

Intelligence MEMOS



From: Benjamin Dachis

To: Ontario Electricity Watchers

Date: November 15, 2021

Re: **ONTARIO GOVERNMENT SHUTTING DOWN THE ELECTRICITY PRICE CASINO**

Early this month, the Ontario government [quietly announced](#) plans to create a pilot “interruptible rate” for large industrial electricity customers. This is good news for customers and for a system that needs to rationalize its pricing regime.

The crux of the issue is how to pay for the cost of energy contracts. Over a decade ago, the government created the Global Adjustment (GA) to cover the cost of fixed-price contracts. It started small, but the Global Adjustment now makes up 60 percent of electricity bills in the province as the Ontario Independent Electricity System Operator (IESO) covers the gap between hourly market prices and the costs of generation from nuclear, wind and all the other sources for Ontario’s grid.

Households and small businesses only see the GA buried as part of their monthly bills, but for thousands of industrial and large commercial users it has become a nightmare.

There are two groups of industrial and large commercial consumers. Class A, and Class B. Class A represents roughly [28 percent](#) of total Ontario electricity demand, and its members are part of the pilot, but only if they are part of the Industrial Conservation Initiative (ICI). The key feature of the ICI is that eligible companies can reduce the annual GA component of their electricity bill by reducing or eliminating their electricity consumption during the year’s five hours of peak demand.

But, crucially, it is up to them to guess in advance what those five hours will be, and adjust their consumption thereby.

If Class A customer used power during those peak hours, the cost as of 2019 was approximately \$110,000/MWh. This is far above the cost of installing added capacity. With such excessive peak prices, the ICI contributes to increased volatility for directly connected industrial loads as certain consumers reduce their consumption in far more hours than those that end up being the top five consumption peaks.

Certain industries became very adept at playing their cards right and shutting down during likely top five hours. But nobody knows with certainty when the peak hours in a year will be until the end of the year. As more companies joined the ICI, it became harder to guess when the peak hours were, even for the card sharks. As more and more companies started guessing when the peaks would be, it altered their arrival. Companies had to shut down regularly over the summer in hopes of hitting a top-five hour.

We shouldn’t blame the players. It’s the game that’s flawed.

This pilot can put an end to the gambling.

ICI-eligible customers could get a lower fixed rate based on the amount of the demand they offer into the demand response market. Such a system would better align the prices industrial consumers pay with the system costs, while also preserving industrial competitiveness.

The details of such a system will matter. Will the pilot create a demand response auction into which current ICI customers would make offers for the price in return for curtailing their power consumption when the system is at capacity? Such a system would create a market-based signal for consumers to invest in electricity storage systems rather than the current arbitrary administrative rules in the ICI.

By creating the right price signals for consumers to reduce electricity consumption during the periods of highest costs, not an arbitrary game around the top five hours, the province can reduce the need for costly peak-period production when extra supply must be provided to meet demand. Aggregate system costs can also fall if consumers increase their demand during periods of low cost.

The second group of industrial users are smaller industrial and commercial customers (Class B consumers) that have their hourly GA component set at the end of the month. That end-of-month price per megawatt hour applies to all consumption of electricity, regardless of the system costs in any given hour. There is no help for them in the proposed interruptible rate pilot.

For smaller industrial and commercial consumers, an immediate solution is to have the IESO set the GA on an hourly basis. Without such time varying charges many industrial and commercial consumers lack incentive to smooth their power consumption. Smoothing load saves costs for the system by reducing the need for additional capacity to meet peak demand. An hourly GA rate would encourage price-sensitive manufacturers to push production to early mornings to avoid high-use, high-system-price afternoons and evenings. The Ontario Energy Board has [examined, at least in theory, such a system](#). And on November 15, the provincial [government asked](#) the Board to develop this in further detail in another pilot pricing system. Details are still to come.

The design of these pricing pilots is critical, but real system change is finally coming to the Ontario industrial electricity system.

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