

Association of Major Power Consumers in Ontario

**Application to Review Amendments to the Market Rules made
by the Independent Electricity System Operator**

**SUMMARY CLOSING SUBMISSIONS
OF THE IESO**

December 9, 2019

STIKEMAN ELLIOTT LLP
5300 Commerce Court West
199 Bay Street
Toronto, ON M5L 1B9

Glenn Zacher LSO#: 43625P
gzacher@stikeman.com
Tel: (416) 869-5688

Patrick Duffy LSO#: 50187S
pduffy@stikeman.com
Tel: (416) 869-5257
Fax: (416) 947-0866

Lawyers for the IESO

I. OVERVIEW

1. The central issue before the Board in this proceeding is the Association of Major Power Consumers of Ontario's (AMPCO) claim that it is "unjustly discriminatory" to amend the market rules (the **Amendment**) to expand the current demand response auction (**DRA**) from a demand response-only auction to a technology neutral capacity auction without first addressing whether demand response (**DR**) resources should be entitled to energy payments in the IESO's real-time energy market (**Energy Market**). In the absence of such payments, AMPCO alleges that DR resources will be at a *competitive disadvantage* vis-à-vis generation resources *in the capacity auction* because some DR resources may have to include Energy Market activation costs in their capacity auction bids.

2. On this issue, the evidence before the Board demonstrates that DR resources will not be at a competitive disadvantage and the Amendment is not unjustly discriminatory because:

- (a) *The Amendment treats DR and generation resources equally in the capacity auction* – All DR and generation resources that successfully bid into the capacity auction receive the same availability payments irrespective of whether they are subsequently economically activated in the Energy Market.
- (b) *The Amendment will not place DR resources at a competitive disadvantage in the capacity auction* – The Amendment will not affect DR resources' competitiveness since there is no evidence or reasonable grounds to support AMPCO's claim that some DR resources may have to include Energy Market activation costs in their capacity auction bids in order to protect against the risk of being economically dispatched in the Energy Market. DR resources can manage and eliminate any material risk and cost of activation in the Energy Market by including economic activation costs *in their Energy Market bids*. The only activation costs which DR resources cannot manage or recover through their energy market bids are the potential costs of certain out-of-market emergency and test activations, which DR resources are compensated for through out-of-market payments. As further explained below, the IESO treats DR resources and generators equivalently in this respect by compensating both for out of market start-up or activation costs which they cannot manage through their Energy Market offers/bids.

- (c) *The Amendment will level the playing field* – The Amendment, far from discriminating, will remedy discrimination by opening up the formerly exclusive DR-only DRA to competition by other resources capable of providing the same capacity service. It will also address other system reliability needs and objectives identified by the IESO.

3. Lastly, while DR resources' claimed entitlement to energy payments is a larger market design question that is not the subject of this proceeding, AMPCO has indirectly put this in issue by claiming that it is unjust for the IESO to implement a capacity auction *without first* addressing this matter.¹ In this regard, it is important to make two observations. First, there is nothing inherently discriminatory or unfair in the fact that DR resources do not receive energy payments. There are sound economic and policy reasons why Ontario's Market Design Committee recommended and the government selected a market design which does not pay loads for not consuming energy. Second, while the evidence before the Board is that there is likely not a case for changing Ontario's market design to provide energy payments to DR resources, the IESO is nonetheless undertaking a comprehensive Energy Payments stakeholder engagement and third-party study (**Energy Payments Engagement**) to reconsider the market rules governing energy payments and if this process warrants market design changes, market rule amendments will follow. This is the appropriate forum in which to consider and address the cost/benefit of significant market design changes.

II. LAW

A. Market Rule Review Authority

4. The *Electricity Act, 1998*² confers primary authority on the IESO to make market rules, subject to limited rights to seek Board review. One of the limitations included in section 33(5) of the *Electricity Act* is the prohibition that no person may apply for Board review of a market rule that was made by the Minister of Energy before market opening on May 1, 2002.

5. Section 33(9) of the *Electricity Act* also limits the scope of Board's review of other market rule amendments to consideration of whether the amendment is inconsistent with the purposes of the *Electricity Act* or unjustly discriminatory. Notably, in the earlier *3x Ramp Rate* decision³

¹ AMPCO, Notice of Appeal, September 26, 2019, paras 4, 11, 35, 51.

² *Electricity Act, 1998*, SO 1998, c 15, Sch A.

³ Revised Decision and Reasons, EB-2007 (OEB), April 12, 2007 ("*3x Ramp Rate*").

the Board determined that section 33(9) is “a jurisdiction-limiting provision”, which precludes broader inquiry into the IESO’s rulemaking processes.⁴

6. The Board also confirmed in the *3x Ramp Rate* decision that as with all other applications before the Board the burden of proof is on the applicant, which in this case requires AMPCO to prove on a balance of probabilities that the Amendment unjustly discriminates against DR resources or is inconsistent with the purposes of the *Act*.⁵

B. Criteria for Market Rule Amendment Review

(a) Inconsistency with Purposes of Act

7. The *Electricity Act* contains a number of varied objects; as such, consideration of whether an amendment is inconsistent with the purposes of the Act requires a contextual analysis.⁶

8. A market rule amendment is not inconsistent with the purposes of the Act because it emphasizes certain statutory objects over others. In the *3x Ramp Rate* decision, the Board acknowledged that the impugned amendment might result in a modest increase in consumers bills – which AMPCO argued detracted from the Act’s purpose of protecting the interest of consumers with respect to price – but determined that on balance it furthered other purposes, including promoting economic efficiency, reliability and responsible management of electricity resources.

(b) Unjust Discrimination

9. Determining whether a market rule amendment is unjustly discriminatory turns on several considerations. First, it must ordinarily be shown that similarly situated persons have been treated differently;⁷ it is not discriminatory to treat different persons differently – e.g., generators who supply energy and DR resources which do not. Indeed, many resource types are treated differently in the IESO market based on their unique characteristics and the services they provide.

10. Second, discrimination *per se* is not unlawful; only *unjust* discrimination. Accordingly, determining whether discrimination is “unjust” requires consideration not only of the interests

⁴ *3x Ramp Rate*, Appendix A, Oral Decision (Vice Chair Kaiser), March 29, 2007, at pp 87, 90.

⁵ *3x Ramp Rate*, at p 18.

⁶ *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 SCR 27 at para 21.

⁷ “Complex” Consolidated Edison Co of NY, Inc v FERC, 165 F3d 992, 1012, 334 US App. D.C. 205 (DC Cir 1999); Western Grid Development, LLC, 133 FERC ¶ 61,029 (2010), at para 17.

of the persons complaining of discrimination, but also the legitimate interests of other participants. In this case, it is appropriate to weigh AMPCO's commercial interests in preserving the DRA against the interests of the IESO, consumers, generators and others who support the Amendment on the basis that it will open up competition, promote reliability and lower costs.⁸

11. Third, in "the context of [the Board's] mandate under section 33 of the *Act*, unjust discrimination means unjust *economic discrimination*".⁹ As Bonbright observes, some discrimination is inevitable and the real question is whether the discrimination is efficient or inefficient.¹⁰

12. Lastly, for impugned conduct to be unjustly discriminatory, it must be discriminatory *in effect*, not just in form or theory. Persons complaining of discrimination must adduce evidence proving that the impugned action has had or will have a material discriminatory impact. As the U.S. Supreme Court stated in its seminal decision, *Federal Power Com v. Hope Natural Gas Co.*:

It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end... And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences.¹¹

III. THE AMENDMENT IS NOT UNJUSTLY DISCRIMINATORY

A. There is no *prima facie* discrimination or unfairness in not paying energy payments to DR resources

13. Since inception, Ontario's Energy Market has treated generation and load participants differently – because they are different. Generators supply energy and receive energy payments for doing so. Loads do not supply energy and therefore do not receive energy payments.

14. Nor do load participants receive energy payments for not consuming energy; although, loads which choose to be dispatchable benefit from avoiding energy consumption at or above market prices at which it is not economic to consume and operate – i.e., when the marginal

⁸ *3x Ramp Rate*, at pp. 23, 26.

⁹ *3x Ramp Rate*, at p 26.

¹⁰ James C. Bonbright et al, *Principles of Public Utility Rates* (2nd Ed), (Arlington: Public Utility Report, 1988), pp. 517-518; See *3x Ramp Rate* at pp. 23-26.

¹¹ *Federal Power Commission v Hope Natural Gas Co.*, 320 U.S. 591, at p 602; The United States Supreme Court "reaffirm[ed] these teachings of *Hope Gas*" in *Dusquesne Light Co v Barasch*, 488 US 299, at p 310. See *3x Ramp Rate* at pp. 23, 25.

benefit of consumption exceeds price. Notably, dispatchable loads (DLs) have for many years participated in the Energy Market in the absence of a DRA and entitlement to energy payments. They have done so because they benefit from exposure to Energy Market price signals which allow them to curtail consumption and avoid high prices when it is economic to do so.

15. As Ontario's electricity sector evolves, the IESO is considering changes to certain market design features, including, at the request of AMPCO, conducting a comprehensive Energy Payment Engagement to reconsider the market rules governing energy payments.

16. At present, however, the evidence before the Board – from the IESO, the MSP, Dr. Rivard, LEI and Navigant – does not support energy payments for DR resources:

- (a) The MSP notes that: "A DR resource that is activated saves the spot price on its demand reduction, analogous to a generator being paid the spot price for its production. On this basis, an energy payment to DR resources looks like a double payment. A number of stakeholders appear to be urging the IESO to accept Order 745 as the definitive ruling on this issue, but the Ontario situation is different and we may not share the same objectives as FERC."¹²
- (b) Navigant notes that: "... there is significant disagreement on whether DR resources should receive a utilization payment when they are curtailed [in the Energy Market]" and, in Ontario, the economic efficiency arguments for utilization payments to DR resources are different than in US markets given that "under the current conditions, more DR activation (as a result of bidding into the market at prices lower than traditional generators) would not actually lead to reduced cost to consumers since generators have their compensation guaranteed [under long-term contract or through regulation]".¹³ In other words, any reduction in market price may just be offset by Global Adjustment costs.
- (c) Dr. Rivard says that it would not be cost-effective to pay DR resources energy payments; and, not paying energy payments DR resources is not "leading to any material inefficiencies in the market".¹⁴ Dr. Rivard further notes that even if the FERC net benefit test were applied, it would rarely if ever be met because of the countervailing effect of the Global Adjustment.¹⁵

17. AMPCO has not provided any expert evidence or analysis to the contrary. Other than referencing FERC's Order 745 and its "net benefits" test – which was precipitated by concerns about DR resource participation in wholesale markets (which is not a concern in Ontario) and which LEI, Dr. Rivard, Navigant and the IESO says is inapplicable or is unlikely to show any

¹² Exhibit K1.6, Tab 12, p 1.

¹³ Exhibit K1.6, Tab 8, pp. 6-7, 13-14.

¹⁴ EB-2019-0242, Hearing (November 28, 2019), Vol 2, ("Hearing Transcripts, Vol 2"), p 155.

¹⁵ Revised Affidavit of Brian Rivard, dated November 21, 2019, para 91.

benefit in Ontario¹⁶ – AMPCO has not provided any evidence to show that the absence of energy payments for DR resources in Ontario is unjust.

B. The Amendment does not have any discriminatory impact because it will not put DR Resources at a competitive disadvantage in future capacity auctions

18. DR resources' lack of entitlement to energy payments *in the Energy Market* does not put DR resources at any competitive disadvantage vis-à-vis generators *in the capacity auction*.

19. As AMPCO concedes, the risk and associated cost of activation turns on DR resources' *probability of being activated in the Energy Market*¹⁷ which is solely a function of how DR resources bid into the Energy Market and the Energy Market clearing price; it has nothing to do with how DR resources bid into the capacity auction.

20. The uncontroverted evidence before the Board is that it is entirely within DR resources' control to manage the probability or risk of activation by including any economic activation costs in their Energy Market bids; and if they do this, the risk and associated cost of being activated is remote and immaterial. On this point, the evidence is definitive. Mr. Anderson admits that the risk is a "low probability"¹⁸; the evidence from other witnesses is as follows:

- (a) The IESO notes that DRA participants have rarely been activated because their bid prices are far in excess of HOEP. Since the launch of the DRA in 2015, DL bid prices have averaged \$1500/MWh and HDR bid prices have averaged \$1700/MWh as compared to an average HOEP of \$25/MWh. The IESO does not expect the likelihood of economic dispatch to materially increase.
- (b) The evidence from LEI and Navigant are that DR resources in Ontario and elsewhere manage their activation costs by including these costs in their Energy Market bids and, as a result, are rarely economically activated. Mr. Goulding observed that any material change in the level of DR resource activations would likely require a "perfect storm".¹⁹ Dr. Rivard said much the same.
- (c) The MSP, in a series of reports on the DRA, observed that DR resources have historically managed the risk and cost of activation by bidding high into the Energy Market and there is no reason to expect this to change:

¹⁶ See EB-2019-0242, Hearing (November 25, 2019), Vol 1, p. 134-137 ("Hearing Transcripts, Vol 1"); Interrogatory Response from London Economics International LLC to Kingston Cogen Limited Partnership, No. 2(d) (November 20, 2019); Revised Affidavit of Brian Rivard, dated November 21, 2019, para 91; Exhibit K1.6, Tab 8, pp. 13-14; EB-2019-0242, Hearing (November 29, 2019), Vol 3, pp. 11-14, ("Hearing Transcripts, Vol 3").

¹⁷ Interrogatory Response from AMPCO to Staff No. 3(c) (November 6, 2019).

¹⁸ Hearing Transcripts, Vol 1, p 93.

¹⁹ Hearing Transcripts, Vol 1, p 174.

- “Given the activation criteria..., the likelihood of an activation is remote.... DR resources can bid into the Energy Market at any price between \$100/MWh and \$2000/MWh”²⁰
- “[Since the start of the DRA]... any bid price over \$220/MWh would not have been activated [and since] 2005 and 2006 [when] all-time demand records were being set in Ontario... no bid price above \$1000/MWh would have been activated, yet most HDR resources bid at twice that price.... Even under the most aggressive demand projections peak demand is not expected to return to record 2005 and 2006 levels until 2029”.²¹

21. The IESO’s witnesses, Ms. Trickey and Mr. Short, stated that DR resources can entirely manage any activation costs by including such costs in their Energy Market bids and if they do this, there is no “actual” or “practical risk” of being activated in the Energy Market.²²

22. Dr. Rivard also addressed this issue at length in his written evidence and in his oral testimony. Dr. Rivard testified that DR resources can include their activation costs in their Energy Market bids and if they do so, the risk of activation is “theoretical” and the “material risk of activation is not real”. Dr. Rivard stated that DR resources are not at any competitive disadvantage to generators in an auction and in response to questions from the Panel and counsel answered that:

I would say... not getting an energy payment right now, based on history seeing how often [DR resources] would actually be activated is, in my words, de minimus in expectation, in which case [DR resources could] could offer in that capacity auction exactly the same that they would have had generators not been there. And then let’s see what competition brings about...

... If I was working for that [DR] company, and that is when I said, based on the evidence for this next auction, if I was advising my CEO, I would say we’re not at risk. I can manage that in my energy bid. We will be as competitive as we can in our capacity auction.²³

23. The Panel expressed some concern that there may be some “slice of costs” or some “added cost component that generators don’t have” when activated and which put DR resources at a “disadvantage” vis-à-vis generators who have their start-up cost guaranteed.²⁴ That is not the case. The shut-down costs referenced by Mr. Anderson in his hypothetical

²⁰ Exhibit K1.6, Tab 6, p 100.

²¹ Exhibit K1.6, Tab 6, p 100-101.

²² Hearing Transcripts, Vol 3, pp. 23, 24, 33.

²³ Hearing Transcripts, Vol 2, pp. 191, 196, 198, 207.

²⁴ Hearing Transcripts, Vol 2, p 195; Hearing Transcripts, Vol 3, p 184.

example – e.g., a steel mill that incurs fuel costs to keep steel molten as well as other value of lost load costs – are all activation costs which the hypothetical steel mill customer can include and avoid through its Energy Market bids. The *only* activation costs which DR resources cannot manage or recover through their Energy Market bids are costs of certain out of market activations. However, in this respect, the IESO treats DR resources in the same manner that it treats those generators who cannot recover their start-up costs. As explained below, the IESO compensates DR resources for these otherwise unrecoverable costs through out of market make-whole payments:

- (a) Non-quick start generators – The IESO guarantees start-up costs under its Generator Cost Guarantee Program for a subset of non-quick start generators that start/ramp slowly and may not be able to recover these costs through their Energy Market offers and revenues they earn in the Energy Market.²⁵ These generators may not start/ramp if they do not believe that market prices will be sufficient to recover their start/ramp costs. The IESO therefore, for reliability purposes, launched the GCG Program in 2003 to incent these generators to start and be available when the electricity system needed them by guaranteeing certain start-up costs *if* these costs were not recovered in the Energy Market revenues.
- (b) DL and HDR resources – The IESO likewise compensates DL and HDR resources for out-of-market emergency or test activations. DLs have been entitled to compensation for out-of-market activations. More recently, HDR resources sought compensation for these activations on the basis that they *currently included such costs in their DRA capacity bids*, but circumstances would change in the “proposed capacity auctions, where HDR will be competing against other resource types”.²⁶ The IESO therefore amended the market rules to allow for recovery of these out-of-market emergency and test activation costs on the basis that these costs – like certain start-up costs incurred by non-quick start generators – could not be recovered through HDR resources’ Energy Market bids.

²⁵ For a discussion on the Generator Cost Guarantee Program, see Hearing Transcripts, Vol 3, pp 27-39.

²⁶ AMPCO, Notice of Appeal, Footnote 14, pp. 2-6 of 16.

24. In short, DR resources are treated in the same manner as generators and are not exposed to any Energy Market activation costs that they cannot manage through their Energy Market bids or through make-whole payments for out of market activations.

C. The Amendment will level the playing field, remedy any discrimination and address other important purposes of the Act

25. The Amendment and future capacity auctions will not, as AMPCO contends, discriminate against DR resources. To the contrary, they will remedy discrimination by opening up the DR-only DRA to all resources capable of cost-effectively supplying capacity, including off-contract generators, storage resources and imports.

26. The IESO commenced its capacity auction initiative with the DRA as a first step, in part, to learn how to integrate DR resources into the IESO markets, help remove some of the barriers to participation by DR resources and ready DR resources for a broader capacity auction.

27. DR resources have benefited from an exclusive DRA and some AMPCO members may have a vested commercial interest in preserving a DR-only auction in which they do not have to compete; however, AMPCO's argument that delaying the broadening of the DRA will promote competition is misplaced. DR resources, will be able to compete on a level playing field with all other capacity resources and opening up the auction will enhance competition and deliver the benefits of competition to Ontario electricity consumers.

28. AMPCO, having succeeded on the stay motion, has maintained the DRA and delayed competition for another year (for the period May 1, 2020 to April 30, 2021); but if the IESO is further prevented from proceeding with a capacity auction, it will have to consider other options for addressing the significant capacity gap starting in 2023. These include re-contracting with generators and other supply resources, which are less competitive and less cost-effective solutions, and ultimately, will not benefit Ontario electricity consumers.

29. Determining whether the Amendment is *unjustly* discriminatory requires consideration of not only AMPCO's members' commercial interest, but of the IESO's statutory objects and the legitimate interests of other electricity sector participants. In this case, the IESO, which is statutorily responsible for maintaining system reliability and administering Ontario's wholesale markets, has given evidence that there are, in addition to the benefits of opening up competition, important system reliability reasons for proceeding with a capacity auction. The IESO's evidence, which has not been seriously challenged, should be given due weight. The

interests of the majority of consumers, whose representatives on the IESO's Technical Panel voted in favour of the Amendment and want the capacity auction to proceed, also warrant consideration, as do the competing commercial interests of KCLP, APPrO and other generators – who to date have not had an equal opportunity to compete to supply capacity.

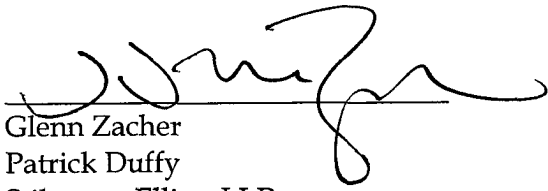
D. The Amendment itself is not alleged to be discriminatory

30. Lastly, AMPCO does not allege that there is anything discriminatory in the Amendment itself. Instead, AMPCO argues that the Amendment has simply made more acute AMPCO's long-standing complaint that load resources are inequitably treated in the Energy Market.

31. AMPCO's position raises an important jurisdictional issue. By asking the Board to revoke the Amendment – which in and of itself AMPCO has no objection to – and thereby prevent the IESO from proceeding with a capacity auction *until* the original market rules governing energy payments are amended, AMPCO is, in effect, challenging government-made market rules which the *Electricity Act* expressly prohibits AMPCO from challenging.

32. For all of the reasons stated herein, the IESO respectfully submits that AMPCO's application to revoke the Amendment should be dismissed and the IESO should be permitted to proceed with its planned capacity auction.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 9th day of December 2019.


Glenn Zacher
Patrick Duffy
Stikeman Elliott LLP