OEB Staff Interrogatory 21c) (OEB Staff 21c) Response), Exhibit I, Tab 5.2, Schedule 1.21 OEB Staff 21, page 2.
[30] OEB Staff 13b) Response, page 2; OEB Staff 21c) Response, page 2.
[31] OEB Staff 13b) Response, page 1; OEB Staff 21c) Response, page 2.
[32] OEB Staff 13b) Response, page 2; OEB Staff 21c) Response, page 2.
[33] Energy Probe 18 Response, page 2.
[34] OEB Staff Submission, pages 24-25.
[35] OEB Staff Submission, page 25.

27. The IESO sees the value in undertaking benchmarking studies, to track progress relative to its comparators. However, it's the IESO's experience that these types of studies only provide value every few years as trends become apparent.

<u>3. Operating Reserve</u>

28. The IESO proposes that its operating reserve be returned to the level of $10 million that was approved for the IESO after its merger with the Ontario Power Authority (OPA).[36] Intervenors and OEB Staff contend that the operating reserve should be retained at the $6 million level that was agreed on in package settlements reached in the context of the IESO's 2017 and 2018 revenue requirement submissions.

29. AMPCO says that a $6 million operating reserve was approved and "sufficient" in previous years.[37] Actually, though, the $6 million reserve was in place during only two of the years after the merger of the IESO and the OPA (2017 and 2018) and, in one of those two years, the $6 million reserve was not sufficient.

30. More specifically, the impact of the accounting restatement referred to in Argument in Chief[38] was greater than the IESO's $6 million reserve[39] and, as at the end of 2018, the IESO was in a deficit position of $4.73 million.[40] A $10 million operating reserve would have gone a long way towards mitigating the 2018 year-end deficit that resulted from this unplanned event.

31. OEB Staff asserts that the impact of the accounting restatement could simply have been separated into another "deficit account", in which case it would have had no impact on the Forecast Variance Deferral Account (FVDA) operating surplus/deficit.[41] But

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[36] Argument in Chief, paragraph 29.
[37] AMPCO Submissions, page 4.
[38] Argument in Chief, paragraphs 33-35.
[39] Exhibit B-3-1, page 3.
[40] *Supra*, page 4.
[41] OEB Staff Submission, page 21.

creating a new account to record the impact of the accounting restatement would have made no difference to the overall deficit faced by the IESO. And OEB Staff's suggestion that the IESO can access credit through the Ontario Electricity Financial Corporation (OEFC)[42] does not change the fact that, ultimately, the IESO has no means to recover a deficit amount other than through its fees.

32. Similarly, CME submits that, in any instance where the existing $6 million reserve is not sufficient, the FVDA would track the difference for future collection from ratepayers.[43] However, this is much like OEB Staff's submission about recording the impact of the accounting restatement in a new "deficit" account: having a place to record a deficit, whether it be the FVDA or a new account, is not an answer to the need for a reserve. Even if the IESO has an account in which to record a deficit, and even if the IESO can borrow from the OEFC when it has a deficit, the IESO must still come forward with a plan for recovery of a deficit through its fees (as it will be doing in its next fees case). A $10 million operating reserve would have mitigated much of the 2018 year-end deficit that the IESO now needs to plan to recover by way of future fees.

33. CME states that the IESO was unable to point to any particularly volatile projects or capital requirements that it is currently undertaking that would justify the increase in operating reserve.[44] However, the IESO has provided evidence for projects with increased capital requirements and project complexities.[45]

34. OEB Staff says that the IESO is faced with uncertainty and project complexities in every year.[46] The IESO has put forward evidence that, in view of uncertainty and project complexities, a $10 million reserve, as was approved following the merger of the IESO and the OPA, is appropriate.[47] The IESO's evidence is that the effect of the accounting restatement would have been substantially mitigated by a $10 million reserve. No

[42] OEB Staff Submission, page 20.
[43] CME Submissions, paragraph 22.
[44] CME Submissions, paragraph 20.
[45] Response to CME Interrogatory 2a) Exhibit I, Tab 0, Schedule 8.02 CME 2.
[46] OEB Staff Submission, page 20.
[47] Exhibit B-1-1, page 7.

evidence has been led in support of a $6 million reserve. The IESO submits that, on the evidence in this proceeding, a $10 million reserve should be approved.

4. Market Renewal Program

(a) OEB Staff Questions

35. As noted above, the OEB Staff Submission puts forward a number of questions for the IESO to answer, including questions about the MRP. The MRP-related questions are as follows:

(i) whether the requested revenue requirement and staffing levels remain appropriate, in light of the IESO's decision not to proceed with detailed design work on the Capacity work stream,[48] particularly given that, according to OEB Staff, the IESO has indicated there is "no need for capacity for the foreseeable future";[49]

(ii) why, after cancellation of the Incremental Capacity Auction (ICA), the dollar amount requested for the General work stream did not change;[50]

(iii) why the IESO's forecast of O&M spending on the Capacity work stream increased by $1.5 million to $2.6 million, even though, according to OEB Staff, detailed design costs that need to be expensed due to cancellation of the ICA amount to only $0.5 million;[51] and

(iv) why the Transitional Capacity Auction (TCA) cannot be included in the MRP, particularly with the cancellation of the ICA, in order to avoid duplication particularly in relation to stakeholder engagement.[52]

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[48] OEB Staff Submission, page 8.
[49] OEB Staff Submission, page 10.
[50] OEB Staff Submission, pages 10-11.
[51] OEB Staff Submission, page 11.
[52] OEB Staff Submission, page 12.

36. The IESO acknowledges OEB Staff's desire for the IESO to clarify the matters raised in the OEB Staff Submission. The IESO will address these matters below, with reference to evidence on the record of this proceeding. The IESO submits that the record is complete, and with this clarity the Board can approve the IESO's Submission for Review.

(i) Revenue Requirement and Staffing Levels Remain Appropriate

MRP Capacity Work Stream and The Need for Capacity in Ontario

37. Much is made of the IESO's announcement on July 16, 2019 that it would stop work on the High Level Design (HLD) for the ICA, and in particular, the IESO's stated rationale that there is a "limited need for new capacity". This has been incorrectly interpreted by OEB Staff to be a statement that there is "no need for capacity".[53]

38. The IESO's evidence in this proceeding shows a forecast capacity gap in 2020 and in every year going forward, increasing to a significant capacity gap in 2023 that must be addressed to ensure the reliability of Ontario's electricity system.[54] The Capacity work stream activities are a critical part of the IESO's strategy to address this significant capacity gap. The IESO will clarify the capacity need, and by extension, the work that must be undertaken in 2019 to fill that need, in the explanation that follows below.

39. On September 13, 2018 the IESO released the Electricity Planning Outlook that forecasted a capacity deficit in the summer of 2023 of approximately 4,000 MW.[55] At that time the IESO also identified that the ICA would not be launched in time to address the projected 2023 capacity gap. ICA implementation was targeted for the end of 2022 – to meet the capacity gap for the summer of 2025.[56]

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[53] OEB Staff Submission, page 10.
[54] Response to OEB Staff Interrogatory 43, (OEB Staff 43 Response), Exhibit I, Tab 6.0, Schedule 1.43 OEB Staff 43.
[55] Response to AMPCO Interrogatory 36, Exhibit I, Tab 6.0, Schedule 13.36 http://www.ieso.ca/-/media/Files/IESO/Document-Library/planning-forecasts/tech-conf/2018-Technical-Planning-Conference-Presentation.pdf?la=en
[56] Exhibit A-3-1, page 7; Response to APPrO Interrogatory 8 (APPrO 8 Response), Exhibit I, Tab 6.2, Schedule 11.08 APPrO 8.

40. As a result, and building on the design fundamentals of the Demand Response Auction the IESO began work on the TCA to meet the Province's near term capacity needs.[57] The TCA provides an opportunity for generators whose contracts are expiring over the next few years, as well as imports and other resources, to compete alongside demand response in meeting Ontario's capacity needs.[58]

41. In July 2019, the IESO made the decision to discontinue work on the ICA, recognizing that there was a limited need for ***new*** capacity build[59] - a main feature of the ICA was procuring new-build capacity. While work on the ICA was discontinued, there continues to be a forecasted capacity gap that must be addressed to ensure the reliability of Ontario's electricity system.[60]

42. The first TCA is planned to run on December 2019 for a commitment period of May 1, 2020 to April 30, 2021.[61] The TCA will also run future capacity auctions in June 2020 (for a May 1, 2021 to April 30, 2022 commitment period), and December 2020 (for a May 1, 2022 to April 30, 2023 commitment period).[62] The IESO will continue to run regular capacity auctions from 2021 onwards.

43. After the discontinuation of the ICA, activities of the MRP Capacity work stream were refocused to prepare for the critical auctions taking place in 2021 and beyond, which will procure capacity for the significant capacity gap forecast for the summer of 2023 onwards. This is what the IESO has referred to in its evidence as the Revised Approach.[63]

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[57] APPrO 8 Response.
[58] Exhibit A-3-1, page 7; APPrO 8 Response.
[59] Exhibit C-2-2.
[60] OEB Staff 43 Response.
[61] Response to OEB Staff Interrogatory 37, Exhibit I, Tab 6.0, Schedule 1.37 OEB Staff 37.
[62] Response to AMPCO Interrogatory 35 (AMPCO 35 Response), Exhibit I, Tab 6.0, Schedule 13.35, Attachment 8, pages 34-35.
[63] Argument in Chief, pages 13-15.

MRP Capacity Work Stream Activities for July to December 2019

44. The Capacity work stream has not been cancelled, as indicated in the SEC Submissions.[64] Rather, the Capacity work stream has been refocused on the following activities that are included in the Revised Approach:

- assessing the aspects of the ICA design that can be repurposed to continue the evolution of the TCA to meeting the future critical needs;
- reviewing potential complementary procurement mechanisms with stakeholders;
- continued efforts to finalize a number of foundational capacity related features that would be common to any mechanism including qualification, obligations, and improved planning requirements; and
- development of any future capacity auction enhancements including a cost/benefit assessment approved by the IESO Board.[65]

45. As set out above, there remains a capacity gap in the immediate term, increasing to a more significant gap in 2023. As part of the IESO's strategy to address that gap, it is evolving its capacity auction. That strategy includes an average of 27 FTEs from July to December 2019, with 25 staff remaining in place by year end to carry out the identified activities in the Revised Approach. Staff resource requirements for the Capacity work stream in 2020 are further reduced to an average of 12 FTEs.[66]

46. Due to the complexities of creating an enduring capacity auction, it would be impractical and imprudent to attempt to introduce the full suite of changes required on the eve of the significant capacity need the auction would be required to address. The IESO submits that progressing in an incremental approach, as the IESO has planned, allows the IESO to:

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[64] SEC Submissions, page 2.
[65] Response to OEB Staff Interrogatory 29, Exhibit I, Tab 6.0, Schedule 1.29 OEB Staff 29 (OEB Staff 29 Response).
[66] Response to OEB Staff Interrogatory 39, Exhibit I, Tab 6, Schedule 1.39 OEB Staff 39.

- provide sufficient time to assess and evolve auction design features, informed by stakeholder input;
- allocate the necessary resources to implement new auction design features in manageable steps; and
- monitor and identify unforeseen consequences arising from new auction design features.

47. It is critical that the IESO evolve its capacity auction in a manner that promotes confidence in the auction process amongst existing and potential auction participants. The IESO submits that a phased implementation of changes will help promote that confidence and is consistent with the IESO's general practice of prudently evolving market design incrementally.

(ii) General Work Stream

48. With respect to OEB Staff's submission related to the General work stream, MRP has a distinct cost centre to track costs incurred by the program.[67] All staff work in support of MRP is charged to the program.[68]

49. For the purposes of tracking and reporting costs, the General work stream was created to collect costs that are not easily distinguishable between energy or capacity such as a cost controller.[69]

50. The General work stream does not represent "IESO staff that assist on MRP but are not dedicated to the MRP" as OEB staff suggest.[70] These types of resources are referred to as shared resources.[71]

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[67] The MRP Cost Report, Exhibit C-2-1.
[68] Exhibit C-2-1, page 12.
[69] Response to OEB Staff Interrogatory 33 a), Exhibit I, Tab 6.0, Schedule 1.33 OEB Staff 33 (OEB Staff 33 Response).
[70] OEB Staff Submission, page 10.
[71] Exhibit C-2-1, Table 12, page 13.

51. Staff functions within the General work stream are still required for both Capacity and Energy work streams to move forward. All staff reductions in association with the Revised Approach came from staff functions within the Capacity work stream.[72]

(iii) Forecast O&M Spending

52. In its comments about the IESO's forecast of O&M spending on the Capacity work stream, OEB Staff recognizes that operating expenses in the first half of 2019 include an amount of $0.5 million that will be expensed, rather than capitalized as planned, as a result of the decision not to proceed with detailed design of the ICA.[73] However, the OEB Staff Submission does not recognize Capacity work stream costs in the second half of 2019 that, for the same reason, will be treated as operating expenses, although originally budgeted as capital costs.

53. As pointed out in Argument in Chief, the operating expense forecast for the Capacity work stream in the second half of 2019 increased by $1.5 million against budget due to staff costs budgeted as capital that will be treated as operating expenses.[74] The amount of budgeted capital costs to be treated as operating costs due to the decision not to proceed with detailed design obviously is much less than the total reduction of capital costs from the budgeted amount, which is $12 million.[75]

54. OEB Staff's focus on operating expenses that have increased due to the accounting treatment of expenses originally budgeted as capital costs must be considered in the light of the overall reduction of the capital cost budget from $12 million to zero. In fact, the IESO's budget for the Capacity work stream has actually been reduced by 75% from the budgeted amount[76]. It should also be noted that the $2.6 million

[72] Exhibit C-2-2, page 4.
[73] OEB Staff Submission, page 11; Argument in Chief, paragraph 50, pages 14-15; Exhibit C-2-2, page 2.
[74] Argument in Chief, paragraph 51, page 15; Response to OEB Staff Interrogatory 31(b), Exhibit I, Tab 6.0, Schedule 1.31 OEB Staff 31.
[75] Argument in Chief, paragraph 52, page 15; Response to Energy Probe Interrogatory 21(b), Exhibit I, Tab 6.0, Schedule 4.21 ENERGY PROBE 21.
[76] Exhibit C-2-2, page 4 (a reduction $12 million on a total Capital and Operating budget of $16.8 million.).

budgeted spending for the Capacity work stream in the second half of 2019 represents approximately 1.4% of the IESO's 2019 revenue requirement.

55. While the IESO’s level of activity on the Capacity work stream in the second half of 2019 has been reduced substantially from expectations at the time when the 2019 budget was set, the IESO’s ongoing Capacity-related work continues to be necessary to address the capacity gap explained under the heading MRP Capacity Work Stream and The Need for Capacity in Ontario, above.

(iv) The TCA and the MRP Capacity Work Stream

56. In its submission, OEB Staff requests clarification on why the TCA cannot be included in MRP to avoid duplication of effort. The work activities for the TCA and the Capacity work stream are separate activities. The IESO is working on the TCA to expand participation and enhance several design features of the Demand Response auctions to be executed in 2019 and 2020, which is distinct from the MRP Capacity work stream that will consider future potential enhancements and additional features to auctions taking place in 2021 and beyond, and complementary procurement mechanisms.[77] The IESO submits that there is no overlap or duplication between current TCA activities and MRP Capacity work stream activities. As the IESO moves forward with these activities, it will assess its approach to organizing the broader capacity effort and what is appropriately reported on under the MRP and core IESO work.

(b) MRP Business Case

57. In number of the submissions made in this proceeding, it has been argued that the IESO should not commit to particular spending on the MRP prior to approval of the MRP Energy Business Case (Business Case) by the IESO Board of Directors (BOD).[78] At this time, arguments about whether or not the IESO should spend or make commitments prior

[77] Exhibit C-2-2, OEB Staff 29 Response; Response to OEB Staff Interrogatory 41.
[78] See, for example, SEC Submissions, page 2; AMPCO Submissions, page 3.

to approval of the Business Case are no longer meaningful, because the business case was in fact approved by the BOD on October 23, 2019.[79]

(i) Detailed Design and Business Case Approval

58. In 2017, the IESO published a Benefits Case that assessed the expected benefits for the MRP based on experience from other jurisdictions and previous IESO studies.[80] The Benefits Case focused on concepts and ideas that could improve Ontario's electricity markets and address well documented inefficiencies with the current design. The study concluded that there were compelling reasons to proceed with the project.[81]

59. As stated in evidence, through the course of 2018 and 2019 the IESO worked with stakeholders to develop made-in Ontario HLD that reflected the practical realities of the Ontario marketplace, for example Ontario's unique supply mix and geography, IESO grid operations and the needs of consumers.[82] The IESO submits that only once the HLDs were complete was there sufficient information on how the reforms would work in practice to develop a robust business case with the appropriate degree of accuracy.

60. In 2019, the IESO engaged stakeholders on the draft HLDs seeking comment, input and feedback.[83] This was an important and critical activity in ensuring that there is broad stakeholder support for the new market designs. As described in evidence, given the substantial benefits estimated in the Benefits Case the decision was made to proceed

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[79] http://ieso.ca/-/media/Files/IESO/Document-Library/market-renewal/MRP-Energy-Stream-Business-Case-2019.pdf?la=en.
[80] Response to SEC Interrogatory 21, Exhibit I, Tab 6.1, Schedule 10.21 (SEC 21 Response) – Attachment 1 - A Benefits Case Assessment of the Market Renewal Project, The Brattle Group – April 20, 2017.
[81] *Ibid.*
[82] SEC 21 Response, page 13.
[83] Exhibit C-2-1 page 5.

with detailed design.[84] The IESO received approval from the BOD in August 2018 to proceed to the detailed design phase of the MRP in 2019.[85]

61. SEC argues that the IESO should not commit to any legally binding financial commitments to procure the Dispatch Scheduling and Optimization Engine (DSO) for the Energy work stream prior to Business Case approval.[86] As of the time of the IESO's response to SEC's Interrogatory 27, the IESO had not concluded that procurement process, nor executed any contracts resulting from that procurement.[87] Further, as noted above, the BOD has approved the Business Case on October 23, 2019, and the IESO has yet to enter into a contract for the DSO supply prior to the approval of the Business Case.

62. With respect to the Revised Approach on the Capacity work stream, the IESO will develop a benefit and costing assessment before implementing any additional Capacity auction design work beyond what has been already approved by the BOD.[88]

(c) Stakeholder Engagement Proposal by APPrO

63. APPrO proposes a condition of approval that the stakeholder engagement process addressing procurement mechanisms be open and transparent and, in particular, that the IESO include an independent cost-benefit analysis of all potential procurement approaches.[89] APPrO further submits that the OEB should review the effectiveness of the engagement process in the IESO's next fees case.

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[84] Response to OEB Staff Interrogatory 30a), Tab 6.0, Schedule 1.30 OEB Staff 30 (OEB Staff 30a) Response).
[85] OEB Staff 30a) Response.
[86] SEC Submissions, pages 2-3.
[87] Response to SEC Interrogatory 27.
[88] OEB Staff 30c) Response.
[89] APPrO Submissions, page 4.

64. The IESO has committed to conducting a stakeholder engagement on complementary procurement mechanisms[90] and as is the IESO's practice, the engagement will be conducted according to the IESO's stakeholder engagement principles, which include the assurance of openness and transparency throughout the process in a way that allows for inclusive participation of all affected.[91] The IESO submits that its engagement principles guide the conduct of the IESO, market participants, stakeholders, communities, customers and the general public towards an efficient and effective process.

65. The IESO further submits that APPrO has provided no evidence that the IESO's stakeholder engagement process has not fulfilled its engagement principles with respect to openness and transparency and no basis for the proposed condition of approval of the IESO's application.

66. As discussed above, following its stakeholder engagement efforts, the IESO will develop a benefit and costing assessment before implementing any additional Capacity auction design work beyond what has been already approved by the BOD.[92]

d) Metrics

67. SEC[93] and AMPCO[94] argue that SPI and CPI should be tracked against a baseline schedule and budget for the project as a whole. As noted in evidence, the IESO will report on annual CPI and SPI for the MRP work performed in 2019, in the 2020 Revenue Requirement Submission.[95] The IESO submits that in addition to the 2020 MRP Cost Report within its annual filing, the IESO will be assessing its reporting on MRP as a whole.

[90] Response to Exhibit C-2-2; OEB Staff Interrogatory 42, Exhibit I, Tab 6.0, Schedule 1.42 OEB Staff 42; APPrO Interrogatory 16, Exhibit I, Tab 6.0, Schedule 11.16 APPrO 16.
[91] http://www.ieso.ca/en/Sector-Participants/Engagement-Initiatives/Overview/Engagement-Principles
[92] OEB Staff 30c), Response.
[93] SEC Submissions, page 4.
[94] AMPCO Submissions, page 4
[95] Exhibit C-2-1, page 15

5. Materiality Threshold

68. In Argument in Chief, the IESO set out a number of reasons why different considerations apply to the issue of a materiality threshold for the IESO than for utilities regulated by the OEB. The IESO submitted that a materiality threshold would only be appropriate if the threshold took into account these considerations.[96]

69. CME accepts that there are differences between the IESO and electricity distributors, but submits that the fundamental nature of the IESO and its “relationship” to the OEB and ratepayers is identical to that of a distributor.[97] The IESO does not agree with this assertion.

70. Even in the context of incentive regulation, OEB-regulated utilities invest in rate base, they look to the OEB to approve a return and they look to ratepayers to pay rates that allow them the opportunity to achieve the OEB-approved return. The IESO does not have any such “relationship” with the OEB and ratepayers (or feepayers). It does not earn a return[98] and thus the projects and initiatives that it proposes in order to fulfill its responsibilities that flow from the *Electricity Act, 1998* have nothing to do with any expectation of return or profit.

71. Arguments such as those made by CME[99] focus on the concept of materiality thresholds guided by the size of the revenue requirement of the particular entity. However, it is clear that using revenue requirement as a guide for setting a materiality threshold is anything but an exact science. Certain intervenors draw an analogy to electricity distributors and, on this basis, propose a materiality threshold of approximately $1 million for the IESO.[100] Yet this suggested analogy to electricity distributors is certainly

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[96] Argument in Chief, paragraphs 62-63, pages 18-19.
[97] CME Submissions, paragraph 25.
[98] Subsection 6(2) of the *Electricity Act, 1998* says that the business and affairs of the IESO are to be carried on without the purpose of gain.
[99] CME Submissions, paragraph 30.
[100] SEC Submissions, page 4; CME Submissions, page 6; BOMA Submissions, page 5; AMPCO Submissions, page 4.

no better than the potential analogy to electricity transmitters recognized by OEB Staff and the materiality threshold for an electricity transmitter with a revenue requirement that is $10 million, or about 5%, higher than the IESO's 2019 revenue requirement ($190.8 million) is $3 million.[101]

72. More importantly, these possible analogies to transmitters and distributors simply look past the fundamental differences between regulated utilities and the IESO and are in no way based on the IESO's role, responsibilities or circumstances.[102] By way of contrast, the $4 million materiality threshold proposed in Argument in Chief does have a specific connection to the IESO, because it is the current threshold that is used to determine if approval of the IESO BOD is required for a project.[103] Information provided to the BOD for projects that meet the $4 million threshold is consistent with the type of information that the OEB required for the Commercial Reconciliation System project in this case.[104]

73. The IESO submits that an appropriate materiality threshold for its revenue requirement submissions is $4 million. Alternatively, should the OEB have any uncertainty about the $4 million threshold, the IESO submits that the OEB could adopt one of the suggestions made by OEB Staff, namely, that the OEB could implement a materiality threshold of $4 million given its consistency with the threshold for IESO BOD approval and revisit whether this level is appropriate after some experience has been gained with the threshold and the types of projects undertaken by the IESO.[105]

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[101] OEB Staff Submission, page 28.
[102] Including, for example, the role and responsibilities referred to in paragraph 62(ii), page 18 of, Argument in Chief.
[103] Argument in Chief, paragraph 64, page 19.
[104] Argument in Chief, paragraph 65, page 19.
[105] OEB Staff Submission, page 28.

7. Conclusion

74. For all of the foregoing reasons, the IESO respectfully requests that the Board approve the IESO's proposed revenue and expenditure requirements for the fiscal year 2019 and the fees that the IESO proposes to charge during the fiscal year 2019.

All of which is respectfully submitted.

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