Ontario

MINISTRY OF ENERGY

IESO BUSINESS PLAN
2017 – 2019

October 2016

Regulatory Affairs and Strategic Policy

Background

- The IESO Business Plan 2017-19 (the Plan) was submitted on September 2, 2016 for Minister's approval as required by legislation.
- The process for IESO business plans and fees is set out in the *Electricity Act, 1998*:
  - The Minister may approve the proposed business plan or refer the Plan back to IESO for further consideration.
  - The IESO is to make an annual application of proposed expenditure, revenue requirements and fees it proposes to charge for the next fiscal year before November 1 with the OEB, but it cannot do so until after the Minister approves the IESO proposed business plan.
  - There are no references to any penalties if the IESO does not make its application with the OEB by November 1 each year.
- The last IESO business plan 2016-18 was approved by the Minister in November 2015. The proposed usage fee for 2016 is currently pending a final decision by the OEB.
- The renewal of the PWU collective agreement expiring March 31, 2017 is expected to take place in late 2016 to early 2017, subject to any applicable new mandates or guidelines from the Province.
  - The Ministry/TBS will need to consider the recent announcement of government no longer negotiating net-zero when communicating mandate/guidelines with agencies.

Highlights of the Plan

Overview

- The Plan reflects the near term activities to fulfil the IESO ’s broad mandate and supports its 4 strategic goals: (1) superior reliability (2) more efficient and sustainable marketplace (3) a trusted advisor, informed by engagement (4) invest in people and processes.

The 2017 Budget

- Total expenses for core operation is $183.3M, an increase of $1.2M (or 0.6%) from 2016 budget.
  - Cost impact from collective agreement is aligned with net zero result in 2017.
  - Pensions and other post-employment benefits are higher as a result of lower discount rate which increases future liabilities and funding requirement. This is partially offset by savings from changes in management group pension.
  - The increase also includes computer services contracts and amortization of system-related expenditures.

Merger Synergy Savings

- Anticipated merger synergy savings of $5.32 was achieved in 2015 and continue to be sustained. The Plan forecasted 2016 synergy savings at $5.99M and 2017 budget at $6.28M.
- The incremental cost from collective agreements with IESO’s unions have been addressed primarily by FTE reductions, vacancy management, hiring lags and reduced consulting support to reach a neutral cost impact.

Proposed Next Steps

1. **Clearance from Internal Audit:**

- Ministry proposes to meet with IA to ensure all recommendations made by OIAD in the 2016-18 business plan have been fully addressed.

2. **Recommendation to Approve the Proposed Plan:**

- Staff review finds the 2017 budget reasonable.
  - The Plan reflects sustaining merger synergy savings, a marginal increase in operating expenses by $1.2M (~ 0.6%) and a reduction of 1 FTE to deliver on its mandate while managing multiple changes in the sector.
  - Its operating costs will result in no change in the usage fee to ratepayers from 2016, ie 9% reduction from pre-merger level.
  - All recommendations from the Internal Audit review of the 2016-18 business plan, including progress towards synergy savings and net zero costing from collective agreements have been fully addressed.
- The Plan reflects the fulfillment of its mandate. It is also is in line with government policy initiatives, including the IESO's lead role in the implementation of conservation first policies and LTEP implementation.
- IESO is supposed to bring forward its usage fee application for the next year to the OEB by November 1 st; however Business Plan approval is required. Minister's approval prior to November will facilitate maximum compliance and timely fee-setting for the next fiscal year.

3. **Minister Response Letter:**

- Ministry is to prepare a letter constituting the Minister's approval of the Plan.
- The letter includes instructions to ensure synergy savings for 2016 and 2017 will be sustained, and additional advice for IESO to be responsive to the developing initiatives in LTEP, CCAP and continued technology change.

Overview of 2017-19 Budget

IESO Core Operations ($millions)	2014 Actual	2015 Approved Budget	2015 Actual	2016 Approved Budget	2017 Proposed Budget	2018 Plan	2019 Plan
Compensation & Benefits	115.2	108.9	105.0	110.3	111.8	114.7	117.0
Professional & Consulting	19.1	22.1	22.2	20.1	18.8	18.7	18.7
Operating & Administration	34.4	33.5	34.9	33.5	35.7	35.9	35.9
Amortization	16.6	18.7	17.9	17.5	17.3	18.2	18.6
Interest	0.8	1.4	1.6	0.7	(0.3)	(0.3)	(0.3)
Total Core Expenses	**186.1**	**184.6**	**184.9**	**182.1**	**183.3**	**187.2**	**189.9**

- 2017 Proposed Budget is $1.2M or 0.6% above the 2016 approved budget
  - Higher compensation and benefits expenses are attributed to higher pension and other post-employment benefits. This is due to lower discount rates which increases future liabilities and funding requirement. The increase is partially offset by savings from change in management pension contributions and benefits. The 2017 budget includes a reduction of 1 FTE.
  - Higher operating ad administration expenses reflect increases in computer services contracts from planned activities such as the market information system, operations readiness initiatives and cyber security.
- The 2017 proposed budget does not yet consider the potential impacts of developing initiatives such as climate change and market renewal.
- Compensation & Benefits line item includes costs associated with recent pension accounting changes.

Focus and Deliverables in 2017-19

Business Functions	Key Activities
Operations	• To maintain and improve the operability of the power system in 3 areas: regulation, voltage control and flexibility. • Implement the Situational Awareness Initiative, operations Readiness Initiative.
Planning	• Develop an implementation plan for the next LTEP in 2017. • Develop an integrated regional resource plan by working with LDCs, municipal representatives, stakeholders, First Nations, Metis and others.
Market and Resource Development	• Leading analysis in support of the development of the market renewal program • Ongoing management of more than 26,000 contracts that account for 26,000 MW of generation
Conservation	• Oversee the implementation of Conservation First Framework to achieving 7 TWh of energy savings by the end of 2020. • Administer innovation and conservation Funding programs
Information Technology	• Ensures 24x7 to maintain the reliable operation of the IESO-grid and IESO administered market. • Promote cyber security best practices
Market Assessment and Compliance	• Monitor compliance with market rules
Enabling Services	• Achieve greater efficiency and cost-effectiveness among in its corporate services, including communications and stakeholder relations, settlements, finance, human resources, First Nations and Metis relations, legal and regulatory affairs.

Strategic Plan and Corporate Performance Measures

- Critical milestones to inform on the development of the business plan are the 5-year Strategic Plan and Corporate Performance Measure (CPM) plan to focus on priorities, define success driver and measures. IESO has consulted with the IESO Stakeholder Advisory Committee representing voices of the sector.

Strategic Plan 2016-20				
Themes	Providing Public Value		Respecting and valuing our communities, customers and stakeholders	Building corporate resilience
Goals	Deliver superior reliability performance in a changing environment	Drive to a more efficient and sustainable market place	Be recognised as a trusted advisor, informed by engagement	Invest in our people and processes to meet the needs of the sector

- **The 2017 CPMs** were developed to be results and outcome-oriented, externally focused, measurable, specific and achievable. A high level summary of the CPMs which gauge on key focus areas is as follows:
    1. Overall progress towards achievement of the 2016-20 Strategic Plan
    2. Reliability of Ontario's power system
    3. Implementation of key recommendations in regional and bulk system power plans
    4. One major LDC is actively engaged in 2-way communication by end of 2017
    5. Cyber security excellence
    6. The IESO continues to focus on price-efficient outcomes
    7. Broader, competitive and more innovative sector participation is enabled by end 2017
    8. Use the 2016 customer satisfaction survey results, improve stakeholder and community satisfaction with the engagement process
    9. Employee engagement increases by 2% from 2016
    10. Expanded operational capacity

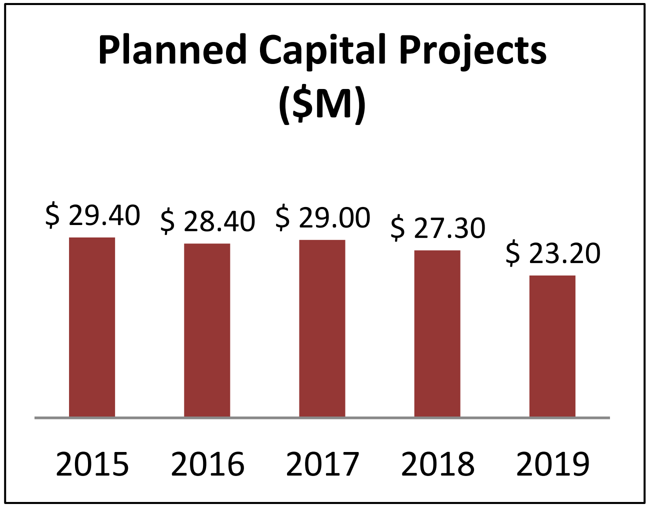
OIAD Recommendations on 2016-18 Business Plan

IESO addressed the OIAD recommendations in a revised business plan 2016-18 in November 2016, subsequently approved by the Minister. Further updates on the issues and actions taken are provided in the 2017-19 business plan.

	Issue	OIAD Recommendations	Actions Taken/ Committed
1	Progress in synergy savings Target: $5.32M	• Ensure planned/estimated synergy savings materialise in 2015 • Alternatively, an additional $0.14M savings need to be identified to meet 2015 budget	• IESO achieved synergy savings of $5.52M in 2015, exceeded the target level.
2	Sustainability of synergy savings target	• Use reasonable and consistent assumptions, support calculations with documentation and analysis • Report periodically or as required by the Ministry	• The 2016 forecast and proposed 2017 budgets are below the synergy target budget level of $184.9M to uphold the synergy savings. • IESO reported on cost review progress with the Ministry regularly during 2016
3	Offsets for the Society award	• Identify savings that align with Minister's direction (changes to management pension plan is not considered a legitimate offset)	• IESO achieved net zero in 2015. In 2016 -17, IESO is on track to meet full cost offsets through vacancy management, hiring lags, reduced consulting support, savings related to OEB fees and offsetting interest income.
4	Offsets for PWU settlement	• Identify savings that align with Minister's direction (changes to employee pension contribution is not considered a legitimate offset)	• Incremental cost of the 3-year agreement will be offset by cost savings of 1 FTE reduction and vacancy management.

APPENDIX A
IESO BUSINESS PLAN FINANCIALS & STAFFING

Summary of Capital Spending



- Consistent with prior years, the IESO establishes approval of an appropriate capital envelope for the 2016-19 planning period, with capital commitments approved individually on an ongoing basis.
- The 2017 budget has increased by 2.1% in capital spending compared to 2016 budget due to planned initiatives supporting cyber security, market information and operations readiness.

Change Initiatives/Projects ($ Millions)	2017 Plan	2018 Plan	2019 Plan
Identity Access Management	2.1		
Operations Readiness Initiatives	2.5	3.0	
Market Information System (MIS) Refresh	2.0	1.7	
Infrastructure Refresh (building services, software licenses & computer hardware)	2.5	2.5	2.3
Enterprise Cyber Security Management Refresh	2.0		
Conservation Demand Management Information System (CDM IS)	1.0	0.4	1.0
Corporate Website including consolidation and enhancement to Save on Energy	1.5	1.0	1.5
CRS Replacement & Migration	1.0	2.0	2.0
Financial Systems Upgrade	1.0	1.5	1.0
MACD Enforcement Support Tool and related projects	1.0	0.5	1.0
FIT, microFIT and other upgrades	1.0	0.7	0.4
Oracle Archetype Expansion and Oracle batch	1.0	1.0	
Wallboard Refresh	1.0		
System Logging and Analysis Upgrade (Qradar)		2.0	
Tier 1 Storage Refresh			2.0
ETP Refresh			1.0
Total Capital Change Initatives/Projects ($1M & above)	**19.6**	**16.3**	**12.2**
Other Capital Change Initatives/Projects	**9.4**	**11.0**	**11.0**
Total Capital Change Initatives/Projects	**29.0**	**27.3**	**23.2**

Progress Towards Synergy Savings

Anticipated synergy savings for the merger is $5.32M. IESO has achieved and exceeded the savings level in 2015, and is projecting to meet and further the savings in 2016 and 2017.

Description of Synergy Savings , $M	**Merger Working Group Estimate**	**2015 Projection per Internal Audit**	**2015 Actual**	**2016 Forecast**	**2017 Budget**
Headcount Reduction	6.68	6.66	6.46	6.46	6.46
Consulting	0.30	1.32	1.76	1.76	1.76
Office space	1.32	0.52	0.62	1.15	1.15
Media service	0.60	0.00	0.00	0.00	0.00
HR services	0.10	0.10	0.10	0.10	0.10
Finance synergies	0.05	0.04	0.09	0.09	0.09
50/50 pension benefit future employees	0.31	0.04	0.10	0.10	0.10
Total Synergy Savings	**8.82**	**8.68**	**9.13**	**9.66**	**9.66**
Less: Additional costs					
Job mapping and post retirement benefits	(3.20)	(3.20)	(3.41)	(3.41)	(3.11)
All other	(0.30)	(0.30)	(0.20)	(0.26)	(0.26)
Total Net synergy savings	**5.32**	**5.18**	**5.52**	**5.99**	**6.28**

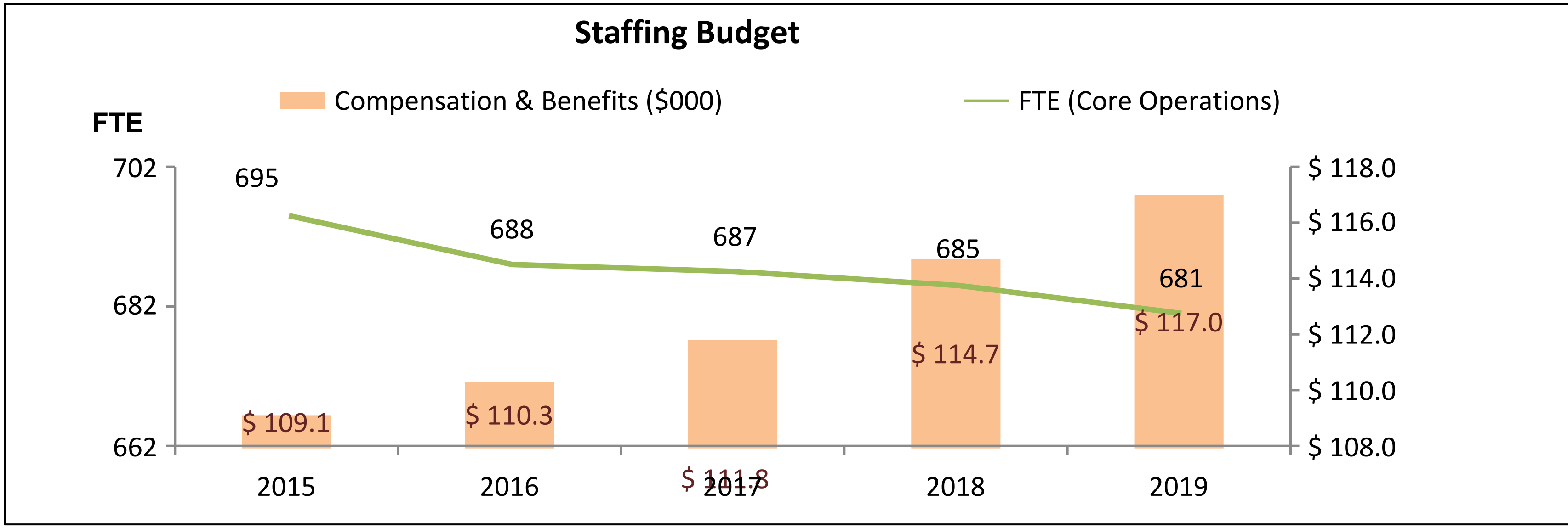
Cost review adj	0.34
	5.52

Trend in Staffing Levels

	Synergy target		OIAD Audit	Proposed 2017-19 Plan		
FTE #	**2014 OPA/IESO**	**2015 New IESO**	**2016**	**2017**	**2018**	**2019**
Year over year change		(35)	(7)	(1)	(2)	(4)
Total FTEs (Core Operations)	730	695	688	687	685	681

Trend in IESO staffing reductions:
- 2015 - 35 FTEs as per synergy target
- 2016 – additional 7 FTEs (6 from Society and 1 from PWU) as offsets to salary increments from collective agreements
- 2017-19 - Further FTE declines are a result of business enhancement efficiencies initiated after the merger.

Staffing and Compensation Budget



- IESO reported that it maintained 2015 an 2016 headcount below the budgeted level. As of Aug 2016, IESO reported actual FTE count was 665, 23 under the 2016 budget.
- 2017 and 2018 staffing budget s are established based on the 2016 budgeted FTE of 688. 2017 staffing budget will decrease by 1 from 2016 to 687 FTEs. Further FTE declines are planned for 2018 and 2019 as a result of business enhancement efficiencies initiated in 2016.
- 2017 compensation budget will increase by 1.4% due to higher pension and other post-employment benefits. The impact of the IESO's collective agreements with its unions is aligned with net neutral costing result in 2017.

Collective Agreements – Neutral Cost Impact

- In February 2015, the Minister mandated the IESO to achieve a “net-zero” increase respecting collective bargaining with its unions, and with offsets in other compensation if there are increases resulting from collective agreements. Collective agreements with Society (2015-2018) and PWU (ending March 2017) do not land to “net zero” but IESO has identified other savings to achieve a neutral cost impact

Society

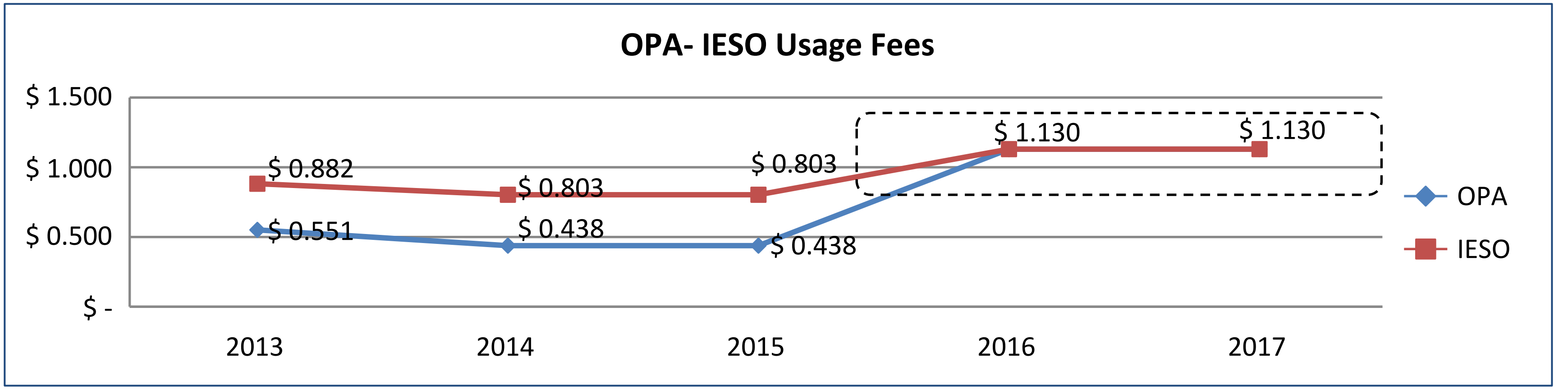
$(M)	2015	2016	2017
Incremental salary cost	1.0	2.8	3.8
Less Offsets:			
Vacancy management	(2.1)		
Hiring Lags		(1.6)	(0.8)
Consulting support		(1.3)	(1.3)
OEB fees savings		(0.7)	(0.7)
Interest income			(1.0)
Savings Balance	**(1.1)**	**(0.9)**	**0.0**

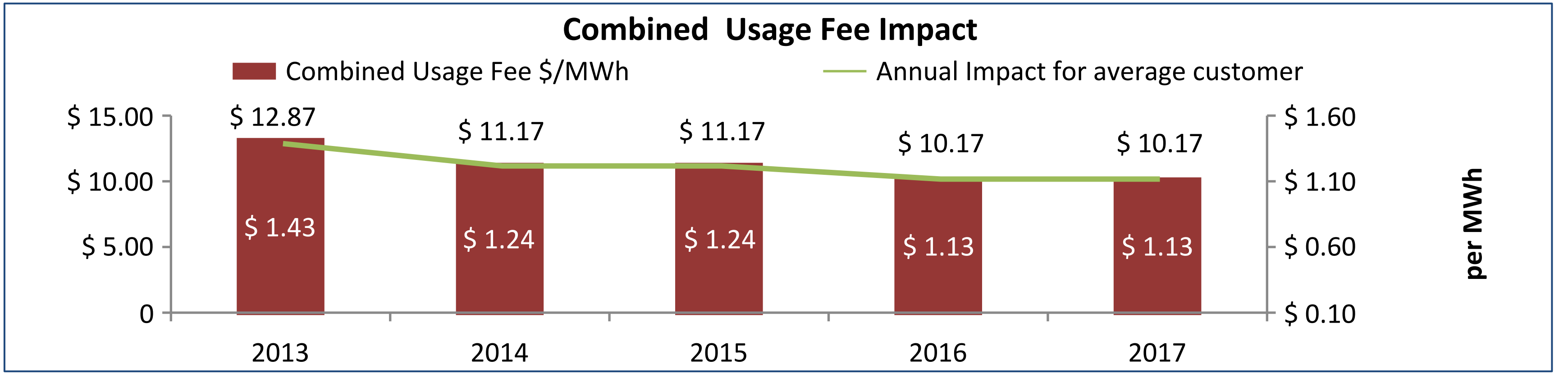
PWU

($000s)	2014-15	2015-16	2016-17	Total 3 years
Incremental salary cost	83.6	197.4	314.1	595.1
Less Offsets:				
Termination of 1 FTE	(203.2)			(203.2)
10% reduction in college co-ops	0	(45.0)	(49.0)	(94.0)
Vacancy management	(116.3)	(116.3)	(65.4)	(298.0)
Savings Balance	**(235.9)**	**36.1**	**199.7**	**0.0**

APPENDIX B
BACKGROUND ON IESO FEES AND CHARGES

Trend of Usage Fee





- The IESO is proposing a usage fee charged to all customers at $1.13/MWh for 2017, the same reduced level that has been submitted for approval for 2016. This represents a reduction by 9% from the 2015 and pre-merger levels.
- The reduction represents an annual savings of $1.00 ($11.17-$10.17) on an average residential customer's bill.

2016 IESO Fees

- The IESO filed an application with the OEB on January 20, 2016 under section 25(1) of the *Electricity Act, 1998,* seeking approval for the IESO 2016 expenditures, revenue requirement and fees. The application is based on the IESO 2016-18 business plan, approved by the Minister in November 2015.
- The 2016 fee application is currently under review by the OEB. A settlement conference was held on August 18. An OEB decision is tracking for Nov - Dec 2016.
- The parties have reached substantial settlement of issues in relation to IESO's 2016 fee. It reflects agreement on the appropriateness of proposed costs, revenue requirements, merger cost and retaining $10M as operating reserve.
- There are remaining unsettled issues around the IESO's proposal of charging a single combined fee. Former IESO fees determinant are based on gross load while the past OPA fee is based solely on energy withdrawals exclusive of embedded generation and exports.
- The OEB has ordered a written hearing to receive written submissions from IESO and intervenors on the unsettled issue in October.
- While the OEB decision on the 2016 fee will have an impact on whether a single fee will be charged, it would not have an impact on the 2017-19 business plan and the budget envelope to be approved by the Minister.

Methodology for Calculating Usage Fee

Usage fee

The IESO revenue source is mainly from system fees collected by the IESO based on OEB-approved rates. There are 3 basic steps involved in calculating usage fee:

1. Project revenue required by the IESO to operate its business (based on the Minister-approved business plan)
2. Estimate the charge determinant (energy withdrawn from the grid + exports+ embedded generation)
3. Usage fee ($/MWh) = revenue requirements (1) / estimated market demand volume (2)

Usage fee determinant

- In 2014, the OEB approved the IESO's methodology to add embedded generation to its combination of energy volume for market demand to ensure payments the LDCs on their total loads are accounted for. Previously, the energy volumes used for fee determinant do not include embedded generation.
- The past OPA fee is based solely on energy withdrawals exclusive of embedded generation and exports.
- For 2016 and future years, the IESO is proposing to charge one fee on the same basis that the IESO fee is currently charged. OEB decision is pending.

Rebate of revenue surplus

- IESO does not operate for profit. Annual revenue surplus is kept in an deferral account approved by OEB.
- The IESO is requesting approval to retain $10M of the accumulated surplus, and the balance in excess of $10M each year will be to return to market participants. The approval of the deferral account for operating surplus and the disposition of surplus balance are to be determined in its annual rate case with the OEB.

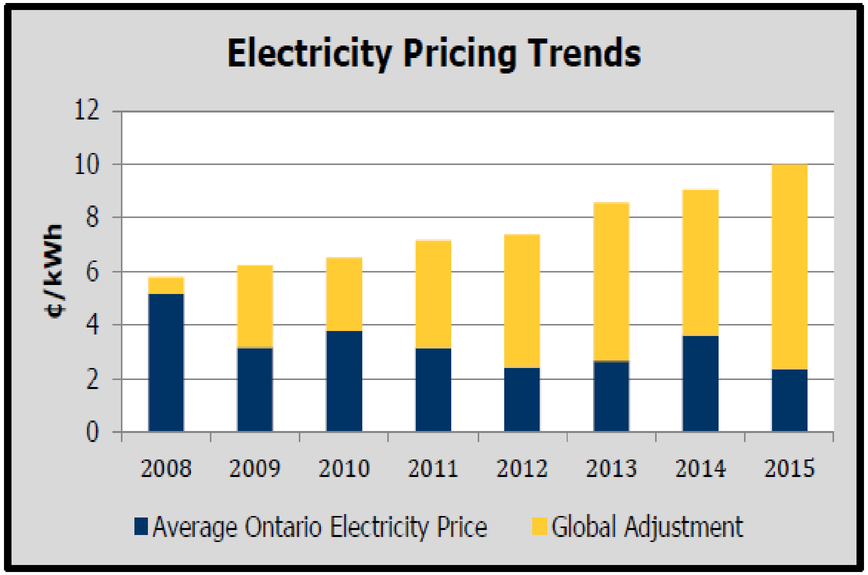
Legislative and Regulatory Process

Business Plan: The IESO has a legislative requirement under the *Electricity Act, 1998* (EA) to submit its annual business plan to the Minister for approval by around September 1 every year. Minister reviews and approves the business plan, including total expense budget of the IESO. The approved budget will form the basis for the IESO's revenue requirements, expenditures and fees it proposes to charge for the next fiscal year, and is subject to the approval of the OEB through a public review process.

Usage Fee: The usage fee review is the mechanism that allows IESO to recover its revenue requirements and expenditures from market participants, which are ultimately passed to electricity ratepayers. EA requires the IESO to submit its fee application to the OEB by November 1, but cannot do so without the Minister's approved business plan. In 2015, the IESO continues to charge the 2014 fees that were approved by the OEB for the predecessor IESO and OPA, respectively, until the OEB approves a new fee. The OEB's role in a fee review is to assess whether the proposed organizational budget is reasonable and is in the public interest.

Smart Metering Entity (SME): The IESO was designated the SME by Ontario regulation 393/07 responsible for project management of the development, delivery and operation of the Data Management Repository. The costs of SME are funded separately from IESO wholesale operations. In March 2013, the OEB approved an SME fee of $0.79 per month for residential and General Service <50KW customers from 2013-2018.

Global Adjustment and Electricity Pricing



Charges (Global Adjustment-GA): GA covers for providing both adequate generating capacity and conservation programs for Ontario. The IESO is responsible for recovering the price differences between market price of electricity (HOEP) and the price it pays to regulated or contracted generators through global adjustment. Global adjustment can be either a credit or charge depending on the changing market price.

However, it has generally been a charge. These charges are required to fund the activities for generation contracts, conservation and demand management programs to ensure both adequate energy supply and green energy for Ontario. Under the provisions of the *EA*, IESO fees and charges are brought to the OEB for review in the same proceeding but the IESO's recovery of these charges is deemed to be approved by the OEB and pass through to electricity ratepayers.