2006-2008
BUSINESS PLAN

ieso
Power to Ontario. On Demand.

Contents

The Independent Electricity System Operator (IESO) manages the province's power system so that Ontarians receive power when and where they need it. It does this by balancing demand for electricity against available supply through the wholesale market and directing the flow of electricity across the transmission system.

INTRODUCTION

The year 2005 was a watershed year for Ontario's electricity sector. New legislation, record loads on the power system, government policy decisions and the resulting customer and stakeholder needs have focused the priorities of the Independent Electricity System Operator (IESO) over the 2006-2008 business planning period.

The IESO's 2006-2008 Business Plan was developed to meet a number of key corporate business objectives, namely that:

- Ontario's integrated electricity system is operated reliably.
- The IESO manages the wholesale electricity market to promote an efficient allocation of resources.
- Customers and stakeholders are confident in the IESO's handling of its critical roles of managing system and market operations.
- In concert with other key entities including the Ontario Power Authority and the Ontario Energy Board, the IESO advances an efficient, reliable and competitive electricity sector for the benefit of all Ontarians.
- The IESO provides products and services today and in the future that are valued by market participants and others.
- The IESO's assets and resources are effective in supporting the IESO in meeting its commitments now and in the future.

In planning to meet these objectives, the IESO has balanced the uncertainties and cost pressures it faces with a goal of reducing its contribution to the electricity-related costs paid by Ontario consumers. Strong management during the current year will see the IESO rebating some $8.9 million from the 2005 fee. In addition, while meeting our accountabilities and responsibilities we are proposing to reduce the IESO's fee by over five per cent from that currently charged to electricity customers, through a five cent per MWh reduction, from $0.959 to $0.909 per MWh. The plan calls for this fee reduction to take effect in 2006 and extend through 2007, with an objective of achieving a further reduction in 2008. In total, electricity consumers can expect cash savings of almost $35 million over the Plan period through a refund and reduced fees.

THE 2006-2008 BUSINESS PLAN

The 2006-2008 Business Plan:

- Communicates to stakeholders the objectives and priorities of the organization.
- Identifies the opportunities and challenges to the business over the planning horizon.
- Serves as the IESO's submission to the Minister of Energy and the Ontario Energy Board (OEB) in its application for approval of the upcoming year's revenues and expenditure requirements, and the fees it proposes to charge.
- Provides all stakeholders with a view of the estimated resource requirements of the business over the coming three years.
- Establishes the approved budgets for the upcoming year, including the Business Unit OM&A and headcount budgets and the corporate capital budget.
- Provides cash flow information to support appropriate debt financing or debt repayments, and capital outlays.

The IESO incorporates and aligns its business planning with risk management, the setting of objectives, decision making, and other IESO management responsibilities. It considers environmental, strategic, operational, and financial risks and opportunities across the IESO and their potential impact on corporate objectives. This process allows management to determine the appropriate responses to the risk profile given the business environment and the IESO's corporate objectives and priorities. The work plans and initiatives set out in this business plan address the key risks faced by the IESO. These risks include various aspects of: industry developments; stakeholder engagement; customer satisfaction; market design; and staffing.

Stakeholder comments have also played a large part in the development of the 2006-2008 Business Plan. The IESO's continued customer focus is reflected in the actions proposed over the next three years and the commitment to undertake those actions at a reduced fee.

The major responsibilities and accountabilities of the IESO are carried forward under Bill 100. While the legislation resulted in the transfer of the Market Surveillance Panel (MSP) to the OEB, IESO staff continue to provide direct support to the Panel. The legislation also mandated a new independent Board of Directors for the IESO, which has established a Stakeholder Advisory Committee and approved a new stakeholder engagement process. The IESO continues to manage the reliability of the power system, dispatch generation through the market and annually administer more than $10 billion of wholesale charges through the issuing of over 100,000 settlement statements to market participants.

The IESO will continue to support the evolution of Ontario's market based approach to address the Province's electricity needs. In doing so, the IESO recognizes the need, in concert with other key entities including the Ontario Power Authority (OPA) and the Ontario Energy Board (OEB), to make consistent progress over the business plan period in advancing an efficient, reliable and competitive electricity sector for the benefit of all Ontarians.

The following sections first discuss key issues in addressing our corporate objectives, and set out proposed IESO expenditures including estimated resource requirements, the corporate capital budget, and cash flow information.

MAINTAINING POWER SYSTEM RELIABILITY

Continued reliability of the Ontario power system remains the IESO's priority as the organization faces numerous challenges over the next decade.

The IESO's 10-year Outlook highlights the need for new supply, transmission and demand management initiatives, a need that is particularly urgent in downtown Toronto and the western Greater Toronto Area (GTA). Equally demanding, the provincial government's planned phase out of Ontario's coal-fired generation represents one of the most significant undertakings in the 100-year history of Ontario's electricity sector.

The IESO's market, system and reliability responsibilities will play a key role in a successful transition off coal and the IESO will take an active part in developing solutions to emerging issues. Such a significant transition brings with it a number of risks and challenges and there will be an ongoing need to address changes in plans, including those resulting from delays or cancellations of proposed supply or demand response projects. The IESO will monitor and assess the coal shutdown and replacement resource plans and provide advice to all parties, including the provincial government, if actions are required to maintain the reliability of Ontario's power system during this challenging period. For example, in order to maintain reliability, it is important that replacement generation provide similar operating characteristics as coal, be sited in appropriate locations and that necessary transmission infrastructure enhancements be identified and completed.

Sustained hot and humid weather during the summer of 2005 strained Ontario's power system as high demand levels exceeded the ability of the province's generation and transmission facilities to meet those needs. As a consequence, on several occasions, the IESO was forced to take emergency control actions, such as five per cent voltage reductions, in order to manage reliability. These reliability pressures, including a need for customers to reduce their electricity use during periods of system strain, are likely to remain over the next several years until new supply and transmission facilities are installed.

The IESO intends to proceed with measures to reduce the need for the types of emergency control actions that were implemented in 2005. These measures are expected to be in place in advance of the summer of 2006.

As new facilities are installed over the next few years, additional pressure will fall on the IESO to ensure that they are successfully integrated into the grid and the IESO-administered market. The increased connection assessment activities resulting from the Generation Request for Proposals selections will require constant work and rework of short-term plans, along with strong coordination with the OPA and with the owners and operators of new facilities.

The high rate of change in Ontario's electricity infrastructure will have a significant impact on the IESO's resources and processes. This risk is increased as there will continue to be uncertainty as to the planned changes to the infrastructure (e.g. the decision to not restart two of the Pickering units), the introduction of a different mix of technologies (e.g. wind power), and the ongoing draw on IESO expertise by other organizations.

There are also changes expected as a result of the passage of the U.S. Energy Bill. The IESO will need to be prominent in representing Ontario's interests – particularly given the potential impact on Ontario operations and our reliance on interconnections. Imports will be a key factor in maintaining reliability over the next few years during high demand periods and the IESO must ensure that unreasonable risks are not placed on the interconnected system.

While a number of the aspects of the Energy Bill will take considerable time to be implemented, the formation of the Electric Reliability Organization and the creation and imposition of mandatory standards and compliance will have more immediate impacts on Ontario and the IESO.

The expected increase on compliance audits, which are staffed primarily from industry participants such as the IESO, will lead to increased demand on IESO resources.

The IESO will also need to monitor the development of new rules that could hamper the ability of market participants to engage in cost-effective and seamless transactions between markets.

All of this places additional pressure on the IESO's ability to manage reliability and has resulted in increased work for the IESO over the short and medium term. The IESO is responding to this increased pressure by realigning staff resources within these areas of the business. Specifically, within the Market & System Operations (M&SO) business unit, staff resources have been repositioned so that there is increased focus on preparing for the coming changes in the systems infrastructure. The ability to allocate increased staff resources to this critical work is partially a result of a corporate realignment the IESO undertook in 2005. Also, the IESO continues to plan and work to be able to deliver an increased volume of work related to connection assessments. In 2005 the IESO hired additional staff – these staff are being trained and developed such that they can perform connection assessment work or perform other ongoing work to allow more experienced IESO staff to focus on connection assessment activities.

A new business unit – Reliability Assurance – was formed to provide an oversight role on the required work necessary to support the significant infrastructure change.

MARKET EVOLUTION

Events of 2005 have played a large role in establishing the IESO's market evolution plans for the next three years. Firstly, the OPA, has been established, and is proceeding with their initial System Plan, and various supply procurement initiatives. While in its early stages of development, the OPA will clearly play the major role in ensuring that sufficient generating capacity is developed in Ontario to achieve the coal retirement program. The second significant event of 2005 was the lessons learned from the extensive stakeholdering efforts conducted by the IESO on the development of the Day Ahead Market (DAM). A clear message from that effort was that many stakeholders believe that some key current market issues must be resolved before they will be able to support further market evolution. Thirdly, the extreme conditions of the summer 2005 have magnified the importance of evolving some key operational aspects of Ontario's current wholesale market design prior to the 2006 summer period in order to avoid ongoing reliability risks to Ontario's electricity supply.

This Business Plan proposes that the IESO will respond to these operational and stakeholder issues by placing its highest priority on resolving current market issues prior to proceeding with significant market evolution programs.

The list of current market issues fall under the following five categories:

- Day-ahead commitment issues. (Addressing the fact that the market is currently unable to commit to electricity imports and the operation of Ontario resources in the day-ahead timeframe, causing significant concerns for the reliability of electricity supply to Ontario.)
- Market pricing issues. (The pursuit of market pricing that provides incentives that result in appropriate actions and rewards during periods of normal operation and during times of scarcity and system stress.)
- Ontario resource dispatch issues. (Addressing problems identified by stakeholders regarding dispatch of Ontario resources which result in excessive wear and tear on equipment, causing degraded performance and additional costs.)
- Intertie scheduling issues. (Coordinating intertie processes with participants and system operators of neighbouring jurisdictions to minimize any seams issues and resultant transaction scheduling failures.)
- Demand response issues. (Ensuring that the right information is provided to the right consumers at the right times to facilitate their effective use of the market, and that load response is used as effectively as possible in cases of emergency conditions on the power system.)

In addition, throughout the period the IESO will be pursuing, in consultation with stakeholders, the development of improved market signals in the day-ahead timeframe.

Addressing the current market issues will consume the evolutionary capacity of both the IESO and the stakeholder community for the first 18 months of the horizon of this Business Plan. One specific target, adopted as a result of the extreme operational challenges faced in the summer of 2005, is to implement a solution to day-ahead commitment issues prior to the summer of 2006. While achieving this target will require substantial effort on the part of IESO staff, and significant stakeholder input into design details, making steady progress on the other real-time market issues remains important. In all cases, progress on real-time market issues will be made in a context that is consistent with Government and stakeholder goals for the evolution of Ontario's hybrid market.

The focus of market evolution efforts in the latter half of the Business Planning horizon will shift more strongly to creating the liquid, competitive, electricity market that provides the necessary signals for future investments in the Ontario electricity industry. This effort will be closely coordinated with the OPA, to ensure an efficient, viable and coordinated transition is possible.

STAKEHOLDER ENGAGEMENT

Stakeholder engagement, the process by which stakeholder views and requirements are identified and factored into decisions, is integral to IESO decision making.

Extensive consultation efforts by the IESO in 2005 and governance changes including a fully independent Board of Directors, have prompted a number of changes for the IESO in the way that it engages stakeholders. A new stakeholder engagement process, developed in concert with stakeholders and approved by the IESO Board of Directors in July 2005, will result in increased stakeholder involvement in IESO decision making.

The IESO Board of Directors also adopted the recommendation to establish a Stakeholder Advisory Committee as an integral part of the new stakeholder engagement process. This newly created body is designed to afford stakeholders the opportunity to provide advice directly to the IESO Board of Directors and Executive on IESO market development decisions (e.g., decisions that have a material effect on the existing electricity market or future evolution of the market), IESO planning decisions (e.g., business plans, work plan prioritization, etc.), or any other matter that may be of concern to stakeholders.

The adoption of a new stakeholdering engagement process with its associated stakeholder engagement principles requires a substantial commitment from both stakeholders and the IESO. Consistent with the recommendations for the new process, a dedicated unit has been created with the express mandate to enhance the capability of the organization to gather and integrate stakeholder views and requirements into IESO decision making.

CORPORATE REALIGNMENT

Providing greater value to stakeholders and ensuring that the IESO's resources are effective in meeting our commitments now and into the future were key drivers for the IESO's 2005 corporate realignment. In realigning responsibilities and accountabilities within the organization, the IESO recognized the rate of change within the province's power system and the need for the IESO to assume new responsibilities to play its part in managing that change, while at the same time addressing the need for continued cost controls.

The IESO's experience since market opening has demonstrated the need for close coordination between our market and system operations. Building on this experience, the realignment has brought together all market and power system operations under one business unit – Market and System Operations. With close to 13,000 MW of new supply or demand-side resources required by 2014 as well as significant renewal and reinforcement of transmission facilities, the Market and System Operations group will ensure the IESO is able to accommodate the physical integration of these new resources into both the system and the market.

Given the magnitude of the expected physical infrastructure change in Ontario's electricity sector over the next short while, a new business unit – Reliability Assurance - was created within the IESO's organizational structure. Although small in resource level, this function has a key oversight role and is responsible for ensuring that the implications of the mid and longer-term changes in the power system are effectively managed.

The new Corporate Relations and Market Development group will house the new Stakeholder Engagement unit and address areas that are expected to require increased attention in the next few years, including market evolution and regulatory affairs. Effective communication with stakeholders is also vital during this period of anticipated change.

The other noteworthy change was the creation of Corporate Services with the combination of Legal Services, Internal Audit, Corporate Planning and Finance. These areas of the business were combined to more effectively address the ongoing and increasing challenges associated with the growing emphasis on corporate governance issues; and with the support of other business units such as Information Technology & Infrastructure, to identify and achieve ongoing improvements in organizational performance.

While the realignment enhances the focus for existing resources, the IESO continues to face the potential for higher levels of attrition over the planning period. By 2008, over one hundred of the IESO's staff will be eligible to take early retirement. The IESO's experience is that staff do not retire as soon as they are eligible and that has resulted in a 'bow wave' of staff with the potential to retire. Although overall attrition has been low, the IESO is addressing this concern through a variety of strategies including training and development, hiring new staff, strengthening its partnership with universities and colleges and ensuring a solid co-op education program, succession planning, use of external vendors and contractors and use of temporary staff.

RELATIONSHIP WITH THE ONTARIO POWER AUTHORITY

The Ontario Power Authority has its own set of separate and distinct responsibilities related to future supply mix, procurement of future capacity, development of an integrated power system plan and conservation. While the responsibilities of the OPA are new to the sector, there is a need for the IESO and the OPA to work closely together to ensure that there is co-ordination so that efforts are not duplicated and that our activities complement each other to effectively serve the province's electricity consumers.

The OPA continues to develop its business processes in order to address its objects under legislation. The IESO and the OPA are working together to identify areas where the coordinated use of IESO resources might be the most efficient and effective solution for Ontario's electricity customers.

For example, one of the new areas being allocated to the OPA is the responsibility for longer term forecasting. The IESO will continue to produce materials including the 18-month Outlook to address our short and medium term forecasting responsibilities as well as longer term outlooks required to satisfy IESO obligations related to reliability of the interconnected North American power system. The IESO and OPA will continue to explore potential opportunities for co-ordination in areas such as forecasting.

CUSTOMER EDUCATION

The Electricity Restructuring Act, 2004, which took effect on January 1, 2005, created a hybrid market where the majority of customers are protected through a regulated rate plan while still allowing larger business and industrial customers to realize the benefits of a competitive wholesale market. Although much of Ontario Power Generation's output is price regulated, the vast majority of the province's generating capacity is still dispatched and administered through the IESO.

While the majority of Ontario electricity consumers fall under the regulated rate plan, more than 50,000 customers representing over 55 per cent of the electricity load are exposed to the market price. Throughout 2005, the IESO's customer education efforts have prompted thousands of wholesale customers to understand that they have the ability -- through the market -- to better manage their electricity costs. The IESO will continue to work with others to address the need for customer education.

MEASURING THE BUSINESS

Corporate Performance Measures

Corporate performance measures are a means by which the IESO monitors its performance to best ensure it is on track to achieve its corporate objectives. While the measures for 2006 remain to be finalized, the IESO continues to use a balanced scorecard approach, which assesses performance in four areas:

1. Effective use of funds;
2. Marketplace evolution;
3. Customer /stakeholder satisfaction; and
4. Operational effectiveness.

The IESO's performance against expectations and targets are publicly reported on our website (www.ieso.ca) on a quarterly basis for all stakeholders and interested parties to review. Feedback from market participants and other stakeholders is also considered, in order to drive improvements, and ensure the organization satisfies its customers and stakeholders on an on-going basis. The IESO's independent Board of Directors approves the suite of corporate performance measures and targets annually, and assesses results achieved.

Consistent with a reshaping of the organization, IESO management has undertaken a review of its corporate performance measures and expectations in 2005 and will adjust them to more closely align with future expectations. For the period 2006-2008, the priorities that will drive IESO work program activities and initiatives in the future are identified by our corporate objectives.

Comparisons with Others

The IESO recognizes the value in comparing itself against its peers. As identified in the 2005-2007 Business Plan, the IESO led a cost comparison initiative in 2004 amongst the independent system operators (ISOs) and regional transmission organizations (RTOs). However, that work was not completed due to the issuance of a Notice of Proposed Rulemaking (NOPR) by the FERC. The NOPR is aimed, amongst other things, at the establishment of a uniform system of accounts for ISOs/RTOs. The IESO continues to work with its peer group, through the FERC process, on developing a method to compare the operating and capital costs of various ISO/RTOs. In its decision on the IESO's 2005 fee application, the OEB agreed that the cost comparison exercise unfolding under the aegis of the FERC was the best way to make meaningful benchmarking comparisons with other system operators. The IESO will file the information compiled in accordance with the FERC process when that process is complete.

FINANCIAL OVERVIEW

The IESO's fiscal management is based on a simple objective – to demonstrate continued prudent financial management while achieving our objects as outlined in legislation, including supporting the staged evolution to a more competitive market.

The IESO believes we have been successful in achieving this objective:

- Long-term debt levels are being significantly reduced:
    - By the end of 2005, $220.0 million (over 60 per cent) of the IESO's long-term debt will have been repaid since 2002; and a further
    - $55.0 million will be repaid over the planning period, bringing total debt repayment to almost 80 per cent since 2002.
- The usage fee has remained at $0.959/MWh for four years in a row – 2002 through 2005.
- An estimated $8.9 million will be refunded in 2006, representing over five per cent of the forecasted fees to be collected in 2005.
- The usage fee is proposed to be reduced by over five per cent in 2006 – a full five-cent reduction - from $0.959/MWh to $0.909/MWh.
- The outlook is to maintain the reduced fee level in 2007 with a further reduction anticipated in the usage fee in 2008.

Through the IESO's success in managing costs, market participants can expect cash savings of almost $35 million over the Plan period through a refund and reduced fees.

PROJECTED 2005 FINANCIAL RESULTS

The second quarter projected 2005 financial results, as shown below, demonstrate the IESO's commitment to operate in a financially prudent manner. Disciplined cost management and higher than expected energy usage will result in overall results for 2005 being better than was budgeted in last year's Plan for fiscal 2005.

2005 Projected Operating Results

($ millions)	2005 Projected	2005 Budget	Variance
Usage Fees	153.9	149.2	4.7
Market-related Interest Income	2.6	1.7	0.9
Cost Recovery for Services	1.1	1.5	(0.4)
Total Revenues	**157.6**	**152.4**	**5.2**
OM&A Program Costs [1]	83.5	86.2	2.7
OM&A Pension Expense	8.2	8.4	0.2
Amortization	47.6	48.5	0.9
Net Interest	8.3	8.5	0.2
Total Costs	**147.6**	**151.6**	**4.0**
Operating Surplus	**10.0**	**0.8**	**9.2**
Accumulated Operating Surplus [2]	**13.9**	**4.7**	**9.2**

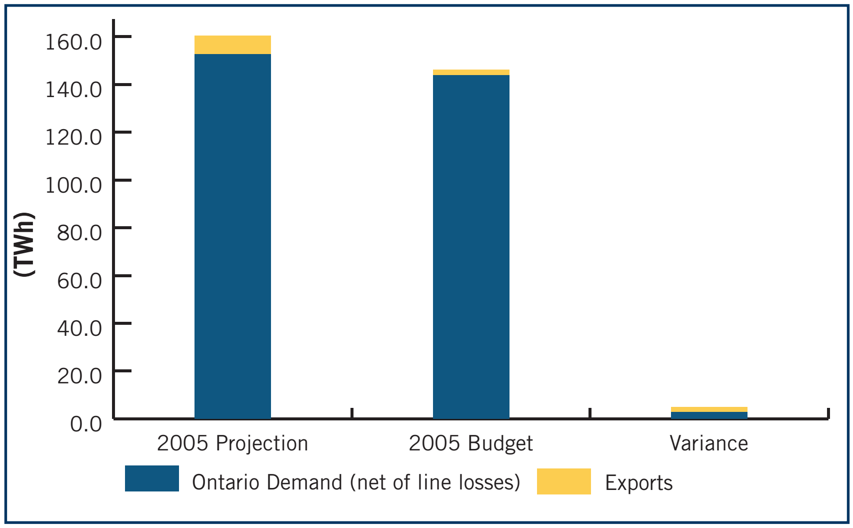
Overall, the 2005 projected operating results would result in an accumulated operating surplus of $13.9 million by year-end. This is determined by adding last year's actual accumulated surplus of $18.9 million, less the $15.0 million in funding for the OPA, to this year's projected surplus of $10.0 million. Consistent with the IESO's proposal that was accepted by the OEB in its 2005 rate application Decision, the IESO will refund any accumulated surplus balance in excess of $5.0 million. Accordingly, the IESO is estimating a refund of approximately $8.9 million - due to essentially equal amounts of higher than anticipated energy volumes and lower than planned total costs.

[1] OM&A Program Costs include those operating costs categorized as 'Market Evolution Program' in the 2005-2007 Business Plan. Please see page 16 for more information.

[2] The accumulated operating surplus is presented prior to the rebate of any balance in excess of $5.0 million.

Usage Fees

The usage fee revenue for 2005 is projected to be $153.9 million, approximately $4.7 million greater than budget. The revenue variance is forecasted to result from higher volumes within the IESO-Administered Markets. The currently forecasted energy volumes for 2005 are 160.5 TWh, or 4.9 TWh higher than the energy levels utilized for 2005 planning. The following chart outlines those variances:



(TWh)	2005 Projection	2005 Budget	Variance
Ontario Demand (net of line losses)	152.7	149.8	2.9
Exports	7.8	5.8	2.0
Total Energy Levels [3]	**160.5**	**155.6**	**4.9**

Higher than planned usage fees are largely responsible for the variance in revenues. This is a result of higher projected domestic demand and exports with almost 60 per cent of this variance related to domestic demand. Demand in 2005 was higher than expected primarily as a result of the hot weather conditions in the summer.

The 2005 forecasted energy volumes represent actual volumes to the end of July 2005 and forecasted amounts for August through December 2005 and are based on the IESO's most recent 18-month outlook.

Market-Related Interest Income

Market-related interest income represents the interest earned by the IESO through the IESO-Administered Markets settlement clearing bank accounts. There are three ways by which interest on market funds can accrue to this IESO account. In its settlement of the market, the IESO typically collects funds from owing market participants (i.e. buyers) and then pays the receiving market participants (i.e. sellers) two business days later. In the period between receipt and disbursement of market funds, the monies are invested with interest earned thereon accruing in the settlement clearing account. In addition, market participants make periodic prepayments and similarly these monies are invested with interest accruing to the settlement clearing account. Lastly, the Business Plan Protection Rebate ("BPPR") is executed

[3] Transmission line losses are taken as 3 per cent of the Demand Forecast. Exports for forecasting purposes are calculated on a five-year moving average.

on a quarterly basis and the interest earned on the funds held during the settlement cycle are also included in the settlement clearing account.

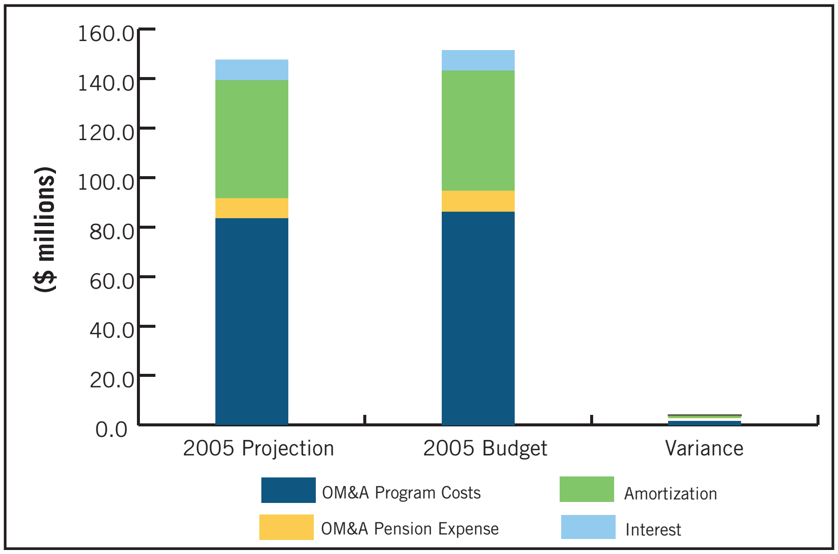
The projected 2005 revenues of $2.6 million are from the interest earned on the above-described funds and represent a positive variance of $0.9 million relative to budget. This variance is primarily attributed to interest earned on BPPR funding. Bill 100 had the effect of eliminating the BPPR; however, at the time the 2005 Business Plan was crafted, the timing was uncertain. Accordingly, the Business Plan was developed with the assumption that the BPPR would not continue into 2005. In 2005, BPPR did continue until August and the IESO earned interest of approximately $0.6 million on those funds. The remaining variance of $0.3 million was a result of higher volumes of prepayments, larger monthly settlement volumes (providing higher than expected cash balances available for investing), and higher interest rates.

Cost Recovery for Services

Cost recovery for services represent fees charged by the IESO for services provided, charged on a cost recovery basis. In 2005, those fees are projected to be $1.1 million and represent work on connection assessments ($1.0 million) and training ($0.1 million). The projected variance of $0.4 million is the result of lower than expected work undertaken on connection assessments. This lower than planned work volume was largely the result of the IESO's challenge in finding available staff, internally and externally, that have the necessary skill set to perform connection assessment work.

Total Costs

The following chart outlines the projected 2005 total costs, including a comparison to the OEB approved budget:



($ millions)	2005 Projection	2005 Budget	Variance
OM&A Program Costs	83.5	86.2	2.7
OM&A Pension Expense	8.2	8.4	0.2
Amortization	47.6	48.5	0.9
Net Interest	8.3	8.5	0.2
Total Costs	**147.6**	**151.6**	**4.0**

In 2005, total costs are projected to be approximately $147.6 million, an amount that is $4.0 million, or 2.6 per cent, below the approved budget of $151.6 million.

OM&A Program Costs

The following table outlines the projected 2005 OM&A program costs relative to budget:

($ millions)	2005 Projection	2005 Budget	Variance
Staff Costs[4]	56.7	56.7	0.0
Computer Support, Maintinance & Equipment	11.3	12.2	0.9
Contract Services & Consultants	7.2	8.4	1.2
Administration	5.5	5.8	0.3
Telecommunications	2.8	3.1	0.3
Total OM&A Program Costs	**83.5**	**86.2**	**2.7**

Staff costs, which represent all operating costs associated with staffing, excluding pension expense, are projected to be $56.7 million in 2005. That projected spending level is consistent with the approved budget.

Computer support, maintenance and equipment costs are projected to be $11.3 million in 2005 or $0.9 million below the approved budget. This variance is a result of: lower than planned use of external resources for systems support due to lower levels of OM&A change

[4] Staff costs include salaries, benefits (excluding pension), relocation, training, and other employee expenses.

requests and remedial action than expected; lower than budgeted increases in hardware support and license costs; and beneficial movement in exchange rates.

Contract services and Consultants are projected to be $7.2 million, or about $1.2 million below the 2005 budget of $8.4 million. The variance is a result of numerous minor differences from the plan, including: lower costs for day-ahead market activities, Board of Director vacancies, higher than budgeted savings in relation to the hiring of an additional internal legal resource, and a later than expected transition to an externally provided meteorological service arrangement as a result of contracting out challenges.

Administration costs are projected to be $5.5 million, $0.3 million below budget for the year. This variance is largely due to lower than expected rent associated with the backup operations center (BOC). The 2005 plan assumed a relocation of the BOC in the year and the need for an overlap in rent as the IESO would hold a lease for the existing and replacement facilities during the transition. Although an active search began in 2004, the IESO has so far been unable to identify a suitable location. At this stage in the year, it is unlikely that a move will be undertaken by year-end; therefore additional rents were removed from the projection. The IESO continues to investigate the relocation of the BOC and expects to relocate in 2006.

Telecommunication costs are projected to be $2.8 million, $0.3 million below budget, as 18 new remote terminal units (RTUs) are currently scheduled to be installed in the year, compared to a budget of 24. Although participants pay for the purchase and installation of the RTUs, the IESO is responsible to pay the associated telecommunication costs for the data transmission lines to the system control center.

Market Evolution Program

As a result of the IESO's corporate realignment, the responsibility for all market evolution development was placed with the Director, Market Evolution within the Customer Relations and Market Development (CR&MD) business unit. All activities necessary to identify, investigate, and design market changes are to be led by that function within the business. Once the changes have been designed, the Vice President – Information Technology and Infrastructure will lead the necessary tools development and implementation activities. Accordingly, there will no longer be a separate line item included in the IESO's business plan for MEP. Rather, the internal staff costs to support this work will reside within the supporting staff member's line organization. Any required external support will be included in the line budget within CR&MD.

For 2005, operating costs associated with the Market Evolution Program were budgeted at $3.2 million. The projected expenditures for the year are $2.3 million, as outlined below:

($ millions)	2005 Projection	2005 Budget	Variance
Day-Ahead Market (DAM)	2.0	2.4	0.4
Resource Adequacy Market	0.0	0.3	0.3
Market Pricing	0.1	0.3	0.2
Program Management	0.2	0.2	0.0
Total Market Evolution Program	**2.3**	**3.2**	**0.9**

In 2005, the IESO will have further consulted on what day-ahead solutions were required to satisfy market and reliability needs and to identify alternatives to the 'comprehensive' **day-ahead market (DAM)** proposals developed in 2004. The project team stakeholdered objectives and the criteria for evaluating alternatives and it developed three options for consideration and these were discussed with stakeholders. The team is in the process of developing market-based cost benefit analyses and are to present their recommendations to the IESO Board of Directors in October 2005. The estimated cost to complete this work is $2.0 million, some $0.4 million below the approved budget. This variance was largely the result of utilizing a smaller than expected core team.

In regards to a **resource adequacy market (RAM)**, the 2005 budget included $0.3 million, $0.1 million for continued investigative work along with a further $0.2 million in operating costs to put a RAM in place (in addition to $0.2 million in capital funding). At its 2005 rate application, the OEB provided approval to the IESO to expend the initial $0.1 million prior to engagement with the OPA that such a mechanism is required. To date, the discussions with the OPA have not taken place and the total expenditure for 2005 is less than $25,000.

Market pricing is an area of work undertaken to address the issues that exist in the current real-time market. Of the 36 pricing issues identified by the Market Pricing Working Group (MPWG) in 2004, 12 were identified for detailed consideration in 2005. Two recommendations from the MPWG related to settlements have resulted in market rule amendments. Market rule changes to reduce the instances of counter-intuitive prices during emergency conditions were approved by the Board in June, and implemented in August. Possible further changes in this area are still being discussed by the group, with the outcome expected in September. Proposed changes to Control Action Operating Reserve that were extensively discussed by the working group will be considered by the IESO Board in the fall. Another initiative expected from the group in 2005 relates to the incorporation of Multi-interval Optimization into the pricing algorithm, with implementation (if approved) requiring software modification. Two other issues expected to be addressed involve pre-dispatch demand forecasting and the intertie offer guarantee. The costs incurred in support of this work are largely those of IESO staff time. Due to the corporate realignment undertaken in 2005, costs in support of this initiative were only tracked separately up until the middle of 2005. Those costs totaled approximately $0.1 million against an approved budget of $0.3 million.

OM&A Pension Expense

The projected OM&A pension expense for 2005 is $8.2 million or approximately $0.2 million lower than budget.

Amortization

The projected amortization costs for 2005 are $47.6 million, or approximately $0.9 million lower than budget. This two per cent variance results primarily from projected capital spending levels that are lower than budget and some project timing being later than the assumptions in the 2005 plan. The details of the IESO's 2005 capital program are included later in this section.

Net Interest

Net interest expense is projected to be $8.3 million, or $0.2 million below the budget of $8.5 million. This positive variance is the result of higher than budgeted investment income as the IESO had higher than planned cash available for investment and the investment returns were slightly higher than planned.

Accumulated Operating Surplus

The accumulated operating surplus at the end of 2005 is projected to be approximately $13.9 million, resulting from a projected operating surplus of $10.0 million in the year, the payment of $15.0 million to the Ontario Power Authority and the opening balance of $18.9 million.

As outlined earlier in this Plan, a closing balance of $13.9 million would result in a refund to market participants in 2006 of the balance over $5.0 million, or a projected refund of $8.9 million.

2005 Projected Balance Sheet

The following represents a summarized projected balance sheet as at December 31, 2005, in comparison to budget.

($ millions)	2005 Projection	2005 Budget	Variance
Cash, Cash Equivalents and Temporary Investments	13.4	22.3	(8.9)
Accounts Receivable and Short-term Pre-paid Expenses	19.5	17.9	1.6
Current Assets	**32.9**	**40.2**	**(7.3)**
Property and Equipment	136.3	140.8	(4.5)
Long-term Investments	9.3	9.4	(0.1)
Prepaid Pension Expense	21.8	20.0	1.8
Total Assets	**200.3**	**210.4**	**(10.1)**
Accounts Payable, Accrued Liabilities and Accrued Interest	19.9	20.3	(0.4)
Long-term Debt	133.2	153.2	(20.0)
Accrual for Employee Future Benefits other than Pension	31.9	31.9	0.0
Total Liabilities	**185.0**	**205.4**	**(20.4)**
Accumulated Operating Surplus	**13.9**	**4.7**	**9.2**
Accumulated Market-related Penalties and Fines	**1.4**	**0.3**	**1.1**
Total Liabilities and Surplus	**200.3**	**210.4**	**(10.1)**

The following outlines the material projected balance sheet variances relative to budget:

The balance of cash, cash equivalents and temporary investments at the end of 2005 is projected to be $13.4 million, or about $8.9 million lower than budgeted. This variance is forecasted to result from the early repayment of $20.0 million in long-term debt; partially offset by the operating surplus in the year that is projected to be $9.2 million better than anticipated.

The projected total property and equipment balance at the end of 2005 is $136.3 million, an expected $4.5 million below the budgeted level. This variance is due to 2005 capital spending that is projected to be $5.4 million below budget, offset by amortization that is projected to be $0.9 million below budget. The projected results in relation to capital spending are outlined in the next section of this document.

Total long-term debt is projected to be $133.2 million at the end of 2005, an amount that would be $20.0 million below budget. This reflects the IESO's financing strategy to minimize cash balances and repay long-term debt whenever possible, even earlier than planned when appropriate.

Accumulated market-related penalties and fines total $1.4 million at the end of 2005. In 2005, $1.1 million of the funding is projected to be spent on customer education programs, with $1.2 million of the remainder to be spent on customer education program initiatives in 2006. The projected residual balance at the end of 2006 of accumulated market fines and penalties of $0.2 million is assumed to remain in the account pending IESO Board approval on the utilization of these funds. Approval is expected to be sought in late 2005 or 2006.

2005 Capital Project Expenditure

In 2005, the IESO is projecting to undertake capital initiatives that will total $14.7 million, an amount that is approximately $5.4 million below the approved budget, as outlined in the following table.

($ millions)	2005 Projection	2005 Budget	Variance
Applications	8.0	10.6	2.6
IT Infrastructure	6.0	9.2	3.2
Facilities Improvements	0.7	0.3	(0.4)
Total Capital	**14.7**	**20.1**	**5.4**

As identified in prior years, given the ongoing need for changes and reprioritization, the IESO does not utilize the business planning process as a mechanism for capital project approval. Rather, through business planning, an appropriate capital envelope for future years is established. However, in preparing its 2005-2007 Business Plan, the IESO recognized stakeholders' desire for increased disclosure and information in terms of project-specific capital plans. Therefore, the 2005-2007 Business Plan included a listing of projects that supported the capital envelope. The following outlines material variances from that listing. In addition, Appendix 3 shows the projected 2005 capital expenditures on a project basis.

Applications

Central Alarms Management is a project that would see comprehensive improvements to system alarms. The project has been approved for some $3.5 million with completion in 2006. This timing is consistent with the 2005-2007 Business Plan, however, the estimated project cost is approximately $1.5 million less than the estimate included in the Plan, resulting in a variance of $1.0 million in 2005.

Outage Management is a project that would replace the existing integrated outage management system. Limited availability of internal staff expertise has resulted in revised timelines for this project, resulting in a variance of approximately $0.6 million in 2005.

Configuration Management, the implementation of configuration management software and related processes, has been cancelled at this time due to reprioritization. This change will result in a variance of approximately $0.3 million in 2005.

Message Exchange Upgrade, a project that would upgrade the existing message exchange, has been cancelled in 2005 due to reprioritization, resulting in a projected variance of some $0.3 million.

IT Infrastructure

Unix Server Infrastructure Upgrade is a project that will see the replacement and upgrade of the existing Unix server environment, an environment that hosts most of the market applications and is comprised of aging hardware. The related architecture work is taking longer than anticipated, pushing back the planned date of the project and the related purchase of replacement hardware. The impact of this is a projected variance of $2.5 million in 2005 capital.

The Back-up Operations Center Relocation and Configuration is projected to take place in 2006, as the IESO continues to investigate suitable locations, resulting in a projected variance of $1.2 million in 2005.

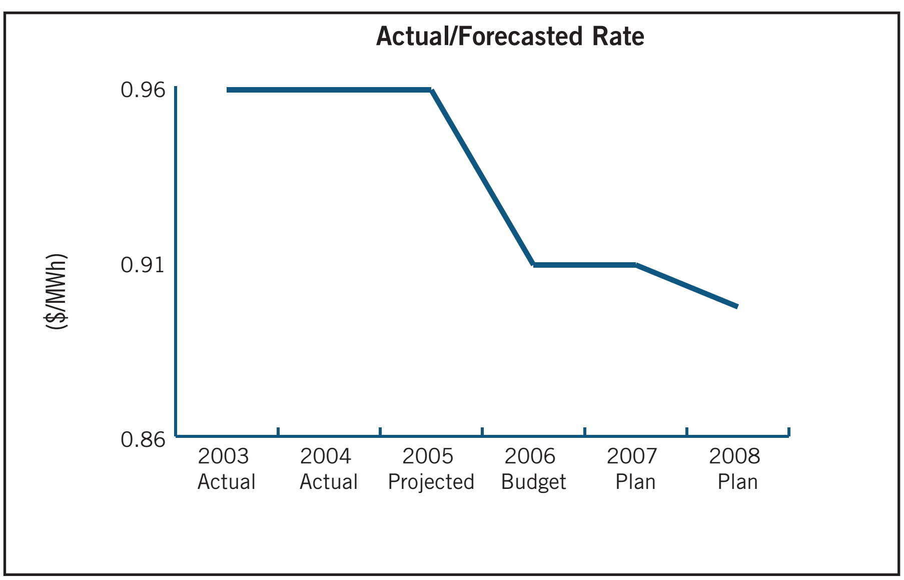
Backup Infrastructure Enhancements, a project that would strengthen the IESO's file archiving approach and solution, is projected to cost $0.8 million in 2005. There was nothing included in the 2005 capital plan for this work as it was expected to be completed in 2006. An ongoing assessment of associated business risk resulted in increasing the priority of this project, resulting in a projected variance of $0.8 million over budget in 2005.

The Remote Access Upgrade was projected to be completed in 2005. This work is now projected to be completed in 2006, resulting in a variance of $0.4 million in 2005.

Facilities Improvements are projected to have some $0.7 million in expenditures in 2005, an amount that would be $0.4 million over budget. This variance is largely the result of unscheduled physical security upgrades at IESO locations as a result of changes in the external threat profile.

FINANCIAL OUTLOOK 2006-2008

The financial outlook for the IESO for the planning period 2006-2008 reflects strong cost management, enabling the IESO to charge a lower usage fee throughout the period. Specifically, the IESO is forecasting to charge a usage fee of $0.909/MWh in 2006 and 2007 and have a further reduction in 2008. This represents an improved financial outlook from the 2005-2007 Business Plan. In last year's Plan, the IESO was forecasting the usage fee to remain at $0.959/MWh through 2007.



Key Assumptions over the Planning Period:

Prior to reviewing the details over the period, it is important to ground these budgets and outlooks with the related assumptions. They are as follows:

- Load forecasts utilized in calculating the usage fees over the plan horizon are based on the IESO's most recent 18-month and 10-year forecasts.[5]
- An estimated $8.9 million of the accumulated surplus at the end of 2005, anticipated to be $13.9 million, will be rebated to market participants, as outlined earlier.
- The long-term debt repayable to the Province of Ontario in 2007 is renegotiated with similar terms to those that are currently in place (i.e. floating rate reset quarterly with repayment option).
- The average annual floating interest rate paid on the long-term debt, excluding the fixed rate debt with the Ontario Electricity Financial Corporation, will be in the range of 3.1 per cent to 4.4 per cent over the planning period.
- $20.0 million of debt owing to the Province of Ontario will be repaid in 2006, with a further $30.0 million repaid in 2007 and the remaining $5.0 million in 2008.
- Capital spending of $25.0 million in 2006, $20.0 million in 2007, and $14.0 million in 2008. This spending level assumes $9.0 million in 2006 and $6.0 million in 2007 for the implementation of day-ahead market.
- Pension expense for 2006 based on actual pension plan returns to the end of April 2005 with the 2007 and 2008 pension expense based on plan returns of 7.0 per cent. This latter rate of return is consistent with the assumed expected long-term return on plan assets.

The table below outlines the planned operating results over the planning period:

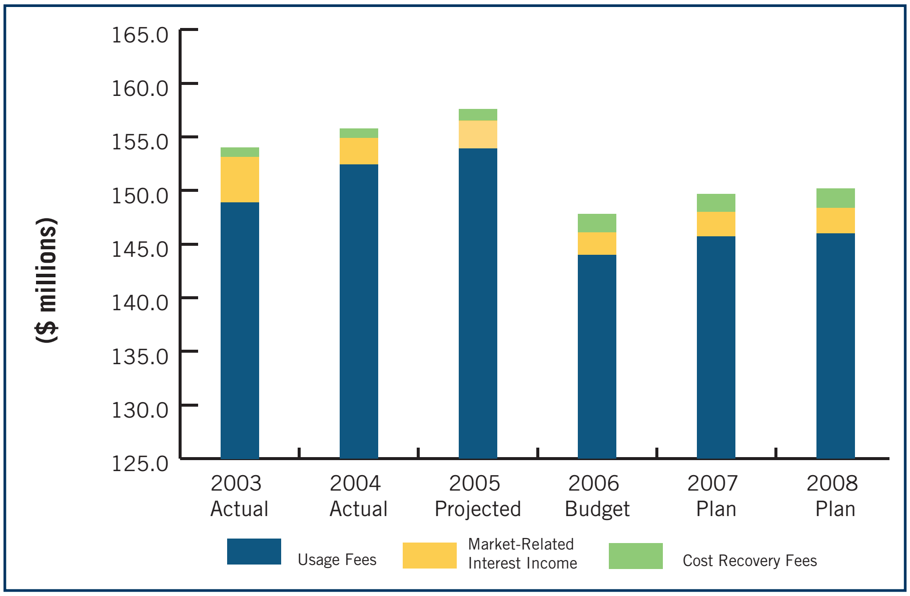
($ millions)	2003 Actual	2004 Actual	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Usage Fees	148.9	152.4	153.9	144.0	145.7	146.0
Market-related Interest Income	4.2	2.5	2.6	2.1	2.3	2.4
Cost Recovery for Services	0.9	0.9	1.1	1.7	1.7	1.8
Total Revenues	**154.0**	**155.8**	**157.6**	**147.8**	**149.7**	**150.2**
OM&A Program Costs	78.1	81.4	83.5	85.9	87.7	90.5
OM&A Pension Expense	4.2	7.4	8.2	16.0	15.6	14.3
Amortization	51.2	52.0	47.6	37.8	41.6	37.6
Net Interest	17.8	9.5	8.3	8.1	6.9	5.7
Total Costs	**151.3**	**150.3**	**147.6**	**147.8**	**151.8**	**148.1**
Operating Surplus/(Deficit)	**2.7**	**5.5**	**10.0**	**0.0**	**(2.1)**	**2.1**
Transfer to the OPA	**0.0**	**0.0**	**(15.0)**	**0.0**	**0.0**	**0.0**
Refund to Market Participants	**0.0**	**0.0**	**0.0**	**(8.9)**	**0.0**	**0.0**
Accumulated Operating Surplus	**13.4**	**18.9**	**13.9**	**5.0**	**2.9**	**5.0**

As depicted above, the IESO is planning to break even in 2006 and then run a minor operating deficit and surplus in 2007 and 2008, respectively. The plan would see the IESO utilize a portion of its $5.0 million accumulated surplus balance to maintain the reduced usage fee in

[5]The forecasted energy demand levels that underpin the revenue forecast included in the plan are 158.4 TWh for 2006, 160.3 TWh for 2007 and 162.8 TWh for 2008.

2007 and would then run a surplus in 2008 to rebuild the accumulated surplus to $5.0 million. In 2008, the operating surplus would be achieved while still providing a further anticipated reduction in fees to market participants. Complete financial statements covering the period 2003 through 2008 are included as Appendix 1.

Total Revenues: 2006-2008



($ millions)	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Usage Fees	153.9	144.0	145.7	146.0
Market-Related Interest Income	2.6	2.1	2.3	2.4
Cost Recovery Fees	1.1	1.7	1.7	1.8
Total Revenues	**157.6**	**147.8**	**149.7**	**150.2**

Total revenues are projected to decrease by approximately $9.9 million in 2006 from levels expected in 2005, due primarily to planned reductions to the IESO usage fee.

Usage fee revenue is forecasted to decrease by $9.9 million in 2006 from the current year projection, with increases of $1.7 million and $0.3 million in each of 2007 and 2008, respectively. The forecasted reduction is primarily reflective of the proposed reduction in usage fee from $0.959/MWh to $0.909/MWh. A reduction of 2.1 TWh from 2005 to 2006 due to reduced export levels is also assumed. The above revenue levels reflect the following energy forecasts: 158.4 TWh in 2006, 160.3 TWh in 2007 and 162.8 TWh in 2008. As stated previously, these forecasted energy levels are based on the most recent 18-month and ten-year forecasts issued by the IESO.

(TWh)	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Outlook Demand Forecast	157.4	156.8	158.3	160.3
Less: Transmission Line Losses [6]	(4.7)	(4.7)	(4.8)	(4.8)
Exports [7]	7.8	6.3	6.8	7.3
Total Energy Levels	**160.5**	**158.4**	**160.3**	**162.8**

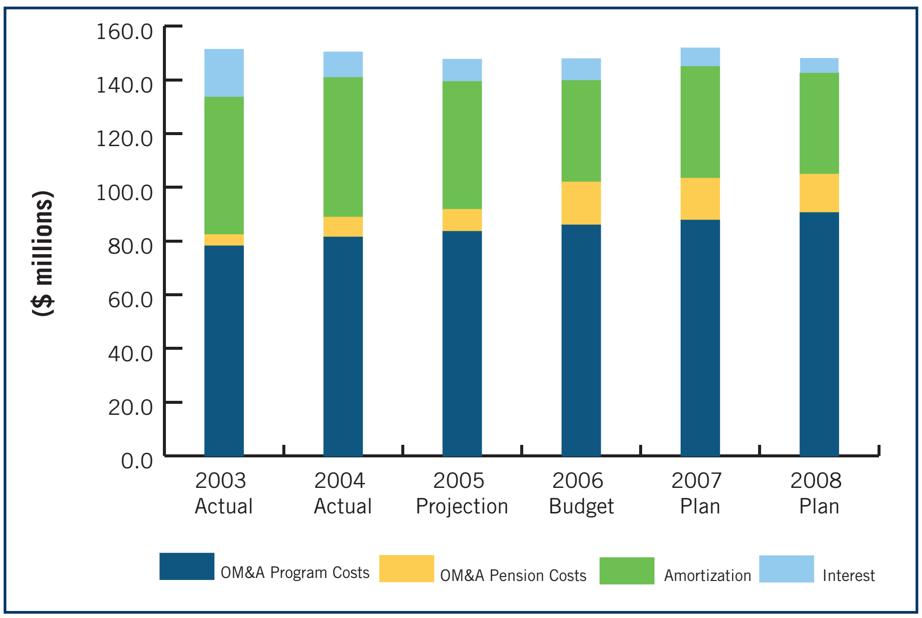
[6] Line losses are assumed to be three per cent.

[7] Exports assumptions are based on a five-year rolling average.

Market-related interest income revenues, which represent investment income earned on market funds as they flow through the settlement cycle, are expected to decrease by $0.5 million in 2006. This reduction is expected to largely result from the elimination of the BPPR, as discussed earlier in this Plan, which is projected to account for $0.6 million of the market-related interest income in 2005.

Cost recovery for services revenues, which are derived from connections assessments and participant training, are expected to increase in 2006 to $1.7 million. In 2007 and 2008, these revenues are forecasted to largely remain flat. The budgeted increase in 2006 reflects the IESO's expectation of increased connection assessment work, accounting for half of the expected increase. The other half of the budgeted increase, or $0.3 million, reflects the estimated volume of work that the IESO will undertake for the OPA on a cost of service basis. This work for the OPA is expected to be in the areas of assessments and reports and some related tools. Since these revenues represent services that the IESO provides at cost, there are corresponding costs within the OM&A program costs for the provision of these services. Accordingly, there is no net impact on the IESO for these services and no impact on the usage fee charged to market participants.

Total Costs: 2006-2008



($ millions)	2003 Actual	2004 Actual	2005 Projection	2006 Budget	2007 Plan	2008 Plan
OM&A Program Costs	78.1	81.4	83.5	85.9	87.7	90.5
OM&A Pension Costs	4.2	7.4	8.2	16.0	15.6	14.3
Amortization	51.2	52.0	47.6	37.8	41.6	37.6
Interest	17.8	9.5	8.3	8.1	6.9	5.7
Total Costs	**151.3**	**150.3**	**147.6**	**147.8**	**151.8**	**148.1**

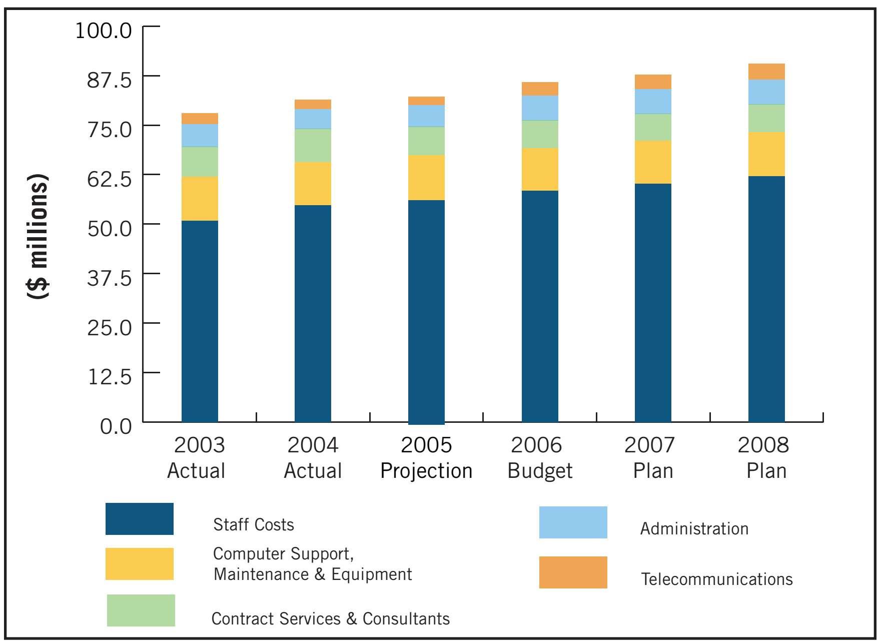
Over the planning period, total costs are expected to remain relatively flat from the anticipated 2005 level. On an annual basis, in 2006, the total costs of the business are anticipated to increase slightly by some $0.2 million, from $147.6 million to $147.8 million. In 2007, total costs are forecasted to increase by $4.0 million, largely reflecting an increase in amortization related to the estimated cost of a DAM, and then reduce in 2008 down to a level that is slightly above the 2005 forecast.

The net changes over the planning period reflect the following:

- Continued aggressive repayment of long-term debt, thereby minimizing interest expenses.
- Annual capital expenditure levels that will continue to result in reduced amortization charges.
- Increases in pension expense, resulting largely from historically low long-term interest rates as well as the continued impact of poor equity market returns from previous years.
- Managed increases in OM&A program costs, reflecting, amongst other things: salary escalation that is principally reflective of existing collective agreements and limited due to the success of continued staff level management; post employment benefits other than pension that are also increasing due to the reduction in long-term interest rates; increased telecommunication costs related to market participant's expanded facilities; and increased rental costs in relation to the IESO's backup operations centre.

The following sections provide the detail and rationale for the changes in each area of cost.

OM&A Program Costs



The following table outlines the OM&A program costs over the planning period.

($ millions)	2003 Actual	2004 Actual	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Staff Costs	50.9	54.8	56.7	58.5	60.2	62.1
Computer Support, Maintenance & Equipment	11.0	10.8	11.3	10.7	10.8	11.1
Contract Services & Consultants	7.6	8.5	7.2	7.0	6.9	7.0
Administration	5.7	4.9	5.5	6.3	6.1	6.3
Telecommunications	2.9	2.4	2.8	3.4	3.7	4.0
OM&A Program Costs	**78.1**	**81.4**	**83.5**	**85.9**	**87.7**	**90.5**

In 2006, OM&A program costs are budgeted to increase by $2.4 million from the prior year, or over two per cent. As evidenced above, the primary reason for this increase relates to an increase in staff costs ($1.8 million), administration expenses ($0.8 million), and telecommunications ($0.6 million).

Staff Costs

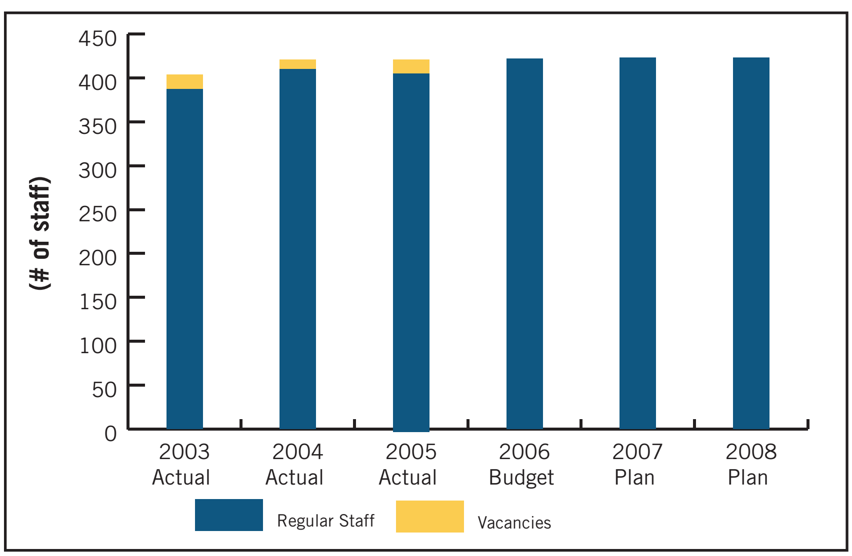
The IESO continues to be a business that is staff intensive in nature. Specific to staffing, over the planning period staff costs represent over forty per cent of the total costs and over sixty-eight per cent of the total OM&A program costs, excluding OM&A pension expense, which although categorized separately nonetheless relate to regular staff. Factoring in the pension expense, staff-related costs account for approximately 50 per cent of total costs in each year of the planning period.

In the first year of the plan, 2006, staff costs are budgeted to increase by about $1.8 million, or about three per cent. This planned cost increase is a result of:

- An increase in the expense for post employment benefits other than pension due to a significant decline of long-term interest rates to 45-year lows. Due to the long-term nature of these costs, a change in long-term interest rates has a large impact on the related obligation on a present value basis; and
- Compensation increases primarily the result of current collective agreements.

What the figures do not show is IESO's commitment to managing staff levels and the large amount of work that is being undertaken to ensure staff levels at the IESO do not increase. As mentioned earlier in this Plan, there are newly created areas of the business – these areas needed to be staffed in order for the business to deliver on stated objectives. In addition, there is an increased volume of work in many of the other areas of the business.

IESO management made a commitment to have no staff level increases in 2006. As a result, staff resources were moved within the business to resource these areas, which include the Stakeholder Engagement and Reliability Assurance. This was accommodated through staff reductions in other areas of the business; namely Information, Technology & Infrastructure; and within Market & System Operations resulting in a net reduction of two staff overall.



The following table outlines the regular staff levels over the planning period:

	2003 Actual[8]	2004 Actual[8]	2005 Actual[9]	2006 Budget	2007 Plan	2008 Plan
Market & System Operations	-	-	192	195	195	195
Information, Technology & Infrastructure	-	-	119	117	118	118
Corporate Relations & Market Development	-	-	32	41	41	41
Corporate Services	-	-	36	37	37	37
Market Assessment & Compliance	-	-	12	13	13	13
Human Resources	-	-	12	12	12	12
Reliability Assurance	-	-	3	5	5	5
Chief Executive Officer	-	-	2	2	2	2
Vacancies	17	11	16	-	-	-
Total Regular Staff Levels	**404**	**421**	**424**	**422**	**423**	**423**

Staffing remains effectively constant over the business planning period.

Computer Support, Maintenance & Equipment

Computer support, maintenance and equipment costs are budgeted to decrease by $0.6 million in 2006 over the 2005 projection. This decrease reflects reduced costs due to the buyout of network equipment at end of lease, desktop equipment and replacement. In later years inflationary pressures are factored in.

In 2007 and 2008, these costs are budgeted to increase only slightly as a result of inflationary pressures.

Contract Services & Consultants

Contract services and consultants are budgeted to decrease by approximately $0.2 million in 2006 from the prior year and then remain fairly consistent across the plan.

Administration

Administrative costs are budgeted to increase in 2006 by $0.8 million, or approximately fifteen per cent over what is anticipated in 2005. This increase is largely due to increased rent costs related to the assumed relocation of our back-up operating centre. Administrative costs are forecasted to remain relatively constant in 2007 and 2008. Administration expenses include memberships in the Northeast Power Coordinating Council, rent, utilities, materials and supplies, rental facilities, building services, and property taxes.

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8 2003 and 2004 actual staff levels are not available for all business units due to the 2005 corporate realignment.

9 2005 actual regular staff levels as of August 31, 2005. Vacancies based on approved 2005-2007 Business Plan.

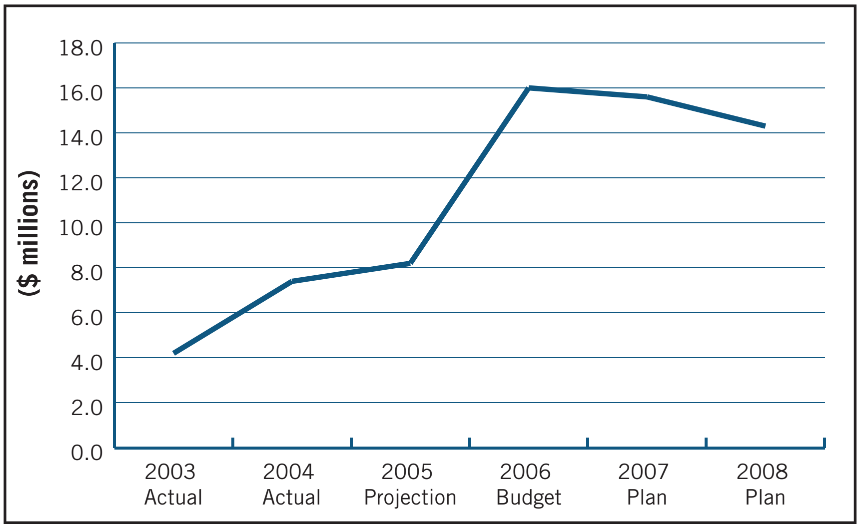
Telecommunications

Telecommunication costs are budgeted to increase by approximately $0.6 million in 2006. This cost increase is expected to result from an increase in the number of leased communication lines to connect to market participant remote terminal units. The increases in 2007 and 2008 reflect anticipated inflationary increases and further remote terminal unit (RTU) expansion.

OM&A Program Costs by Business Unit

OM&A program costs have been outlined by cost type, explaining the associated work. For information purposes, business unit budgets are included in Appendix 2.

OM&A Pension Expense



($ millions)	2003 Actual	2004 Actual	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Pension Costs	4.3	7.5	8.4	16.3	15.9	14.6
Less: Capitalized Pension	(0.1)	(0.1)	(0.2)	(0.3)	(0.3)	(0.3)
Total Pension Expense	**4.2**	**7.4**	**8.2**	**16.0**	**15.6**	**14.3**

Pension expense represents the actuarially estimated accounting cost of providing pension benefits to IESO employees. This expense reflects the proper charge for pension in the IESO's financial statement. Three factors that have a large influence on these expenses are: the institutional arrangements in place; pension plan investment performance; and the critical assumptions utilized.

In terms of institutional arrangements, the IESO has its own pension plan. Therefore, the pension expense to be charged through the usage fee is directly impacted by many variables, including fund performance and interest rate assumptions. For some organizations, they are part of a larger pension plan and their pension expense would represent their required contributions to that plan. Those contribution levels would certainly be impacted by plan performance and changes to assumptions, however, the rate of change is likely to be more measured than those of an individual plan sponsor, like the IESO.

On pension plan investment performance, over the period 2001 through 2004, the IESO earned an average annual return of 3.9 per cent. Although this return exceeded the benchmark (3.4 per cent) over that period, the return was much lower than IESO management's long term assumed rate of return of 7.0 per cent. In particular, in 2001 and 2002, the average annual fund return was a loss of 3.5 per cent - again, better than bench-market (-4.6 per cent) but significantly below the assumed rate of return. These return levels were a result of poor stock market returns. The impact of these returns is that there is less than expected plan assets to invest and this results in lower than expected investment income, driving an increase in pension expense. In recognition of the long-term nature of these obligations, the IESO utilizes a smoothed-value of assets in calculating its pension expense. The effect of this is that actual equity returns are not immediately recognized in the pension expense and this has the effect of smoothing the impact of stronger or weaker than expected returns on pension expense. At the IESO, the poor returns dating back to 2002 continue to be smoothed into the values in the 2006 pension expense. That is why the IESO has been forecasting an increase to pension expense in the outlying plan years since the 2004-2006 Business Plan. Specific to 2006, this accounts for approximately $1.6 million of the budgeted increase.

On pension plan assets, the other factor that impacts the pension expense is the assumed long-term rate of return on plan assets. Due to experience over the past three or four years, the IESO revised its assumption in this area, from 7.25 per cent down to 7.0 per cent. The effect of this change is an estimated increase in pension expense of approximately $0.6 million.

Within the pension equation, on the opposite side of the pension plan assets is the pension liability. That liability represents the actuarially estimated, present-valued liability of the pension promises made to date to IESO employees and retirees. It also estimates the present-valued cost of expected increases in that liability over the coming years. This estimate is impacted by: pension plan details; long-term interest rates; plan membership; mortality and other assumptions and experience, amongst other things.

At the IESO, pension plan provisions have not changed over the last couple of years.

Since this long-term obligation, there is an assumption made as to what interest rate to utilize to present-value the obligation. That interest rate is referred to as the discount rate and, per Canadian Generally Accepted Accounting Principles, that rate should reflect the long-term interest rates, on high quality corporate long bond yields, in effect at the time of measurement. At the IESO, the measurement date is September 30th. For planning purposes, we utilize the rate that is in effect at the beginning of our planning process, with revisions made only if a material change takes place. Over the last few years, long-term interest rates have been dropping significantly. This results in a large increase in the present valued liability and the cost of benefits for the current period (known as the current service cost). The effect of this change is a budgeted increase of some $4.8 million to the IESO's pension expense in 2006.

Lastly, there is a legislative requirement of all pension plan sponsors to undertake a complete actuarial valuation of the plan at least every three years. This valuation is required to help ensure appropriate funding of the pension promise. In 2005, the IESO undertook an actuarial valuation. The effect of this is that it represents an opportunity for a true-up of the plan status to that assumed by the actuaries between valuations. An example of this would be membership profiles – the actuary makes certain assumptions about employees that replace retiring employees. When a valuation is completed, the actual employee population is known, or trued-up. The estimated impact on the 2006 pension expense of these true-ups is an increase of approximately $1.1 million.

The following table summarizes the details of the projected pension expense in 2006.

($ millions)	Current Service Costs	Interest of Benefit Obligation	Expected Return on Assets	Amortization of Experience	Total
Projected 2005 Pension Costs	6.0	18.0	(18.1)	2.5	8.4
Expected Developments	0.2	1.1	(1.3)	(0.2)	(0.2)
Valuation True up – plan membership and member profile	0.5	0.3	0.0	0.3	1.1
Fund Performance	0.0	0.0	0.7	0.9	1.6
Change in discount rate	1.7	(0.2)	0.0	3.3	4.8
Change in return on asset assumption	0.0	0.0	0.6	0.0	0.6
Budgeted 2006 Pension Costs	**8.4**	**19.2**	**(18.1)**	**6.8**	**16.3**

Looking out to 2007 and 2008, based on no change in long-term interest rates and a plan return of 7.0 per cent, the pension expense is expected to decrease modestly each year as less prior year experience losses are recognized.

It is important to recognize that this situation is not unique to the IESO as virtually all corporations with a pension plan are experiencing similar results. Even when equity market returns increased significantly in 2003, 2004, and 2005, the positive effect of these returns on pension expense is overwhelmed by a continued decline in the discount rate (determined by reference to high quality long-term corporate bonds) and the continued recognition, for accounting purposes, of very poor stock market returns in the years 2000 through to 2002.

Capital Spending

Over the planning period, the intent is to make business and tool improvements that are currently estimated to total $25.0 million in 2006, $20.0 million in 2007, and $14.0 million in 2008. This total three-year spending level of $59.0 million, which includes an anticipated spending level for the DAM in the order of $15.0 million, is considerably lower than the actual and projected spending level of $108.9 million for the three-year period ending in 2005.

Given the ongoing need for changes and reprioritization, the IESO does not utilize the business planning process as a mechanism for capital project approval. Rather, through business planning an appropriate capital envelope for future years is established. This practice is consistent with prior years. However, the IESO continues to recognize the need for increased disclosure and information in terms of project-specific capital plans within the business plan.

As such, the following table provides more information on the IESO's capital plan.

($ millions)	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Applications	8.0	16.4	11.7	7.6
IT Infrastructure	6.0	7.1	6.9	5.8
Facility Improvements	0.7	1.5	1.4	0.6
Total Capital	**14.7**	**25.0**	**20.0**	**14.0**

The planned capital spending level of $25.0 million in 2006 represents a $10.3 million increase from the 2005 projected level of $14.7 million. As depicted above, the main increases are within Applications, which includes DAM at $9.0 million, or approximately 90 per cent, of the increase with the remainder of the increase occurring in the areas of IT Infrastructure and Facility Improvements. The following sections outline the various components of the capital program over the planning period.

Applications

Applications represent both functional improvement to existing systems (e.g. Energy Management System/Market Information System) and upgrades or replacements to systems/software. Since most of the IESO's systems were developed and deployed prior to 2002, large portions of the existing systems are planned for upgrade or replacement over the planning period. Current applications require upgrading or replacement to allow for continued functioning with new hardware and to allow for continued support from vendors. In 2005 a total of $8.0 million is projected to be spent in this area. The single largest project within this area is the implementation of Central Alarm Management, which represents $3.0 million of the 2005 costs. The overall project has a total capital cost of $3.2 million. In 2006, capital spending on applications related to system improvements and software upgrades is expected to decrease slightly to $7.4 million (excluding DAM), with further reduced spending levels in 2007. The identified projects are included in Appendix 3.

As outlined previously in this document, the IESO is investigating alternative day-ahead mechanisms in 2005. The results of this analysis are to be presented to the IESO Board of Directors in the fourth quarter of 2005. At that time, the planned direction will be increasingly solidified. Until that time, for planning purposes, this Plan assumes spending of $15.0 million on day-ahead mechanisms, $9.0 million in 2006 and $6.0 million in 2007. The Plan is also premised on the resulting capital assets going in-service in the first quarter of 2007.

IT Infrastructure

IT Infrastructure represents capital initiatives directed at maintaining and, as necessary, enhancing the overall technology backbone of the IESO. In 2005, the projected level of spending in this area totals $6.0 million. This spending level increases to $7.1 million in 2006 before declining in future years. Similar to most systems within the IESO, most of the IT infrastructure has been in service for a number of years, in many instances dating back to 2001 or earlier. Therefore, consistent with the need identified in last year's business plan, investment in the IESO's infrastructure is necessary to reasonably ensure the information backbone of the IESO remains effective, reliable, and efficient. The identified projects are included in Appendix 3.

Facility Improvements

Other capital projects represent improvements to the physical assets of the IESO, such as heating, ventilation and air conditioning (HVAC) and fire detection system upgrades.

These detailed capital plans, including those in Appendix 3, represent the best current view of the IESO.

Throughout the planning period, based on shifting priorities, opportunities, and challenges, the actual plan executed may differ from that outlined in this plan. Within the IESO, all capital projects require Business Unit Leader, President and CEO, or Board of Directors approval as appropriate prior to initiation.[10]

Asset Service Lives

As part of the business planning exercise, IESO management undertakes a review of the service lives utilized in its amortization of capital assets. This activity involves a review of existing assets against the proposed capital plan as well as a review of any service life changes that were required during the year. Ultimately, this review is undertaken to determine if there is a need to reduce existing service lives due to early replacement or sufficient support for the prudent extension of any asset lives.

In its 2003 and 2004 reviews, the IESO revised service lives. In 2003, the revisions served to shorten some service lives on IT infrastructure assets, resulting in service lives of IT infrastructure assets that typically range from three years (small servers) to five years (communications network). In 2004, the revisions served to change service lives on some of the IESO's major market systems, resulting in service lives that range from about four years (market participant interface) to seven and an half years (Energy Management System).

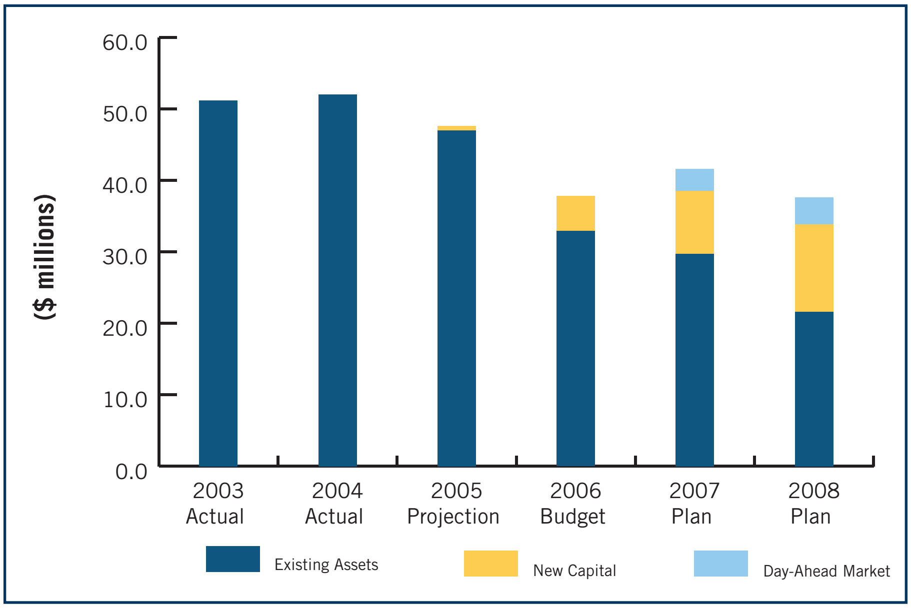
The review undertaken as part of 2006-2008 planning did not identify a need for any service life adjustments.

[10] Business Unit Leaders can approve capital projects up to $200,000, President & CEO can approve capital projects up to $4.0 million, and the board of Directors approves all capital projects in excess of $4.0 million.

Amortization Expense over the Planning Period

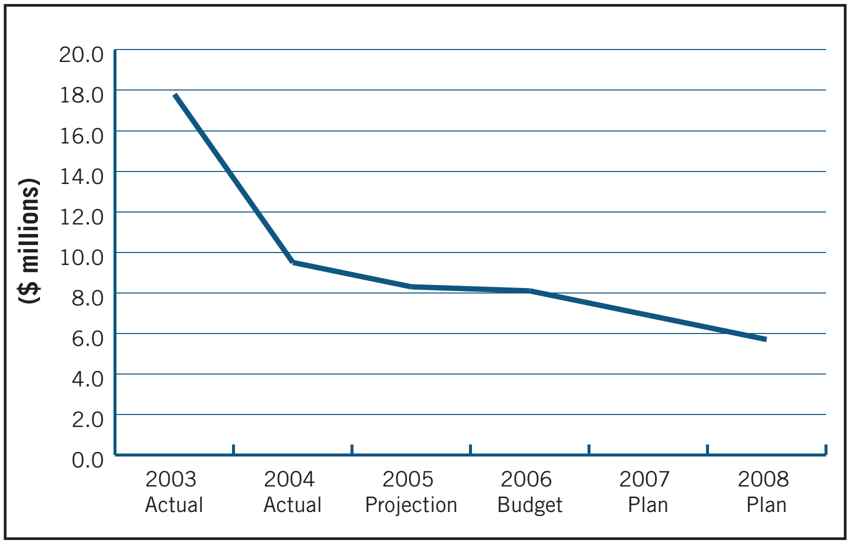
Over the planning period, annual amortization expense is anticipated to decrease by $10.0 million from the projected 2005 level. At a high level, this reduction reflects the IESO's success in utilizing some information system infrastructure longer than originally planned and the lowering of costs for replacement infrastructure. As well, for those applications that are being upgraded or replaced over the planning period, the expectation is that this work will cost less than the original implementation due to increased IESO knowledge and the added cost of initial development that result from the development of the market rules in parallel to the development of the systems.

The following table outlines the details of the amortization expense over the planning period:



($ millions)	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Existing Assets In-Service	47.0	32.9	29.7	21.6
New Capital	0.6	4.9	8.8	12.2
Day-Ahead Market	0.0	0.0	3.1	3.8
Total Amortization	**47.6**	**37.8**	**41.6**	**37.6**

Net Interest Expense



($ millions)	2003 Actual	2004 Actual	2005 Projection	2006 Budget	2007 Plan	2008 Plan
Net Interest Expense	17.8	9.5	8.3	8.1	6.9	5.7

The interest expense over the planning period is largely based on the following financing strategy.

Financing Strategy

At the beginning of 2005, the unsecured long-term debt of the IESO was comprised of the following notes payable:

- $125.0 million held by the Province of Ontario, repayable on March 31, 2007, bearing a floating rate of interest of Bankers Acceptance rate plus 50 basis points, reset quarterly.
- $78.2 million held by Ontario Electricity Financial Corporation ("OEFC"), repayable on May 1, 2009, bearing a fixed interest rate of 7.9 per cent.

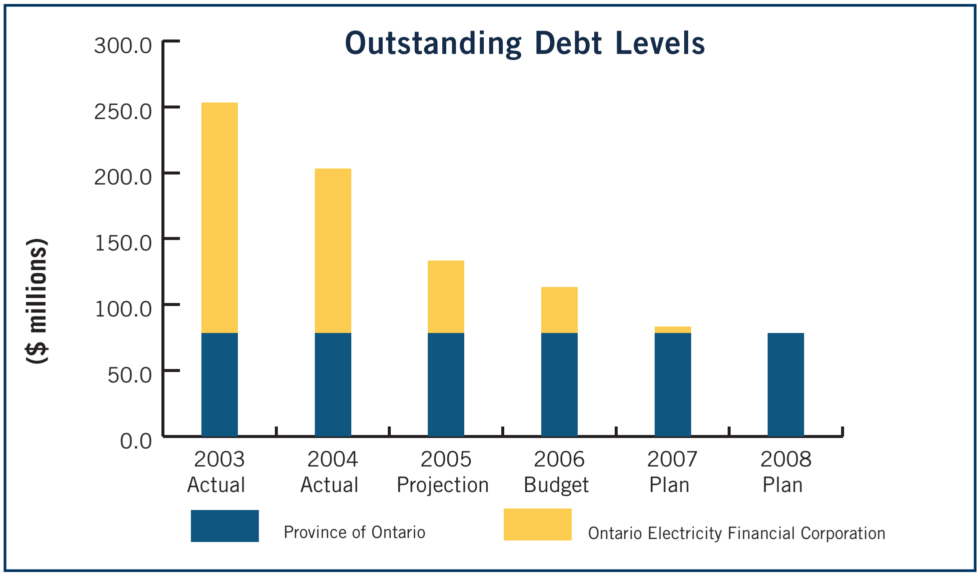
The debt with OEFC is expected to remain in effect for the duration of the planning period and will result in $6.2 million of interest annually.

As anticipated in last year's Plan, the IESO repaid $50.0 million of the Province of Ontario debt in 2004 and is projecting to have repaid a further $70.0 million by the end of 2005.

Over the planning period, the following are the assumed average interest rates on this debt for each year over the planning period:

- 2006: 3.8 per cent
- 2007: 4.1 per cent
- 2008: 4.3 per cent

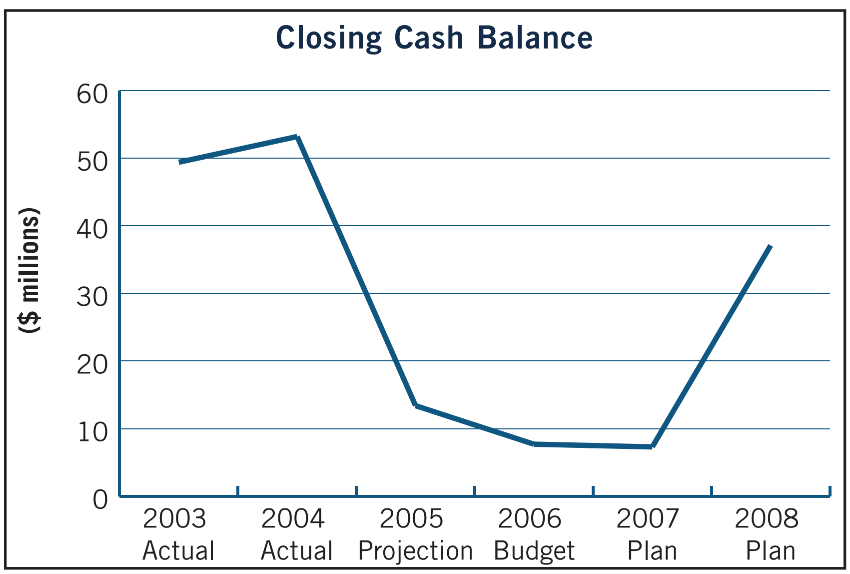
In addition, based on budgeted cash flows, the IESO anticipates sufficient cash to facilitate repayment of $20.0 million of the Province of Ontario debt in 2006, $30.0 million in 2007 and the final $5.0 million in 2008.



The financing strategy above outlines the plan to continue to reduce the IESO's long-term debt over the planning period. The resulting interest costs, which accordingly reduce over the planning period, are estimated as follows:

- $8.3 million in 2006;
- $7.1 million in 2007; and
- $6.3 million in 2008.

Over the planning period, the IESO intends on maintaining adequate cash balances, while still enabling debt repayments as outlined above. The following chart depicts the planned closing cash balances from 2003 through 2008.



The investment of this cash will result in investment income that will partially offset interest expense. The assumed average rates of return on investments are 3.0 per cent in 2006, 3.1 per cent in 2007 and 3.3 per cent in 2008. These rates are in comparison to a forecasted rate of return on 2005 investments of 2.6 per cent.

The resulting expected investment incomes are:

- $0.3 million in 2006;
- $0.3 million in 2007; and
- $0.9 million in 2008.

The IESO also maintains two separate lines of credit: $10.0 million for corporate contingency needs; and $100.0 million for market settlement needs. The costs of these lines of credits, aside from any interest on drawn amounts, include stamping fees and a standby charge. In total, this represents an annual cost of approximately $0.3 million in each of the planning years.

Lastly, for large and enduring projects, the IESO capitalizes interest on funds expended prior to the project being placed in-service. Over the planning period, this would include the Day-Ahead Market.

The resulting capitalized interest is:

- $0.2 million in 2006; and
- $0.2 million in 2007.

The following table outlines resulting net interest expense over the planning period:

($ million)	2003 Actual	2004 Actual	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Interest on Long-term Debt	21.5	10.1	8.9	8.3	7.1	6.3
Investment Income	(3.7)	(1.1)	(0.9)	(0.3)	(0.3)	(0.9)
Financing Charges	0.4	0.5	0.3	0.3	0.3	0.3
Capitalized Interest	(0.4)	0.0	0.0	(0.2)	(0.2)	0.0
Net Interest Expense	**17.8**	**9.5**	**8.3**	**8.1**	**6.9**	**5.7**

As depicted in the above table, due to debt repayment and reduced interest rates, the overall interest expense is projected to have been reduced by $2.6 million, or over 31 per cent, over the three-year planning period.

Ensuring Coordination and the Efficient Use of Resources with the OEB & OPA

Consistent with stakeholder expectations, the IESO is working with the OEB and OPA to ensure the most efficient use of resources.

Ontario Energy Board

Under Bill 100, the Market Surveillance Panel (MSP) was transferred from the IESO to the OEB. In 2004, the direct costs for the MSP were slightly less than $0.2 million, representing the panel member's remuneration and associated expenses. In 2005 and thereafter, these costs were not included in the IESO's 2005 budget. In addition to the direct panel costs, there are costs associated with ongoing staff support of the MSP. Historically, these formed part of the costs for the IESO's Market Assessment and Compliance Division (MACD). In 2005, the IESO and OEB agreed that it was most efficient to have the support of the MSP continue to be provided by the IESO's staff in MACD. These efficiencies result from the fact that most of the analysis required to support the MSP is identical to work which the IESO needs to continue to perform in its role of market operator. Annually, these arrangements are estimated to achieve in the area of $500,000 in efficiencies. As these are costs that would be incurred by the IESO to meet its own responsibilites, there is no cost recovery from the OEB.

The *Protocol Relating to Market Surveillance Panel*, between the IESO and the OEB, was formally put in place on April 25, 2005 [11]. This agreement formalizes the arrangement between the two parties.

Ontario Power Authority

Bill 100 and its associated regulations introduced new market settlement requirements of the IESO to effect changes for such matters as the global adjustment and regulated rates on OPG assets. In effect, this placed upon the IESO a requirement to settle the marketplace and provide the OPA with the settlement information they need. This was completed in 2005. As this work is governed by legislation, there is no cost recovery aspect to this effort.

In 2005, the IESO also provided support to the OPA in its establishment through the provision of corporate and topic-specific policies, procedures and education on how the IESO operates. This support was provided on an ad hoc basis and did not require a significant amount of time by IESO staff, however the provision of this support and information likely resulted in savings to the OPA.

Going forward, given their roles in the domains of system reliability and system planning, the IESO and OPA, respectively, will have a need to share information. That sharing of information will be governed by formalized non-disclosure agreements.

Also, although the creation of the OPA resulted in the establishment of an organization to undertake activities within the electricity sector that were not previously being done, there are opportunities for the IESO to work with the OPA to help ensure efficiencies for all of Ontario. In 2005, the IESO and OPA have held, and continue to hold, discussions on how the IESO's expertise and information can be best leveraged by the OPA. This has resulted in gen-

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11 See http://www.oeb.gov.on.ca/documents/msp_protocol_250405.pdf.

eral agreement that there are some areas of the OPA's work that are best undertaken by the IESO on a fee-for-service basis. Some of this support will likely be in the areas of analysis to identify: transmission enhancements needed to connect new generation; current or potential transmission system or area supply deficiencies; short-term assessments of resource adequacy; transient stability studies, data model runs; and the use of various tools. Accordingly, the IESO include $300,000 in IESO revenues with a corresponding $300,000 OPA costs to reflect the provision of these services.

YEAR 2006 REGULATORY APPROVALS

This section details the calculation of IESO fees for which approvals will be requested from the OEB for the year 2006. The fees are set in the context of all revenue sources for the IESO, followed by detailed rationale, derivation and amounts.

Revenue Sources

There are several sources of revenue for 2006:

- Cost Recovery for Services
- Interest Earned on Market Settlement Funds
- Revenue from IESO Fees

Cost Recovery for Services

The IESO will continue in its plan to recover the cost of services that are directly attributed to a participant, such as training, assessments, and other services rendered to the Ontario Power Authority on a cost recovery basis. In aggregate, total revenues from cost recovery in 2006 is estimated at $1.7 million.

Interest Earned on Market Settlement Funds

As per the market rules, at the end of each year, monies which have been earned from interest on market settlement funds are applied to off-set the IESO administration charge in the following year. This market-related interest income is projected to be $2.1 million for the year 2006.

Revenue from IESO Fees

The IESO's fee methodology was approved by the OEB in 2000. The fee structure, which has been in effect since market opening, includes an application fee of $1,000 per application plus a $/MWh usage fee. The revenue from application fees is expected to be negligible in 2006.

Usage Fee

This section derives the fee for the year 2006 for approval of the OEB, and provides a projection for 2007 and 2008.

The calculation of the IESO usage fee starts by calculating the revenues to be recovered by this fee as shown in the following table:

Revenue Requirement Calculation for IESO Usage Fee (in $ million)	**Year**		
	2006	2007	2008
Revenue Requirements	147.8	151.8	148.1
Less: Other Revenues			
• Cost recovery for services	1.7	1.7	1.8
• Interest earned on market funds	2.1	2.3	2.4
• Deferral account balance allocation	0.0	2.1	(2.1)
Revenue Requirement to be recovered by IESO Usage Fee	**144.0**	**145.7**	**146.0**

The second step is to estimate the charge determinant for the usage fee. It is the total AQEW (Allocated Quantity of Energy Withdrawn) for the year, including exports out of Ontario:

Year	**18-Month & 10-Year Outlook Demand Forecast (TWh)**	**-**	**Transmission Line Losses (TWh)**	**+**	**Export (TWh)**	**=**	**Forecast AQEW (TWh)**
2006	156.8	-	4.7	+	6.3	=	158.4
2007	158.3	-	4.8	+	6.8	=	160.3
2008	160.3	-	4.8	+	7.3	=	162.8

The third step is the rate calculation:

Year	**Revenue Requirement To Be Recovered ($ million)**	**÷**	**Forecast**	**=**	**Usage**
2006	144.0	÷	158.4	=	0.909
2007	145.7	÷	160.3	=	0.909
2008	146.0	÷	162.8	=	0.897

Implementation of 2006 usage fee

Pending approval by the OEB for the 2006 usage fee, the IESO will continue to charge the 2005 usage fee to market participants. Once the approval is rendered by the OEB, the IESO will rebate to market participants the difference between the old and new usage fee based on the allocated quantity of energy withdrawn for the period January 1, 2006 and the end of the month in which the approval is rendered by the OEB. The rebate will be redirected to market participants in the next billing cycle following the month in which the approval is rendered by the OEB.

Disposition of Deferral Account Balance Surplus

Based on the Settlement Agreement, which was accepted by the OEB on March 18, 2005, any surplus held by the IESO at the end of a year in excess of $5.0 million is returned to the market participants in the form of a rebate in the following year, based on the market participant allocated quantity of energy withdrawn during the prior year.

Overall, the 2005 projected operating results would result in an accumulated operating surplus of $13.9 million by year-end. This is determined by adding last year's actual accumulated surplus of $18.9 million, less the $15.0 million in funding for the Ontario Power Authority, to this year's projected surplus of $10.0 million. The IESO is estimating a refund of approximately $8.9 million.

The final amount to be refunded will be based on the IESO's audited financial statements for the fiscal year 2005 and the refund will be rebated to market participants in the next billing cycle following the month in which the 2005 financial statements are approved by the IESO Board of Directors.

APPENDIX 1: FINANCIAL STATEMENTS

Actual and Pro Forma Statement of Operations and Accumulated Surplus/(Deficit)
For the Year Ended December 31
(in Millions of Canadian Dollars)

	2003 Actual	2004 Actual	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
REVENUES						
Usage fees	148.9	152.4	153.9	144.0	145.7	146.0
Market-related interest income	4.2	2.5	2.6	2.1	2.3	2.4
Cost recovery for services	0.9	0.9	1.1	1.7	1.7	1.8
Total Revenues	**154.0**	**155.8**	**157.6**	**147.8**	**149.7**	**150.2**
EXPENSES						
OM&A program costs	78.1	81.4	83.5	85.9	87.7	90.5
OM&A pension expense	4.2	7.4	8.2	16.0	15.6	14.3
Amortization	51.2	52.0	47.6	37.8	41.6	37.6
Net Interest	17.8	9.5	8.3	8.1	6.9	5.7
Total Expenses	**151.3**	**150.3**	**147.6**	**147.8**	**151.8**	**148.1**
Operating Surplus/(Deficit)	**2.7**	**5.5**	**10.0**	**0.0**	**(2.1)**	**2.1**
Accumulated Operating Surplus - End of Year	**13.4**	**18.9**	**13.9**	**5.0**	**2.9**	**5.0**
Market-related Penalties & Fines	2.2	0.3	0.1	0.0	0.0	0.0
Customer Education Fund Expenditures	0.0	(0.1)	(1.1)	(1.2)	0.0	0.0
Accumulated Fines and Penalties - End of Year	**2.2**	**2.4**	**1.4**	**0.2**	**0.2**	**0.2**

Actual and Pro Forma Statements of Financial Position
As at December 31
(in Millions of Canadian Dollars)

	2003 Actual	2004 Actual	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
ASSETS						
Current Assets						
Cash & cash equivalents	36.9	7.3	13.4	7.7	7.3	37.1
Temporary investments	12.5	45.9	0.0	0.0	0.0	0.0
Accounts receivable	17.8	18.3	17.6	17.0	17.3	17.4
Short-term prepaid expenses	1.5	1.9	1.9	1.9	1.9	1.9
	68.7	**73.4**	**32.9**	**26.6**	**26.5**	**56.4**
Property & Equipment						
Property & equipment in service	319.7	327.3	336.4	360.0	389.0	403.0
Less: accumulated amortization	(108.3)	(160.1)	(207.7)	(245.5)	(287.1)	(324.7)
Net Book Value	211.4	167.2	128.7	114.5	101.9	78.3
Construction-in-progress	1.7	2.0	7.6	9.0	0.0	0.0
	213.1	**169.2**	**136.3**	**123.5**	**101.9**	**78.3**
Other Assets						
Long-term investments	6.5	8.0	9.3	11.3	13.4	15.5
Prepaid pension expense	24.6	22.1	21.8	13.6	5.9	(0.5)
	31.1	**30.1**	**31.1**	**24.9**	**19.3**	**15.0**
TOTAL ASSETS	**312.9**	**272.7**	**200.3**	**175.0**	**147.7**	**149.7**
LIABILITIES						
Current Liabilities						
Accounts payable & accrued liabilities	16.4	17.9	18.9	18.9	18.9	18.9
Accrued interest	2.0	1.7	1.0	1.0	1.0	1.0
Current portion of long-term debt	0.0	0.0	0.0	35.0	5.0	78.2
	18.4	**19.6**	**19.9**	**54.9**	**24.9**	**98.1**
Long-term debt	253.2	203.2	133.2	78.2	78.2	0.0
Accrual for employee future benefits other than pension	25.7	28.6	31.9	36.7	41.5	46.4
TOTAL LIABILITIES	**297.3**	**251.4**	**185.0**	**169.8**	**144.6**	**144.5**
ACCUMULATED SURPLUS	**13.4**	**18.9**	**13.9**	**5.0**	**2.9**	**5.0**
Accumulated Fines and Penalties	2.2	2.4	1.4	0.2	0.2	0.2
TOTAL LIABILITIES & ACCUMULATED SURPLUS	**312.9**	**272.7**	**200.3**	**175.0**	**147.7**	**149.7**

Actual and Pro Forma Statement of Cash Flows
For the Year Ended December 31
(in Millions of Canadian Dollars)

	2003 Actual	2004 Actual	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
OPERATING ACTIVITIES						
Operating surplus/(deficit) for the period	2.7	5.5	10.0	0.0	(2.1)	2.1
Market Participant Rebate	0.0	0.0	0.0	(8.9)	0.0	0.0
Market Penalties and Fines	2.2	0.3	0.1	0.0	0.0	0.0
Customer Education Fund Expenditures	0.0	(0.1)	(1.1)	(1.2)	0.0	0.0
Amortization	51.2	52.0	47.6	37.8	41.6	37.6
Decrease in Prepaid Pension Expense	4.3	7.5	8.5	16.4	15.9	14.6
Increase in Accrual for employee future benefits	3.3	4.0	4.5	6.0	6.1	6.3
Pension plan contributions	(4.4)	(5.0)	(8.2)	(8.2)	(8.2)	(8.2)
Payment of employee future benefits	(1.0)	(1.1)	(1.2)	(1.2)	(1.3)	(1.4)
Changes in Non-cash items related to Operations	(3.0)	0.9	1.0	0.6	(0.3)	(0.1)
Cash Provided from Operations	**55.3**	**64.0**	**61.2**	**41.3**	**51.7**	**50.9**
INVESTING ACTIVITIES						
Net Sale (Purchase) of Temporary Investments	52.7	(33.4)	45.9	0.0	0.0	0.0
Purchase of Long-Term Investments	(6.5)	(1.5)	(1.3)	(2.0)	(2.1)	(2.1)
Investment in Property & Equipment	(12.4)	(8.7)	(14.7)	(25.0)	(20.0)	(14.0)
Cash Used in Investing Activities	**33.8**	**(43.6)**	**29.9**	**(27.0)**	**(22.1)**	**(16.1)**
FINANCING ACTIVITIES						
Retirement of long-term debt	(100.0)	(50.0)	(70.0)	(20.0)	(30.0)	(5.0)
Draw on contribution to the OPA	0.0	0.0	(15.0)	0.0	0.0	0.0
Cash Provided from Financing Activities	**(100.0)**	**(50.0)**	**(85.0)**	**(20.0)**	**(30.0)**	**(5.0)**
Net Change in Cash Flow	**(10.9)**	**(29.6)**	**6.1**	**(5.7)**	**(0.4)**	**29.8**
Cash and Cash Equivalents - Beginning of Year	**47.8**	**36.9**	**7.3**	**13.4**	**7.7**	**7.3**
Cash and Cash Equivalents - End of Year	**36.9**	**7.3**	**13.4**	**7.7**	**7.3**	**37.1**

APPENDIX 2: OM&A - BUSINESS UNIT DETAILS

($ millions)	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Market & System Operations	26.9	27.5	28.1	28.7
Information Technology & Infrastructure	32.4	33.1	33.9	35.1
Corporate Relations & Market Development	6.8	7.6	7.9	8.1
Corporate Services	7.7	8.0	8.0	8.2
Market Assessment & Compliance	2.2	2.1	2.1	2.2
Human Resources	2.5	2.5	2.5	2.5
Reliability Assurance	0.5	0.9	0.9	1.0
Chief Executive Officer	3.0	3.1	3.1	3.2
Board of Directors	0.7	0.8	0.8	0.8
Market Evolution Program	2.3	0.0	0.0	0.0
Corporate Items	6.7	16.3	16.0	15.0
Total OM&A	91.7	101.9	103.3	104.8
Less: Pension Expense	8.2	16.0	15.6	14.3
OM&A Program Costs	**83.5**	**85.9**	**87.7**	**90.5**

Due to the corporate realignment in 2005, reliable comparative figures are unavailable for 2003 and 2004.

APPENDIX 3: CAPITAL PROJECTS[12]

Applications

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Central Alarm Management	Comprehensive improvements to system alarms related to IESO's operations to provide integrated management and prioritization of alarms addressing: Electrical Systems and Grid; Market Conditions and Events, and IT Systems in order to: reduce the frequency of failed IESO services; decrease the duration of failed IESO services; and help IESO meet its corporate objectives.	3.0	0.5		
Application Changes/ VCR's	A funding envelope, to support minor changes to IESO applications. Allocation of these funds is managed by a cross-functional IESO team, the IT User Committee, comprised of representatives of all business units. Funding release is supported semi-annually via a business case submission.	2.7	2.0	2.0	2.0
Outage Management (IOMS)	Provide an automated and integrated real-time outage tool to deliver significantly improved outage management services. Currently two separate applications: Integrated Outage Management System (IOMS) and Outage Scheduler (OS), provide outage management services for submitting, modifying and viewing outage information. A single new automated and integrated application will improve data validation, on-line viewing of outage information, improved planning capability, and reduced process inefficiencies. It will also provide IESO staff with additional capability to perform performance tracking, and will reduce internal process inefficiencies. The project would result in IESO being able to determine security limits with greater accuracy thereby positively impacting on the efficiency and security of the IESO-controlled grid.	0.5	0.6		

12 Costs included in this table represent the forecasted cost in the year. Some projects may have actual costs prior to 2005 or forecasted costs beyond 2008.

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Security Software Enhancements	Provide upgrades, improvements and additions to enhance and reinforce the IESO's current cyber security architecture and contribute toward ensuring compliance with evolving Audit, NERC and Access Control standards and contribute to maintaining IESO's cyber security posture at a level consistent with those evolving threats and security practices elsewhere. Deliverables include: External Firewall re-configuration; Improved Anti-Virus protection; Improved Intrusion Detection Software / Intrusion Protection Software; Improved SPAM control; Additional firewall hardware and software to improve internal electronic access controls; Improved administration of the Content Management Software and; Authentication Software.	0.3	0.2		
NERC Cyber Security	Satisfy the requirements of recent NERC Standards CIP-002 through CIP-009 by improving Authentication software and associated hardware to integrate logical and physical access controls; Hardware/software for centralized logging; Hardware/software to capture network traffic; Hardware/software for forensic analysis and detection; Software used to monitor compliance with security related policies and procedures; Security awareness training software and an associated delivery vehicle	0.3	0.2		
Enterprise Risk Management Tool	Deliver a tool that allows for complete and adequate documentation of risks, controls and mitigation activities to support the implementation of Enterprise Risk Management across the IESO. This project will enable the IESO to better monitor, assess and react on a timely basis. The current process is not supported by an efficient tool capable of dealing with risk management needs in the future.		0.3		
Server Management Software	Provide tools and processes for centralized administration of servers and desktop computers, automating routine tasks, reducing business risk through security patch management, and providing on-line backup/recovery to minimize downtime. Expected benefits include improved security administration, improved response time and lower desktop administration costs.	0.3			

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Human Resource Information System Upgrade	Upgrade the IESO's corporate human resources information system (HRIS) for time and exception reporting and for payroll processing and maintenance of employee related information. The current system was commissioned in 1999 and no system upgrades have been performed since that time. The new products will provide an efficient Employee Self Service capability which will permit employees to report their time directly without the need for manual entry by a time reporting clerk.	0.1			
Desktop Management Software Tool	Provide tools and processes for centralized administration, automating routine tasks, reducing business risk through security patch management, and providing on-line backup / recovery to minimize downtime for desktop computers. Expected benefits include improved security administration, improved response time and lower desktop administration costs.	0.1			
Energy Management System/Market Information System Upgrade	Upgrade the EMS/MIS which monitors and facilitates the reliability of the IESO controlled grid, and supports market operations. The upgrade will extend the life of the current systems from 2008 to 2011 (when the current operating system will no longer be supported). The upgrade is required to maintain system performance, provide improved functionality and reduce the support burden.		3.0	2.0	
PLC Replacement	The Participant Lifecycle (PLC) System is the primary repository of market participant data at the IESO and is used to provide this data to the critical market systems. Improvements will address handling of contact information, integrate information currently stored in the Facilities Registration database and address meter registration issues.			0.2	0.2
Records Management Replacement	Replace the IESO's existing Foremost Records Manage-ment system; the vendor will cease all support for this software in 2007. Replacement is required to maintain the existing records management system capabilities and to accommodate increased storage needs.				0.2

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Control Room Log Replacement	Improve the system for retaining Control Room Logs in order to improve the accuracy of the logs for downstream processes. The project will; Integrate manually entered notes and actions with specific events detected by the Central Alarm Manager to reduce the effort required to create accurate logs of operational issues; Provide IESO staff with improved status information about log items; Simplify communication between shift changes about outstanding log items, and; Provide reports and views of the logs to authorized users outside of the control room.			0.3	
FRS Replacement	Replace the current File Routing System (FRS) when it reaches end of life in 2007. The FRS is a core element of the IESO's Information Publishing System (IPS) and is responsible for moving files between various systems at the IESO. The project will also: Move to an event-driven service-oriented architecture; Change the FRS logic to use server domain name instead of IP address to reduce costs associated with changes; Add capability to handle UNIX symbolic links, and; Add the capability to interface with the Central Alarm Management System.			0.3	
Automated Document System Replacement	Replace the current Automated Document System (ADS) when it reaches end of life in 2008. The ADS is the core IESO report generation system and will become the primary system for report creation in 2006 once the remaining report systems such as Actuate and BRIO SQR are decommissioned and reports migrated to ADS.				0.2
ODS Replacement	Replace the current Operational Data Store (ODS) when it reaches end of life in 2008. This replacement will look after the re-architecture of the ODS system and redevelopment of the data preparation modules to Java from PLSQL. If performance and reliability continue to be a problem it may be necessary to do some of this work prior to 2008 and through a refresh of underlying technology.				0.2
Lawson & Essbase Upgrade	Upgrade primarily the Lawson and Essbase corporate financial systems to be on a current platform and technology with applications supported by the vendor.				0.6
Day-Ahead Market			9.0	6.0	

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Market Participant Interface Modernization	Provide market participants with greater convenience in connecting to IESO systems and improved security management to the IESO. Other objectives are to reduce IESO maintenance costs, support internal and external Identity Management and enforce standards in the deployment of market facing applications such as the Real Time Web Interface, Message Exchange Day Ahead Market, Outage Management System, Report Navigation Interfaces and new workflow applications.	0.7	0.2		
Customer Information System	Deliver an off-the-shelf Customer Information System that would facilitate improved customer support by tracking customer contacts, characteristics, issues and activities in an integrated fashion throughout the IESO. It would also provide significantly enhanced reporting capabilities.		0.2		
Real-Time Web Interface – Phase 4	Consolidate the technologies used to support the provision of data on the Today's Market and Today's Market: Power View pages of IESO's web site and enhance the Real Time Web Interface application to address a number of functional deficiencies. These enhancements will lead to improved operational efficiency and reduced costs.		0.2		
Outbound Report Management System Upgrade	Deliver an upgrade of the functionality of outbound reports to the public and to market participants			0.3	
Publishing Tool Replacement	Deliver a tool which provides more flexible and feature rich security and adequacy assessment functions, the results from which are published to the marketplace in XML format. The objective is, by streamlining and automating the process, to reduce manual effort by staff, and simplify by removing the requirement for IESO to maintain Oracle Forms development specialist skills.			0.3	
Corporate Web Site Replacement	Replace the current corporate web site and migrate it into the Market Portal which is being delivered as part of the Market Participant Interface Modernization project in 2005/2006 and will build towards a single entry point to the IESO. This is a replacement project based on the Lifecycle Management Unit (LMU) model.			0.2	
Real-time Commercial Reconciliation System Upgrade	This project upgrades the Commercial Reconciliation System and its Graphical User Interface (GUI) from the current version and will put the settlement process on an up-to-date technology platform that is supported by the vendors. This will result in reduced support costs and a system which is compatible with IESO technology standards.				1.0

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Meter Trouble Report and Notice of Disagreement Upgrade	Place the Meter Service provider/Market Participant facing MTR and NoD workflow systems on a current platform and technology with applications supported by the vendor.				0.6
Message Exchange Upgrade	Enhance the functionality of and upgrade the technology of the Web based message exchange facilities. This project will: Deliver a web based message exchange system that can fully support dispatch instructions and dispatch advisories (not currently available) ; Include market participant requested changes to support distributed messaging; Upgrade the system to run on currently supported technologies and; Decommission the older ICCP-based message exchange.				0.2
Market Transaction Interface Replacement	Replace aging and not-cost-effective hardware and software that implements the existing market transactions into the standard IESO Market Participant Interface (MPI) portal. It will also complete the migration of original MPI components provided by the original vendor onto a standards based platform. This project will also: Integrate the energy market transaction data entry forms and application interfaces into the IESO portal; Provide standards and processes for integrating all market participant transactions into a single interface; Simplify and streamline IESO ability to deploy new transactions; Decommission the existing Market Operating System Web services.				0.1
Transmission Rights Auction Replacement	Provide a number of user-driven improvements, and facilitate auctions more efficiently. Deliverables include: New features identified by market participant users, features that offer cost benefits to the IESO; Integrating transmission rights user interfaces into the IESO portal; Integrating transmission rights market participant transactions into market transaction interface application, and; Decommissioning of hardware and infrastructure software that is no longer cost effective to maintain and operate.				0.1
Provision for unidentified Projects	This is an estimate of expenditures for currently undefined capital projects, used for planning purposes.			0.1	2.2
TOTAL APPLICATIONS		**8.0**	**16.4**	**11.7**	**7.6**

IT Infrastructure

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Windows Server Infrastructure Replacement Phase 2& 3	Replace aging Windows server infrastructure (Hardware & Software), much of which no longer has Vendor support in order to reduce associated business risk (Security, Reliability) and operational costs (Parts, Support & Maintenance). This core infrastructure project will lay the foundation for reduced operational costs, reduce the number of Windows servers, simplify the environment, increase E-Mail reliability and address security concerns. Phase 2 will facilitate the replacement of the current E-Mail system, the selection of a new server hardware vendor and the building of a new core MS Windows Server 2003 infrastructure. This phase provides the foundational architecture that is essential for the subsequent migration of IESO's corporate business applications in WSIR Stages 3, 4 and 5. Phase 3 will facilitate the deployment of the new E-Mail system, core Windows infrastructure and the migration of 30 business critical servers.	1.5	1.5		-
Backup Infrastructure Enhancements	Improve performance and capacity of the Corporate Tape Backup system, which is currently reaching full capacity and end of life.	0.7	0.3		
MV90 Reliability Improvement Project	Upgrade MV90 Hardware including servers, operating systems and database engine to ensure continuing ability to meet electricity market needs and deliver expected performance and reliability levels of MV90 market data acquisition system for up to 5 years, The system is currently at the end of its technological life cycle and is experiencing challenges due to increasing data volumes.	0.5			
Telecom Expansion Program	Upgrade and refresh technology to ensure the continued reliability, security and scalability of the IESO's voice systems expansion and address recommendations made following the August 2003 Blackout This project will facilitate a more efficient call accounting and call reporting, a reliable secondary means of communication with critical market participants as outlined in the Market Rules, a refresh / replacement of the operations voice recording system, expand the capacity of the operational inbound call management system, allowing the handling and prioritization of a larger volume of inbound calls specifically in emergency situations.	0.5	0.4		

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
UNIX Server Infrastructure Refresh & QA Environnent	Replace aging UNIX server infrastructure on an on-going basis. The work will be sequenced according to system criticality, the availability of vendor support and spare parts and maintenance costs. Benefits include: Reduced support calls due to hardware failures; Increased reliability with newer more stable systems; Reducing licensing costs; and S÷÷erver consolidation.	0.3	2.4	2.5	1.0
Remote Terminal Unit/Frame Relay and Router expansion	Provide additional Frame Relay Access Devices (FRADs) and ASEs to enable more incoming operational data via the Remote terminal Units (RTUs) from Market Participant locations; and provide additional routers to provide the DWS and MIM services to Market Participants.	0.3	0.4	0.4	
Printer Consolidation	Replace end-of-life printing, copying, faxing and scanner equipment, and reduce the number and variety of printers, copiers, faxes and scanners leased or owned by the IESO and their associated costs.	0.3	0.2		
Network DMZ Redundancy Improvements	Replace problematic low cost hubs with established vendor switches to improve both the future availability and reliability of the network gateway for all Internet based access to and from the IESO. In addition, resolve the emerging cross-site congestion situation due by maximizing use of existing bandwidth.	0.2			
Real-time Telemetry Upgrade	Upgrade and expand the infrastructure necessary for receiving telemetry data to meet ongoing customer needs.	0.2			
System Voice Circuit Replacement	Implement a telephony solution to address voice communications capabilities that were lost when IESO discontinued its use of voice circuits owned by Hydro One for confidentiality reasons.	0.2			
Interconnection Metering	This project will deliver an upgrade of, or result in the purchase of metering on certain intertie connections with another ISO jurisdiction. This is required to satisfy operational obligations.		0.2		
Storage Infrastructure Enhancements	Purchase and install an integrated Storage Area Network (SAN) and Network Attached Storage (NAS) solution for the IESO to address capacity and reliability concerns.	0.7			
Network Infrastructure Replacement (load balancers)	Replace the network load balancers which are no longer supported by the vendor and are creating an increasing risk to the backbone network. Replacement system will improve capacity, functionality and attract improved vendor support.	0.1			
Audio Visual Upgrades	Replace outdated and unreliable TV's, VCR's, and other audio/visual equipment at various IESO locations and conference rooms within the IESO, and introduce some video conferencing capability.	0.1			

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Remote Access Project (aka VPN Replacement)	Improve the security of remote access for vendors and staff and establish the security architecture required to permit larger volumes of remote access traffic. As well as the improvement to security, this will also provide additional options for the IESO to respond to contingencies that would make on-site operation difficult or impossible.	0.1	0.4		
Desktop Hardware Refreshment	Provision for the refresh of desktop PC's used by IESO staff, based on standard lifecycle planning.		0.5	0.5	0.5
Increased Disk Storage	An ongoing program to address planned increases in storage capacity requirements.		0.3	0.2	0.2
System Data Repository Constellation	Reconfigure the market activity data warehouse (constellation style) database design, enabling improvements in handling the large and increasing data volumes, which are utilized in supporting market analysis and satisfying reporting obligations. Current demands on the System Data Repository requires modifications and upgrades to handle increasing data volumes, and facilitate faster and more effective data retrieval and analysis in support of surveillance and compliance activities.				0.7
Plant Information Modernization	Improve the performance and reliability of the real time data historian to ensure availability of real time historical Plant Information (PI) displays used by the control room operators.			0.2	
Windows Refresh Program Stage 4	Migrate of those Business Application next deemed critical from a reliability, capacity or performance perspective to the new Windows Server 2003 infrastructure. [See Windows Refresh Program Stage 2&3]			2.7	
Windows Refresh Program Stage 5	Complete overall WSIR project to replace IESO aging Windows server infrastructure (Hardware & Software), by migrating the remaining Business Applications to the new core MS Windows Server 2003 infrastructure. [see Windows Refresh Program Stage 4]				1.5
CISCO Network Gear Equipment Buyout	Exercise option to buy out the equipment at the end of the lease. This will produce significant operating cost savings in equipment that serves as the technical infrastructure facilitating the connection between corporate business applications.		0.3		
Network Equipment Replacement	Replace the existing Network equipment that has a technological life cycle end of life in 2008.				1.5
Other Minor Projects and Contingency		0.3	0.2	0.4	0.4
TOTAL IT-INFRASTRUCTURE		**6.0**	**7.1**	**6.9**	**5.8**

Facilities Improvements

($ millions)					
Project Name	Description	2005 Proj.	2006 Budget	2007 Plan	2008 Plan
Physical Security Upgrades	Deliver physical security upgrades to IESO facilities consistent with currently assessed threat levels.	0.5			
Control Center HVAC Upgrades (2005 - Chiller 3 Conversion)	Install necessary Heating, Ventilating, Air conditioning upgrades to the IESO operations control centre.	0.1	0.2	0.1	
Back-up Operating Centre Relocation and configuration	Re-locate the IESO's backup control centre to a more secure location, to address the current and assessed future security context.		1.2	1.3	
UPS Battery Replacement	Replace the Uninterruptible Power Supply (UPS) batteries at the IESO control centre.				0.6
Other Minor Projects and Contingency	Miscellaneous Facilities Improvements	0.1	0.1		
TOTAL FACILITIES IMPROVEMENTS		**0.7**	**1.5**	**1.4**	**0.6**

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