Energy Marketing
A subsidiary of Hydro-Québec

April 19, 2012

Mr. David Robitaille
Section Head - Operational Analysis
Independent Electricity System Operator

Subject: IJTSC April 12, 2012 Meeting - Comments of HQ Energy Marketing Inc.

Dear Sir:

HQ Energy Marketing Inc. ("HQEM") welcomes this opportunity to submit its comments regarding the proposed rule on the treatment of export transactions out of the Independent Electricity System Operator ("IESO") market. HQEM participated at the April 12th Inter-Jurisdictional Trading Standing Committee ("IJTSC") meeting and hereby wishes to elaborate on its position.

HQEM generally favours stability in market rules and is a proponent of market-based solutions to issues facing the IESO market. The proposed rule, forcing negative export settlement prices to 0$, departs from this stability and leaves a number of issues unanswered.

The proposed rule would introduce a discrepancy between the financial and physical energy markets, undermining external market participants' ability to hedge their export transactions during negative price periods. Financial products such as financial swaps are typically indexed to market prices. As this proposed rule would be accounted for in the market participants' settlements and not in the market prices, external market participants will no longer be able to hedge their export transactions with physical flows when the market price is negative. It will undoubtedly introduce more uncertainty and render export transactions less attractive. As was discussed at the last IJTSC meeting, the proposed rule could also have an indirect impact on the transmission rights ("TR") value, which would need to be assessed by the IESO. Moreover, HQEM has a hard time understanding how introducing a constraint to exports wouldn't emphasize Surplus Baseload Generation ("SBG") conditions in Ontario, particularly as neighboring markets do not impose such a constraint.

An increased reliance on nuclear manoeuvres could also lead to market uncertainty, as higher-than-forecasted demand, coupled with reduced supply have caused price volatility in the past[1]. Finally, considering the other issues highlighted by traders at the IJTSC meeting, the net impact of this measure on the Ontario market is highly uncertain, and should be assessed more thoroughly by the IESO before moving forward.

[1] See for example the April 5, 2012 *IESO Bulletin*, March 2012 Pricing Events.

Market-based solutions in replacement to the proposed rule

To more effectively manage the forecasted SBG conditions and associated negative prices, the IESO could explore market-based solutions instead of adopting the proposed rule. One of those solutions could be to add a bid-based price guarantee for real-time exports during forecasted SBG periods. A complementary approach would be to enter into agreements with neighboring jurisdictions to implement higher-frequency scheduling, which could be implemented within a few months and could prove more economic than actual SBG-management products. New ancillary services, tailored for IESO needs, could also be developed.

Taking into account the operational issues facing the IESO, HQEM believes a proactive approach in developing market-based solutions would prove to be most efficient for Ontario. It would also limit the occurrence of *ad hoc* amendments to market rules and import transaction curtailments[2], both of which introduce uncertainty in the market.

Provided the IESO nevertheless moves on with the proposed rule after a thorough assessment of its impacts (and notably the TR and financial market impacts), HQEM would ask that exporters' costs such as the Export Transmission Service Tariff and Uplift Charges be taken into account in the related settlement calculation. In particular, Uplift Charges could be adapted to compensate market participants for relieving surplus generation in Ontario. A new bid-based price guarantee for real-time exports, as explained above, could also be considered. Finally, HQEM would also request that Implied Wheels be excluded from this measure, for the same reasons Linked Wheels are proposed to be.

Best regards,

Matthieu Plante
Manager, Regulatory Affairs, HQEM

[2] The IESO tends to curtail import transactions during SBG conditions, whether or not those import transactions are economic relative to internal generators. Further, while doing so, the import transactions are removed from the unconstrained schedule. It should be noted that the Market Surveillance Panel has already recommended the IESO not to remove those transactions from the unconstrained schedule (see *Market Surveillance Panel Report*, May 2010 - October 2010, Chapter 3, section 2.2).