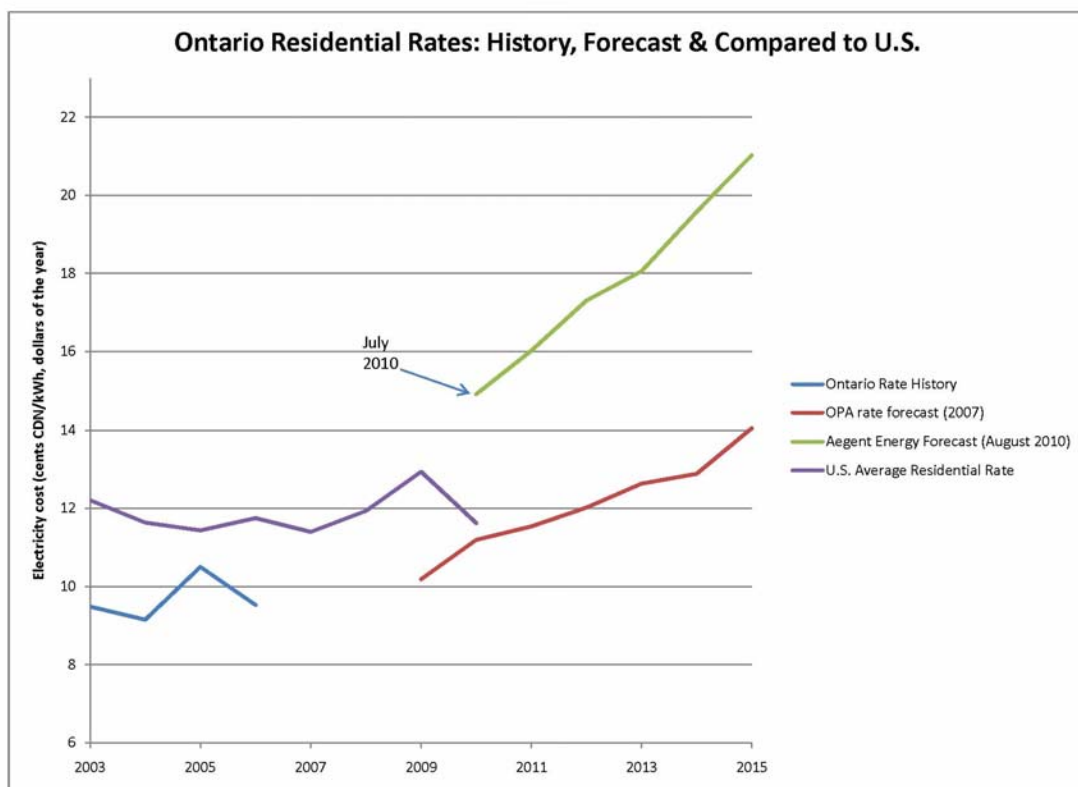


Ontario Power Rate Rip-Off: McGuinty Doubling Your Rates, A Historical Review

by Tom Adams

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Seen an Ontario power bill for September yet? It is sky high and the trajectory is heading much higher still.



The graph shows Ontario's electricity rate history since the election of the McGuinty government¹, the Ontario Power Authority's rate forecast issued in August 2007 as part of the Integrated Power System Plan adjusted to reflect sale taxes and inflation into the future at 2%,

¹ IPSP Exhibit G-2-1 Table 13 provides the history until 2006 and the forecast from 2008 forward assuming 2% inflation. The 2010 cost of power is obtained from the OEB at <http://www.oeb.gov.on.ca/OEB/Consumers/Electricity/Your+Electricity+Utility/All+Electricity+Utility+Bills>

the U.S. weighted average residential price for the 50 continental states², and a forecast of prices until 2015 produced by Bruce Sharp of Aegent Energy Advisors.³

There is a stark contrast between the position of consumers in electricity policy in Ontario for the period up until the election of the McGuinty government in 2003 and the period after.

Before Adam Beck, power in Ontario was extremely expensive, provided by insecure investors using primitive equipment. You see the same thing today in places like Haiti.

Adam Beck thought he had a recipe for cheap power. Beck's idea was that engineers would run a quasi governmental power agency. By design, it would be too complicated for politicians to understand, thereby insulating it from accountability. The government would co-sign its loans, give it sweeping expropriation powers, agree not to tax the agency, and grant it access to valuable Crown natural resources at zero or near zero cost. Top accountants would keep the movement of money reasonably proper but hidden in inscrutable accounts to further insulate from accountability. The engineers promised to not steal and to keep their partying behind closed doors. In return, the politicians were to stay out of the gentleman's club except when invited. The prime directive was to keep rates low.

Beck's scheme lasted for 92 years.

Some folks back in Beck's day, like the first academic economist in Canada, James Mavor, warned that Beck's scheme would be ruinous. Specifically, Mavor warned that the politicians would meddle, the engineers would make bad technological gambles, and the accountants would push too many costs onto future generations.

For about 80 years, Beck looked like a genius. From 1906 when Beck got rolling until 1973, the inflation-adjusted price of power dropped every year. Ontarians were proud of Ontario Hydro, never tiring of comparing rates with the Americans. Hydro was particularly revered in rural communities. The warmth the farmers felt toward Hydro was fueled by rich urban to rural cross-subsidies.

A handful of naysayers did not share in the majority's love of Hydro. A few Indians and trappers watched the bones of their ancestors wash up on the shores of the new lakes Hydro built. Pre-Beck electric utility investors who were victims of Beck's state-sponsored theft also had hurt feelings. Naysayers were not allowed to interfere with progress.

From the beginning, politicians worried about Hydro almost continuously but were too confused, scared or otherwise occupied to do much. In the '20s there was the Gregory commission, in the '30s the Beauharnois scandal investigating committees. Every decade brought another political

² US Energy Information Administration, Average Retail Price of Electricity to Ultimate Customers: Total by End-Use Sector, (updated August 2010)

http://www.eia.doe.gov/cneaf/electricity/epm/table5_3.html, converted to Canadian currency using annual or YTD average exchange rates.

³ The Aegent Energy report was filed as evidence to the Ontario Energy Board, August 31, 2010 in the proceeding EB-2010-0008.

dance, but mostly they danced in circles. There were exceptional politicians who briefly gained an upper hand on Hydro. Premier Davis's Finance Minister Darcy McKeough in 1977 curtailed the credit lines the engineers were running up. Hydro's engineers spat epithets about blackouts and hunkered down to wait. Soon the attention of government moved in other directions and the partying returned to normal at Hydro.

In the early 1980s, during a minority government, a legislature committee went so far as to recommend not completing two of the four reactors then under construction at Darlington. Hydro issued more epithets and again hunkered down to wait. Soon the attention of government moved in other directions and the partying resumed.

Rates started moving up in the early 1970s when nuclear power arrived, steadied, and then moved up again from 1989 until 1992.

Hydro's formerly stalwart allies in industry started fuming about their eroding rate advantage during the recession of 1991. Hydro's bosses ordered austerity. Job positions and budgets were cut. Even sacred budgets of the priesthood of nuclear engineers felt the insults.

First a little in 1995 and then with gusto in 1997/1998, the unthinkable happened. With the federal nuclear safety regulator breathing down Hydro's neck and unbudgeted costs breaking out all over, Hydro was forced to shut down 40% of its nuclear fleet half way through their planned lives. Mavor had been right about the engineers being blind to investment risk, although his grandchildren might have been too old to notice. The accountants tried, but couldn't move enough of the mess off to future generations. A few more people started wondering about fatal flaws in Beck's scheme.

In 1995, Premier Harris had appointed former federal Finance Minister Donald Macdonald to propose a plan for Hydro.

Macdonald agreed with Beck's premise that the purpose of the power system was to serve consumers. However, Macdonald's plan was to switch from government monopoly to free trade in electricity. Macdonald plan was hard to grasp in concept and even harder to implement. Many economists and a handful of law scholars and off-beat environmentalists fell in love with Macdonald's plan.

When the second round of nuclear shutdowns were announced, Harris suddenly faced an insolvent utility, at risk of not being able to buy fuel for its power plants, cover payroll, or service its debts. With no other plan handy, Harris signed on to Macdonald's plan to take the rocky road up the mountain toward the clear, thin air of competition.

Macdonald's most fervent supporters knew that finding enough efficiency to overcome the loss of subsidies the old Hydro had enjoyed would be tough. Macdonald and his supporters failed to anticipate that many Ontario consumers would come to see floating electricity prices as proof that past practice was better.

Folks who think that gasoline prices are controlled by gangsters became a rapt audience for the Toronto Star and NDP leader Howard Hampton hectoring about how the gangsters would control their hydro rates. Some Hydro unions generously funded campaigns on the theme, "Did you know that Enron lawyers helped to write Ontario's electricity market rules?"

Even before competition could get moving, Energy Minister Jim Wilson had already crashed the competition prototype a couple of times, frightening potential power plant investors. Mavor had seen Jim Wilson from a long way off. In one particularly intemperate moment, Minister Wilson, ably assisted by former NDP Finance Minister Floyd Laughren then appointed to head the OEB, unwittingly handed \$7 billion of ratepayers savings embedded in the municipal distribution utility assets over to the cities. The mayors took a break from yelling about provincial downloading long enough to find ways to blow the uploaded windfall. Hamilton used its windfall of ratepayer cash to build the Red Hill Expressway, paving the last big natural watershed on the Niagara Escarpment inside city limits. Mel Lastman bought himself another term as mayor of Toronto. Some smart financial people took note of the \$7 billion slipping out the back door.

In November 2002, another politician Mavor would have recognized, Ernie Eves, took the competition plan out behind the barn and shot it.

When Premier McGuinty came along in 2003, the newspapers told him he had a big electricity problem.

At this point, the total cost of power was about 8.5 cents but hidden under the bill were rotting liabilities built up by Eves and others. (All prices quoted here are inflation adjusted to 2007 currency.) The liabilities were starting to smell.

McGuinty said that consumers had to pay the real cost. Only foolish folk disagreed.

Rates edged up to 8.7 cents. Consumers swallowed the increase without complaint.

McGuinty noticed that people still liked him despite rising rates. He decided to decorate the province with a few fashionable wind turbines like the cool politicians do in Denmark and California. Rates rose to 9.5 cents.

The no-price-is-high-enough green contingent started showing up at Liberal party barbecues. The partying really got going. Somebody got out a box of crayons and they started drafting the Green Energy and Cosmic Time Travel Act. Consumers were not even an afterthought.

Government lawyers worked so hard getting the Cosmic Time Travel clauses deleted, they had no time to clean out the section violating the Magna Carta's taxation principle or the several sections gutting public utility regulation. Energetic Minister George Smitherman agreed to delete the Cosmic Time Travel clauses but he took a small group of special friends to Europe for a really mind blowing renewable energy trip. George and crew had such a great experience, they hopped a plane to Korea for dessert and awards.

The Green Energy Act passed while the opposition members were fumbling to find the light switch.

At this point, the guys who really understand money read the law and started pinching themselves to see if they were dreaming. The get rich quick potential was awesome. Those who had noticed the \$7 billion disappearing in 2000 and 2001 knew they had to move fast. The money boys started hosting green Liberal fundraisers. Only chumps slowed down long enough

to sign the Lobbyist Registry. Nobody has accused Samsung, the largest corporate beneficiary of the Ontario government's green subsidies, of being chumps. To this day, Samsung hasn't bothered registering.⁴

McGuinty put four ingredients into his PR blender: one part green goo, one part "investment", one part "infrastructure", and one part "jobs". Comforted that none of the costs would slop onto his deficit legacy, the new green smoothie tasted great late into the night.

The hangover for consumers is just starting to build. Green blackouts have started.⁵ This week's power bills reflect the increases approved as of July 1st. Rates are up about 18% so far this year. A recent expert report from Bruce Sharp of Aegent Energy Advisors, presented in the graph above suggests that householders should expect another 38% to 47% by 2015. Industry could get hit by increases up to 64% over rates today. This forecast appears to be carefully prepared and thorough. However, it assumes the Green Energy Act is not allowed to get too crazy, no major cost shifting between rate classes occurs, and natural gas prices don't budge above the historically low and stable range they have been for the last 21 months. The actual outcome for consumers may well be worse than Aegent projects.

Sometime late last fall, the average rate households paid for power in Ontario blew past parity with the U.S. average of 12.4 cents (in Canadian currency). U.S. rates are expected to remain flat for several years.

Some on McGuinty's team started wondering whether the green energy trip is less Cosmic and more like an electoral toboggan run. Two Band-aids were inserted into the most recent provincial budget -- the Northern Energy Credit and the Ontario Energy and Property Tax Credit. McGuinty started flip-flopping on some of the more outrageous pillaging rights initially promised to solar developers under the Green Energy Act. Green advocates are stammering about caring for future generations while parents are coming home from factory and resource sector jobs showing their pink slips to their kids.

Sometime around the election in October 2011, Ontario's residential power price will blow past the doubling point relative to the 2003 price consumers paid when McGuinty was first elected. By 2015, Ontario's residential power rates will equal those households currently pay in Germany, one of the models from Mr. McGuinty's restructuring of Ontario's power system. Only about half of the increases so far this year have pure green roots but the Green Energy Act is only 15 months old.

⁴ See: <https://lobbyist.oico.on.ca>

⁵ "Green Blackout", National Post, July 8th.