

Memorandum

To: Technical Panel

From: John MacKenzie, Market Rules

Date: November 13, 2008

Re: MR-00338: Economic Dispatch of Linked Wheel Transactions

Attached are the following three documents from the MR-00338 Working Group for Technical Panel information and consideration:

- Current draft design proposal for Economic Dispatch of Linked Wheels (IESOTP 219-2b);
- Draft description of the benefits of economic dispatch of linked wheels (IESOTP 219-2c); and
- Description of IESO-identified issues with respect to the proposed design (IESPTP 219-2d).

Background Information

During the discussion of MR-00338 at its meeting on July 8th, 2008, the Panel requested that “a small group of members from the Inter-Jurisdictional Trading Standing Committee and IESO staff address the design issues and finalize the potential design. The Panel would then review the proposed product from its broader perspective.”

The Working Group was formed in August 2008 with representatives from the following companies:

- i) Brookfield Power
- ii) Constellation Energy
- iii) Hydro Quebec Energy Markets
- iv) IESO
- v) Ontario Power Generation
- vi) Powerex
- vii) Silverhill

The Working Group has met 5 times through September October and November. The Working Group targeted to have a recommended design for the Panel by the end of October 2008.

Status of Proposed Design

The Working Group has developed and considered various design options and features to address the financial risks faced by intertie traders conducting linked wheels through Ontario. Of the various design options and features considered, the stakeholder members of the Working Group believe that the draft design described in the attached IESOTP 219-2b document best addresses those financial risks.

In summary, the design would have linked wheels physically scheduled and settled on the basis of the difference between the 'sink' intertie zone price and the 'source' intertie zone price as determined in the pre-dispatch constrained sequence. This would, in effect, provide a form of locational pricing for linked wheel transactions. The estimated IESO implementation costs for the draft design is approximately 1 million\$.

The Working Group is not in a position to make a recommendation to the Panel at this time because of the outstanding design issues (refer to document IESOTP 219-2d). The Working Group intends to further explore these issues with the goal of resolving them and returning to the Panel with a recommendation in the first quarter of 2009.

Stakeholders on the Working Group have strongly asserted that maintaining the status quo with respect to the significant financial risks that intertie traders are forced to assume when conducting linked wheels through Ontario is unacceptable. Traders are not forced to assume such risks in other markets.

Assessment

In the Working Group proposal, the efficiency benefit to the Ontario market identified is that any distortion in the intertie zone prices caused by the existing 'price taker' requirement for linked wheels would be lessened or removed. This would result because under the proposed pricing rules, linked wheels would be less likely to contribute to congestion at the interties insofar as linked wheel transactions would not be scheduled if there are other market participants who are willing to pay more for an export from Ontario or offer energy into Ontario at a lower price. The result would be intertie zonal prices that more accurately reflect the true cost of trading opportunities at the interties.

The IESO agrees that the proposed design would, in principle, result in more efficient scheduling of transactions on the interties. There may also be consequential efficiency gains in the dispatch of internal resources if intertie transactions are more efficiently scheduled.

However the IESO sees significant challenges in moving forward with the design proposal. Some of those challenges are articulated in the IESOTP 219-2d, and those issues arise from the integration of the proposed linked wheel design into the existing Ontario market design. Other challenges include:

- Quantification of the expected efficiency benefits to justify the expected costs of implementation;
- Integration into the ongoing EDAC design;

- IESO and stakeholder resource availability and expertise to undertake further analysis to address the identified design issues and quantification of benefits.

On one specific point in the IESOTP 219-2c document, it is suggested that the IESO's existing linked wheel requirements are at odds with FERC Order 888. We believe this suggestion to be incorrect as the Ontario market rules have been found by FERC on two occasions to be functionally equivalent to the pro forma tariff approved by FERC in Order 888.

In summary, we believe that significant work remains in developing the proposed design and seek Panel feedback on the merits of undertaking that work and priority that work should have relative to other market rule amendments.

Yours truly,

John MacKenzie

Attach.