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Independent Electricity  
System Operator  
655 Bay Street  
Suite 410, PO Box 1  
Toronto, Ontario M5G 2K4  
t 416 506 2800  
www.ieso.ca

# Memorandum

To: THE BOARD OF DIRECTORS  
of the Independent Electricity System Operator

From: Bruce B. Campbell  
Vice President – Corporate Relations & Market Development

Date: December 11, 2007

Re: Update re Day-Ahead Electricity Market

At the December 5<sup>th</sup> meeting of the Stakeholder Advisory Committee there was a presentation by the IESO and a subsequent discussion regarding the status of the IESO staff effort on improved day-ahead mechanisms. SAC members were asked whether they agreed that the IESO and stakeholders should continue with their investigation of the unconstrained day-ahead market (UDAM, Option 3) on a timeline that results in providing the Board with a recommendation in June.

Chair of SAC, Brian Bentz put this question to the Committee. There was consensus from SAC members that we should move forward with our day-ahead market investigation according to the revised timeline. However the Chair noted that there were "varying degrees of enthusiasm about going to the next stage". These are summarized on the attachment to this memo.

Given the Board representation at the SAC meeting, I am proposing that at tomorrow's Board meeting, we would respond to questions following a much truncated presentation from Ken Kozlik.

A handwritten signature in black ink, appearing to read "Bruce B. Campbell".

for: Bruce B. Campbell  
Attach.

Bruce B. Campbell  
Vice President  
Corporate Relations &  
Market Development  
bruce.campbell@ieso.ca  
d 416 506 2829  
f 416 506 2804

# IESO Stakeholder Advisory Committee

**To:** IESO Board of Directors

**DATE:** December 12, 2007

**FROM:** Stakeholder Advisory Advice on Day-Ahead Electricity Market (December 5, 2007 meeting)

This memorandum is to advise the IESO Board of Directors that the Stakeholder Advisory Committee has considered the recommendations for the evolution of the day-ahead electricity market. The Committee supported the recommendations for the IESO to continue with the analysis of the unconstrained day-ahead market (UDAM) design. Below is a summary of the comments offered by Committee members in providing their support.

**Advisory Committee Members in Attendance:**

Mr. Brian Bentz, Chair (representing Distributors)  
Mr. Bruce Campbell (representing IESO)  
Ms. Julie Girvan (representing Residential Consumers)  
Mr. Richard Horrobin (representing Generators)  
Mr. Mike Humphries (representing Embedded Industrial Consumers)  
Mr. Bruce Lourie (representing Environmental)  
Mr. Paul McMillan (representing Marketers/Brokers)  
Mr. Doug Reeves (representing Distributors)  
Mr. Chuck Stradling (representing Commercial Consumers)  
Mr. Adam White (representing Wholesale Consumer Market Participants)  
Mr. Gary Wight (representing Marketers/Brokers)  
Mr. John Witjes (representing: Public Service Consumers)

**Advisory Committee Members Absent:**

Mr. Steve Dorey (representing Transmitters)  
Mr. Daniel Whyte (representing Generators)

**Summary of Stakeholder Advisory Committee Input:**

Mr. Kozlik asked for feedback from the Committee on whether the IESO should continue its further study and focused attention on an Unconstrained Day-Ahead Market (UDAM) design, noting that to do so would require significant effort by both stakeholders and the IESO.

Mr. Humphries remarked that his constituents focus on what the end result will be and at this time they are not sure that the end is worth going through the process. He also noted that a red flag for his constituents is the comment that an effective day-ahead mechanism requires adjusting industry arrangements such as centrally held contracts and regulation of OPG assets.

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Mr. Humphries provided a personal perspective. He said that until you have the interval meter, additional DAM demand response benefits cannot be realized. With the information available now, those who wished could achieve about 90% of demand response benefits without a DAM.

Mr. Bentz questioned how a day-ahead market price would incent demand response/load reduction on mass consumers, RPP consumers, a default supply consumer or a consumer who has a retailer. Mr. Kozlik said that a day-ahead market helps those 50-60,000 accounts, which represent 50 to 55% of consumption, that are charged the hourly energy price. He acknowledged that time of use will be a key driver of demand response in relation to the regulated price plan.

Mr. Reeves asked how generators who have Ontario Power Authority (OPA) contracts would participate in the day-ahead market. Mr. Kozlik stated that the clean energy supply (CES), early mover and, he believed, the combined heat and power (CHP) contracts are conducive to responding to market signals. Certain other contracts being held by the OPA are somewhat removed from market drivers. The challenge will be to figure out how facilities under these other contracts will present themselves to the DAM and keep similar financial and risk allocation arrangements.

In relation to considering the design for DAM Mr. Lourie asked whether demand response would be primarily a passive response or whether there are things that would be done in the DAM design to facilitate demand response. Mr. Kozlik stated that when it comes to design of the DAM, the purpose is to make the right market signals available and we are working with the OPA so they can use the market drivers to design them into demand response programs, while providing a financial hedge day-ahead and encouraging response to real time prices.

Based on the presentation Ms. Girvan agreed that further study is required before a decision is made. She also enquired whether the \$16 million cost referenced in the presentation is for the full implementation of a DAM and also enquired about the costs for the continued investigation of UDAM over the next 6 months. Mr. Kozlik stated the \$16 million was based on quotes to build the 2004 design of DAM, and only included IESO costs and not the costs to participants to make the changes in their organization. The costs to study DAM over the next six months include IESO staff resources as well as stakeholders costs to continue to be part of the investigation.

Ms. Girvan noted that the presentation identified concern by generators under contract as well as consumers. Mr. Kozlik confirmed that it is necessary to work OPG and Bruce Power generation into the DAM, and that the "consumer concern" referred to large consumers.

Ms. Girvan does not see the harm in the IESO preparing a price forecast; it would just be another tool to help people participate in the market.

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Mr. Bentz asked about the connection between DAM and load-serving entities and whether DAM could survive on its own without market evolution occurring. Mr. Kozlik responded that the DAM design was built with the idea that the IESO would provide the DAM a forecast of default demand. If load-serving entities develop they would take on the role of forecasting default demand. If load-serving entities do not materialize, the system can continue to operate with the IESO forecasting the default demand but the market will not be as effective.

Mr. White commented that in a proper market in addition to demand response, consumers will manage their own consumption and/or purchase hedge products. He noted that Ontario lacks an active secondary market for hedge products. He also noted that not all demand response represents a success, reflecting instead adverse economic impacts. Ultimately the question is whether the options being offered will be of benefit to consumers who have some operational flexibility. At present we lack the detail to assess the consequences of the ability to lock in price day-ahead, which is critical to understanding whether a DAM is an improvement. He is not opposed to further study but the further study could look at different iterations of Option 3 (mandatory or optional participation). In the alternative, there should be a reference for the specification of the day-ahead market that assumes the real world with no contracts, regulations and all consumers represented on an active basis. Mr. Kozlik confirmed that the intent of the DAM is to give consumers more tools and that the IESO does not consider demand response to include demand destruction. Mr. White clarified that in order to understand the dynamics day-ahead and in the real-time market, there needs to be an understanding of who is going to participate in the market, as well as the balance between the DAM and real-time balancing market. His constituents are willing to tolerate further study but require specifics on the value of UDAM sooner rather than later.

Mr. Horrobin acknowledged the IESO's work to date and commented that the revised schedule is appropriate given the need to continue to do further work and analyze the impact of the day-ahead proposals. It is equally important, however, that work continue on the real-time pricing issues. Mr. Horrobin asked for the implementation date because they are looking at the associated system costs. Mr. Kozlik responded that a high level expectation of the implementation date, if a DAM is approved, is the end of 2009.

Mr. Wight said that the marketer/broker community believes that the DAM is a necessary tool and platform in the market evolution process and commented on the intangible benefits of a DAM as a tool to manage risk and obtain value from the interties. These linkages need to be considered. He commented favourably on the significant effort by the IESO to stakeholder and study the issue.

Mr. MacMillan stated that the trader community supports the day-ahead market. It must be acknowledged that there is imperfect information; the real question is whether

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there is a reasonable assessment. Mr. MacMillan said that you need to assess where the industry is headed, consider components embedded in the price such as the global adjustment and uplift, as well as the future generation mix, and contract integrity impacts on investment in infrastructure. The economic assessment requires knowledge of where the industry will end up. He supports the revised schedule to allow for appropriate study and consideration.

Mr. Witjes commented that having a more accurate representation of the day-ahead price would be very advantageous for the public service sector consumers running cogeneration facilities for economic benefit.

Mr. Bentz summarized that he was hearing a desire to continue with further analysis of UDAM

DRAFT