

Howard I. Wetston, Q.C.

Chair

Ontario Energy Board

SPEECH

APPrO Annual Conference

November 21, 2005

Check against Delivery

Good morning.

It's great to be with you this morning and to help kick off this very important conference.

The last time I was here I had only been Chair of the OEB for about six months. Since then, in almost two years, we have made a lot of changes - in governance, in how we operate and in how we carry out our regulatory responsibilities.

As a result, the OEB is much better prepared to respond quickly to developments in government policy in both the electricity and gas sectors and to anticipate areas where action might be required.

But while much has changed, our basic goals have not - to provide fair, transparent and effective regulation and to strike the right balance between consumer protection and the financial viability of utilities.

While the Board certainly has greater authority over transmission and distribution than over generation, in the last two years we have been given an increasing role in certain aspects of generation, both directly and indirectly.

For example, we have been given responsibility for:

1. Developing the Regulated Price Plan
2. The Market Surveillance Panel
3. Market rule amendments of the Independent Electricity System Operator – or IESO
4. Licensing the Ontario Power Authority and approving its budget
5. Approving the Integrated Power System Plan and procurement process of the OPA
6. OPA contract procurement approval where there is no ministerial directive

Beginning in 2008, the OEB will also regulate Ontario Power Generation's base load generation assets.

And because we do have an increasing role with respect to certain aspects of generation, I thought I would discuss this morning some of the main issues facing all of us over the next few years.

I'd like to focus on six key areas:

- The Integrated Power System Plan
- The Minister's Directive on Coal Displacement or Early Movers
- The Standard Offer Contracts
- Our Natural Gas-Electricity Interface Review
- The future Electricity Reliability Organization (ERO)
- The Transmission System Code

Let me begin with the Integrated Power System Plan - the IPSP.

While the government had a number of objectives in creating the OPA, significant ones were power system planning and securing adequate supply for Ontario.

As the summer of 2005 made clear, electricity supply is at a low level in Ontario. This, combined with rising energy prices, environmental concerns and the time required for new power plants to be built, makes a comprehensive power system plan critical.

To achieve its goals related to adequacy and reliability of supply, the Plan might focus on the effective management of electricity supply, transmission, capacity and demand – including alternative and renewable supply – as well as demand management.

Quite simply, the government sets the overarching goals and the OPA develops a plan to meet them. The government may also issue a directive which sets out specific objectives relating to fuel mix and a number of other matters. In those cases, the plan also aims to meet those objectives.

Our role is to review the plan to determine if it actually meets the government's goals and whether it does so in a way, and this is important, that is both economically prudent and cost effective.

Following our review, the Board may approve the IPSP or send it back to the OPA for further consideration. Once the IPSP is approved, our role is to facilitate its implementation.

In this regard, the OPA will seek the Board's approval for the process by which it plans to procure electricity supply, ensure capacity and guide demand management.

Once this process is approved by the Board, the OPA can then enter into procurement contracts. And any costs incurred under those contracts are recoverable by the OPA without further regulatory review.

While any IPSP obviously begins with legislation – and our review criteria is determined by that – there are also some criteria that may emerge when it comes to seeking economically prudent and cost effective implementation of the plan. These will include tradeoffs among transmission, generation and demand management.

It is important that the IPSP be considered in a transparent and public way and we are thinking about how we can develop a process that gives the OPA and the public greater certainty about the criteria that we will use at the Board in reviewing the plan. We are also considering the pre and post public filing

processes of the IPSP to ensure openness and efficiency. That is only fair to the OPA and only fair to other stakeholders who are interested in the plan.

As you know, the government's energy policy includes taking coal-fired generation out of service and some actions have already been taken to help meet the 2009 target.

I mention this because it brings me to the second area of Board involvement regarding generation and that is the Minister's Directive to the OPA to enter into contracts with generators to displace coal fired generation. These are the early mover contracts.

All told, some seven generators are involved - one combined cycle, five cogeneration plants and one hydro electric plant.

The contracts are subject to the approval of the Board and must meet certain threshold tests set out in the Minister's directive.

One of the key tests is that the contracts must be at reasonable cost. In determining what's reasonable, the directive states that, and I quote, "... reference should be had to the economic value associated with the Clean Energy Supply contracts". Close quote.

Now the Clean Energy Supply contracts contemplate dispatching gas fired generation when gas prices make it economic to do. So, it will be up to the OPA to demonstrate how the economic value of the two types of contracts should be compared.

We are about to issue interpretative guidelines to provide the Board's interpretation of these requirements under the Directive.

With a December 15th target date for the OPA to negotiate these early mover contracts, there is obviously no time to be wasted.

Once filed, and in keeping with our commitment to greater openness, the contracts will be reviewed in a transparent, public process.

Let me turn now to the Standard Offers, the third key area of generation where the OEB has a role to play.

Standard offer contracts, of course, are an alternative to the competitive procurement process which can place a real financial burden on smaller generators.

As you know, the Minister of Energy has asked the Board and the OPA to work together to develop the terms and conditions of a standard offer program for small generators that use clean or renewable resources.

The OPA is developing the pricing model for the power purchased under such a contract, while at the OEB, we are working on guidelines for small generators to connect to electricity distribution systems. The OPA and the Board have issued discussion papers – and I'd encourage you to have a look at them.

At the OEB, we want to make sure that administrative barriers don't exclude these smaller generators from playing a role in enhancing the diversification of Ontario's sources of electricity.

We want to make connection processes as simple and timely as possible while protecting the integrity of the system and the safety of those working on it.

To that end, we are examining the technical standards governing interconnection to remove points of dispute between distributors and generators. We are looking at requiring distributors to make available detailed information about their systems to aid design and comparison of alternatives.

We are also developing template connection agreements for plants up to 10 MW to let small developers know what obligations are standard in order to reduce the need for negotiation.

And we are looking at issues surrounding distribution rates, including the use of standby charges, rate classes for fixed charges and allocation of connection costs.

With all of these efforts, we are trying to simplify and streamline the process for small generators, minimize the licensing procedures and enable them to play their part in helping to diversify Ontario's sources of electricity.

Let me turn now to the fourth area that affects primarily the larger generators and that's the interface between natural gas and electricity.

At the Board, we recognized that this was going to be a critical issue as Ontario moves away from coal-fired generation toward more gas-fired generation.

And so, earlier this year, we initiated the Natural Gas-Electricity Interface Review. This Review is looking at issues surrounding the anticipated expansion of the natural gas network in Ontario to serve the growth in gas-fired generation.

In particular, it explores the need for the expansion of the gas storage and transportation network, identifies issues associated with the allocation of costs of paying for this infrastructure and examines whether new rates need to be established to serve the needs of gas-fired generators.

It so happens that a comprehensive study prepared by our staff is due to be released today and I would like to give you a preview of its main conclusions and next steps.

Board staff concluded that while significant new gas infrastructure is going to be needed in the next few years, the current process used to allocate costs for infrastructure investment is satisfactory and need not be addressed in a generic hearing.

Indeed, the analysis suggests there is no qualitative difference between previous infrastructure expansions and those that will be needed over the next few years. As a result, staff recommended that the Board continue to review facilities on a case by case basis and that the Board avoid being seen as the “central planner” of the gas system.

The study reached quite a different conclusion with respect to the impact of an expanded system on rates and services. In this case, aided by submissions received from APPrO among others, it was felt that the need for operational flexibility on the part of the new generators will require new rates.

Specifically, it is recommended that Union Gas Limited and Enbridge Gas Distribution file proposed rates that would feature hourly nominations for distribution, storage and transportation and firm high deliverability from storage.

The hourly services would aid generators in balancing their potentially volatile daily requirements.

But these hourly services will work best if they are coordinated with hourly services on upstream capacity. The study therefore urges the Board to encourage the major pipelines - TransCanada Pipelines and Vector Pipelines - to file proposals for competing or complementary hourly services.

Now in addition to developing rates that give generators more flexibility, the study also recommends that the Board address the following three issues – all of which were raised in discussions with stakeholders and generators:

- the movement of gas interfranchise;
- the ability to redirect gas at short notice to another delivery point; and
- title transfers of gas in storage.

Finally, recognizing the critical role that storage will play in serving the new generators, the study recommends that the above issues be considered as part of the upcoming proceeding on storage.

This storage proceeding will examine whether economic regulation of natural gas storage will continue or whether there is sufficient competition in storage so that the Board can forbear from regulating it.

We will be inviting comments on the Natural Gas-Electricity Interface Review in the coming weeks. Once that feedback is received and reviewed, we will be considering a Procedural Order which will set out the issues and information requirements for the proceeding. I expect that proceeding to begin during the first calendar quarter of 2006.

Now moving to the fifth point where the OEB will be involved – I will talk about the reliability of the supply of electricity.

As you know, Ontario is highly interconnected with the United States. As the 2003 blackout made clear, the reliable operation of our system is dependent on reliable operation by our neighbours.

While we all aim to operate based on standards developed by the North American Electric Reliability Council – or NERC - compliance with these standards is voluntary in most jurisdictions.

That's not true here in Ontario where we have had a system of mandatory compliance with NERC reliability standards. Moreover, any changes to those standards are incorporated into the market rules.

Compliance with and enforcement of these standards is largely done by the IESO. However the Board also has a role, as we are the appeal body for certain IESO orders made under the Market Rules, including orders imposing financial penalties in excess of \$10,000.

The 2003 blackout has caused the U.S. to also move towards mandatory compliance with reliability standards. In fact, the U.S. Energy Policy Act calls for the creation of a self-regulatory organization - the Electric Reliability Organization which is expected to be NERC's successor to oversee electric reliability in the US and ultimately across North America. This will be under the umbrella of the Federal Energy Regulatory Commission or FERC.

So where are we in the process?

It is expected that the ERO will be recognized by next summer, meaning that from that point forward, the US will also be operating under mandatory – and enforceable – reliability standards.

One of the requirements of the ERO is that it obtain recognition from Canadian jurisdictions. In Ontario, the Electricity Act already recognizes NERC and its successor (i.e., the ERO) as the electric reliability standards authority.

In other words, we should have fewer problems for recognition in Ontario.

But recognition not only involves establishing a bilateral relationship between us and the ERO. It also means co-ordination among provincial regulators and we are working with other provincial regulators to increase awareness and co-ordination of our activities in this area.

The Board is also participating in key NERC committees and has for the past few years _ which give us a good appreciation of the issues involved in the transition to the ERO. In this regard we work very closely with the IESO which has been very supportive of our role with NERC.

Now, just before closing I want to touch on one other issue and that's the Transmission System Code or TSC.

As you know, the Code sets out the obligations of electricity transmitters with respect to their customers, including how the costs of a new generation connection are allocated. I mention the TSC because a number of recent changes should enable new supply or conservation initiatives.

As you know, we have had responsibility for the TSC as well as the Distribution System Code, or DSC, since they went into effect in May, 2002.

These two codes were developed within a short time frame for market opening and were very much based on the "old" model which focused primarily on large generators connecting to the transmission system.

Soon after market opening, a number of concerns were raised by stakeholders regarding the TSC, among them the inclusion by the transmitters of a "no bypass" clause in agreements before a customer could receive service.

We have reviewed the TSC and made a number of important amendments aimed at reducing barriers and enhancing certainty for new generation.

In particular, we have revised the TSC to better recognize the opportunity for increased distributed generation in Ontario. For example, we have developed a more comprehensive definition of embedded generation which clarifies what is – and is not - bypass.

The revised code now provides that any new generation that is connected on the customer side will be considered embedded – that is, not bypass. This will be the case regardless of the ownership or location of the generation, the voltage level, the size of the generation capacity or the number of generating units.

APPPrO and others provided some very useful input in arriving at this definition of embedded generation. We thank you for your submission.

We have also revised the TSC to clearly prohibit a transmitter from continuing to place construction work on hold pending the outcome of a dispute.

Those are just two of several changes that we have made to the Code. We revised the TSC to expedite a fair and non-discriminatory connection and our Compliance Office stands ready to help you get connected in as efficient and timely a manner as possible.

I should also add that we will continue to review our codes to identify and eliminate any remaining barriers that may exist.

That, in some detail, is a picture of how the OEB will intersect with the generation community.

We will soon be circulating our proposed business plan for 2006 to 2008. And I can tell you that one of our core objectives will continue to be To Help Meet Ontario's Challenges for The Renewal of Its Energy Infrastructure and Supply.

Our vision of strong economic regulation includes fostering a healthy energy sector.

That means maintaining the two pillars I talked about earlier: first, investors and shareholders must feel confident in their ability to obtain a fair return for their significant financial commitment.

And second, Ontarians must feel confident that their energy needs are being met in the most cost-effective and environmentally responsible manner - that the charges they pay represent prudently incurred expenses and that they have the information and tools they need to manage their costs.

So, in the days and months that lie ahead, new generation will play a key role in meeting the energy needs of this province. There are changes coming. As David Butters notes in your conference materials, the scope of the challenge before you is enormous, the opportunity unprecedented.

At the OEB, we understand those challenges. We know the unprecedented pace of change. And we are working hard to help you manage that change in a way that both serves our province and sustains your industry.

I look forward to working with all of you as we pursue those goals together.

Thank you.