



12 April, 2006

Alberta Electric System Operator  
Attn: Mr. Wes Green, Director Market Services  
Via Email: wes.green@aeso.ca

Dear Wes,

**Re: TMR Reference Price Methodology**

Further to the AESO's request for input on appropriate methodologies for determining the TMR Reference Price, I am writing to provide ATCO Power's comments.

Background

Price reconstitution (the exercise of re-building the price) is not what participants asked for during the market policy development process.

At that time ATCO, along with others, argued that the current practice of removing TMR generation and an equivalent amount of load from the price setting mechanism is inconsistent with a single price market. Accordingly, it was requested that the practice of setting pool price be changed to become the intersection of all supply offers and all demand.

If continuing to set the price using only some of the offers and some of the demand and then reconstituting it, gets you to the same place as you would have been had you simply used all of the offers and demand in the first place, it is perhaps only a circuitous approach that causes no real harm. Unfortunately, unless the suppliers' actual offers are used in reconstitution, that is not true and in addition to being unnecessarily circuitous, the exercise will distort market prices and reduce price fidelity.

One need only consider the ramifications of the ideas that are on the table for creating the phantom offers to verify this conclusion:

- *Use an estimate of TMR suppliers' variable costs:* offering at variable cost is not common practice because it is not a rational offer strategy for the majority of suppliers' volumes. Replacing actual offers with variable cost offers would therefore distort the market price the vast majority of the time.
- *Use a fixed heat rate:* in addition to being arbitrary, this approach would create a phantom shelf in the merit order that would have the added disadvantage of distorting real offers.

- *Use a random number generator:* in an attempt to reduce the impact on real offers that the phantom shelf would have, it has been suggested that it be randomly set within a range. The impact on market credibility of a statement along the lines of "... the Alberta market price was set by a random number generator for several hours yesterday..." does not bear thinking about.

Why then is there a reluctance to take the simple, direct path to calculating pool price thereby obviating the reference price quagmire?

### Market Power Mitigation

Setting the pool price in the absence of competitive forces is no more legitimate than using a random number generator. Although we already have in place mechanisms to deal with market power abuse (and presumably will be revisiting this issue as part of the ongoing market review), TMR arguably presents a special challenge. A TMR generator that is reasonably certain that he would be required to run for transmission reasons no matter what his price, would be at liberty to offer unencumbered by competitive forces and that offer may affect the entire market clearing price. That is not a reasonable outcome and avoiding it is an important objective.

At issue are the appropriate mechanisms and tools to reduce the opportunity for abuse and to deal with any abuse that might nevertheless occur. These should be viewed in the context of the overall market and not just the narrow issue of TMR.

Directing that all TMR supplier offers be overridden by a reference price is a draconian approach that would set an onerous new offer cap for generators required for supply security (i.e. potentially more than TMR suppliers when the market is tight) and would introduce ex-ante, automated bid mitigation to the market. It is not a precedent to be taken lightly.

There are alternative approaches that are arguably more suited to our market:

- Ex-post review of TMR offer prices by the MSA;
- If it appears sufficiently clear that a TMR need is leading to non-competitive offers, provision of extraordinary powers:
  - To the MSA to mandate an interim change in offer practice – pending referral to the tribunal and,
  - To the AESO to exclude those offers from the price setting mechanism.

If successful, these measures will generate supplier offers equivalent to those that would have occurred in the absence of congestion. These offers could then be used in setting the market price and there would be no need of a reference price. At a minimum, they will provide a mechanism for protecting consumers from non-competitive TMR offers until the potential market power issue has been addressed.

### ATCO Power's Proposal

Suppliers in the STA Working Group argued that actual offers should be used in reconstitution but accepted that a reference price might be used as a short term expedient so as not to hold up the whole STA package. That was last August.

Holding one's nose only makes sense for so long. Our clear preference would be to resolve this issue as part of an overall market power mitigation discussion.

To the extent that a more immediate solution is required, we no longer support a reference price approach even on an interim basis. Instead, ATCO Power provides the following specific suggestions:

- In the absence of market power abuse, use actual supply offers when reconstituting the pool price;
- Have the MSA regularly review TMR offers to guard against ongoing market abuse; and,
- If the AESO and MSA agree that some TMR offers are likely non-competitive, do not reconstitute pool price for those offers, have the MSA impose an interim change in offer practice and refer the matter to the MSA tribunal for resolution.

Thank you for the opportunity to provide input on this issue.

Sincerely,

A handwritten signature in black ink, appearing to read 'CF', is written over a faint, illegible printed name.

Carl Fuchshuber  
Senior Manager, Commercial