Wholesale Consumer, Adam White

March 2, 2011 Sector Priorities

MR. A. WHITE: I am going to start with the caveat that the views that I am going to express are largely focused on economic issues. I don't want to take away, at all, from the IESO's critical role regarding reliability. It's just that I don't know if we take it for granted, but we expect that there will be issues and we'll deal with those issues as they arise. But from the perspective of the organization that I operate and the industrial customers with whom I interact, most of the things I hear and the issues that I am charged with transmitting to the sector really are economic.

And we start with two broadly defined priorities. One is cost control, and this is something we've been doing forever: trying to ensure, in everything that is done in this sector, that customers' needs are being met in a way that is least costly and/or most cost-effective.

The second priority relates to efficiency. So really, what we are talking about in terms of efficiency is the design and operation of the markets, price discovery, and extending the benefits of market participation to larger numbers of relatively smaller customers.

The other part of efficiency deals with regulation, which typically is rate design. The first part - market design and operation and price discovery - really is the bailiwick of the IESO. And here, we are talking about two issues: one has to do with the size of the pie; the other has to do with how that pie is sliced.

What's important to industrial customers is the delivered cost of power over time. And there's obviously been a lot of concern over the last couple of years, in particular, about the rapid rate of escalation. We are working on our longer-term outlook now and I am pretty sure that that's going to generate a lot of additional concern about future rates of escalation for the delivered price of power.

HOEP, as it's currently designed, is likely to be less and less important over time. I defend the Hourly Ontario Energy Price and the IESO's operation of the wholesale power market. I think that the HOEP provides a reasonable proxy of the marginal cost of energy in the electricity market, but because of the two schedule system, i.e., the HOEP is the product of an unconstrained run, the HOEP is going to be a less important signal of what's happening in the market.

It's my view that wholesale market service charges are going to be where the more interesting economic signals exist or don't. In particular—referring to the IESO's activities related to renewable integration—I think we have the potential to see some fairly significant incremental costs related to congestion management and losses because of the way the grid is evolving and the way the supply mix is evolving. For almost all customers in Ontario, the wholesale market service costs are shown to them on their bill as an average, an average which really doesn't vary, at all, even though the underlying costs vary significantly and dynamically in real time. What's interesting about this is that the pricing issues that are most important really are at the frontiers of the market: during critical peak periods, during surplus baseload periods, and during periods when the market is experiencing high rates of ramping. This is where the HOEP perhaps either isn't doing the job it could do or can't do the job that price signals that are meaningful to consumers need to do.

We have been taking our case to the Ontario Energy Board since 1999, without much luck, talking to the OEB about the portion of the bill over which it has oversight and the importance of the decisions that the Board makes in terms of making rates intuitive and meaningful to customers. Current electricity bills are non-intuitive and perplexing to most customers. All they can see is the bottom line and it goes up in ways that they can't understand.

In summary, the design of markets continues to be important to industrial consumers. I emphasize the plural because it's not just the wholesale market for power, but there are opportunities to expand the definition of markets for ancillary services, in particular, to meet the challenges associated with dispatchability of new renewables and to allow customers to play the role that they are capable of playing in that.

Well-designed markets can create meaningful opportunities for customers to benefit. Well-designed markets accurately signal to customers the costs of serving them. There are opportunities in Ontario to improve the accuracy of price signals, both geographically and in time. Good market design and good prices and rates appropriately reward good behaviour—to promote more efficient demand management—and will effectively inform and engage customers in opportunities for more efficient demand management. All of these things are among the purposes of Ontario’s legislative framework. None of these things have any priority in the business plans, it seems to me, of the agencies which are creatures of that legislation.

I will make a comment on Global Adjustment just because it's come up a couple of times. The assumption that it's a zero sum gain is false. If it's not a zero sum gain, then it's a more interesting policy initiative. We are working on the business case and policy road map to extend proper price signals to more customers. We have to do this in a way that's logistically possible. As much as the IESO worked hard and well (and I tried to help over the last two or three months to engage large users in the new regulation), we must not underestimate the challenges of extending that to the next customer tier. We are talking about orders of magnitude greater numbers of customers and an order of magnitude less engagement in the market and less awareness of market dynamics. It's going to be much more complicated to extend good pricing to customers, especially as we move line by line down the bill. If there was a way to coordinate that work—to coordinate the efforts of the various regulatory agencies—it could be made simpler.

I will close by saying with the application of digital technology to the grid, smart meters, and what's called a "smart grid", technology no longer is the barrier to good market design, and effective customer participation in those markets. We must reach through the arbitrary barrier which is the LDC service franchise, and engage more smaller customers in the market, to allow those customers to benefit from participating in the market.

It isn't as if we don't understand the policy opportunity, it isn't because we don't have the technology in place; the real impediments now to moving forward are institutional. This says to me is that there are opportunities to revisit the mandate, governance and structure of the regulated and regulatory side of the sector, and there are obvious opportunities for rationalization that we'll be carefully exploring over the next 12 to 18 months. I will say, though, that we do see an ongoing critical role for the IESO and its functions and there are some opportunities, I think, for the IESO to expand on the good work it does.