KPMG

Independent Electricity System Operator

Audit Planning Report

For the year ended December 31, 2016

September 12, 2016

kpmg.ca/audit

The contacts at KPMG in connection with this report are:

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At KPMG, we are **passionate** about earning your **trust**. We take deep **personal accountability**, individually and as a team, to deliver **exceptional service and value** in all our dealings with you.

At the end of the day, we measure our success from the only **perspective that matters – yours**.

Executive summary

Audit and business risk

Our audit is risk-focused. In planning our audit we have taken into account key areas of focus for financial reporting. These include:

- Revenue recognition and market participant rebate accrual,
- Post-employment benefits,
- Asset capitalization policies

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KPMG team

The KPMG team will be led by Matthew Betik. Subject matter experts will be involved to ensure our approach is appropriate and robust.

Effective communication

We are committed to transparent and thorough reporting of issues to the CFO, CEO, senior management and the Audit Committee.

Audit Materiality

Materiality has been determined based on total net revenue. We have reviewed the scope of work across segments and within the entity. We have determined materiality to be $3,500,000 for the year ending December 31, 2016. This is based on estimated Corporate revenues of $190 million and Smart Metering Entity revenues of $45 million.

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Independence

We are independent and have extensive quality control and conflict checking processes in place. We provide complete transparency on all services and follow Audit Committee approved protocols.

Current developments

There are no new relevant accounting or auditing changes to be brought to your attention at this time.

Audit approach

Professional standards presume the risk of fraudulent revenue recognition and the risk of management override of controls exist in all companies.

The risk of fraudulent recognition can be rebutted, but the risk of management override of control cannot, since management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Professional requirements	Why	Our audit approach
Fraud risk from revenue recognition	This is a presumed fraud risk.	However, the audit team has rebutted this presumption due to the following reasons: — The presumed fraud risk is ordinarily associated with profit oriented enterprises; — The majority of revenue is calculated based on market accounts data and is not subject to complexity or judgement at the corporate level; and — KPMG does not believe that the use of inappropriate cut-off or “channel” stuffing would be utilized to perpetrate fraud.
Fraud risk from management override of controls	This is a presumed fraud risk. We have not identified any specific additional risks of management override relating to this audit.	As the risk is not rebuttable, our audit methodology incorporates the required procedures in professional standards to address this risk. These procedures include — testing of journal entries and other adjustments; — performing a retrospective review of estimates; and — evaluating the business rationale of significant unusual transactions.

Audit approach

Other areas of focus include the following:

Other areas of focus	Why	Our audit approach
Pensions and other post employment benefits	• Significance of the account balance • Estimates and judgements used by management • Complexity of accounting guidance • Regulatory scrutiny	• Communicate with management's actuarial specialists • Confirm fair values of investments • Assess the reasonableness of the process to determine market related values for expected return on plan assets • Assess the reasonableness of assumptions used • Test the appropriatenesss of the underlying data, including employee populations We will also use the work of AON Hewitt in our audit of the accounts and disclosures. We will rely on AON Hewitt for the calculation of actuarially determined values, as permitted by Canadian Audit Standards.
Revenue Recognition and Market Participant Rebates	• Judgements used in determining the amount of the regulatory deferral account • Stakeholder impact of the rebate and its impact on the rate setting process	• Test the amounts received from market accounts • Test controls around the recording of revenues • Perform independent analysis of system fees based on usage trends • Assess existence of system fees through the examination of market participant Notices of Disagreement • Assess the reasonableness of the year-end market participant rebate accrual based on rate submission and other relevant evidence We will use the service organization auditors' report and use the findings of the CSAE 3416 report on controls in the market accounts system.
Asset capitalization policies	• Significance of account balance • Stakeholder impact of the rebate and its impact on the rate setting process	• Discuss capitalization policies and their application with management • Test a sample of capital additions to ensure existence and accuracy • Test items recorded as repairs & maintenance or other similar accounts to ensure completeness of capital additions

Materiality

Professional standards require us to re-assess materiality at the completion of our audit based on period-end results or new information in order to confirm whether the amount determined for planning purposes remains appropriate.

Our assessment of misstatements, if any, in amounts or disclosures at the completion of our audit will include the consideration of both quantitative and qualitative factors.

The first step is the determination of the amounts used for planning purposes as follows.

The determination of materiality requires professional judgment and is based on a combination of quantitative and qualitative assessments including the nature of account balances and financial statement disclosures.

Materiality determination	Comments	Amount
Metrics	Total revenue	
Benchmark	Based on an estimate of total revenue for the year. This benchmark is consistent with the prior year.	$235 million
Materiality	Determined to plan and perform the audit and to evaluate the effects of identified misstatements on the audit and of any uncorrected misstatements on the financial statements. The corresponding amount for the prior year's audit was $3.5 million	$3.5 million
% of Benchmark	The corresponding percentage for the prior year's audit was 1.5%	1.5%
Performance materiality	Used 75% of materiality, and used primarily to determine the nature, timing and extent of audit procedures. The corresponding amount for the prior year's audit was 75%	$2.6 million
Audit Misstatement Posting Threshold (AMPT)	Threshold used to accumulate misstatements identified during the audit. The corresponding amount for the previous year's audit was $175 thousand	$175 thousand $500 thousand for reclassification adjustments not impacting the market participant rebate calculation

Value for fees

In determining the fees for our services, we have considered the nature, extent and timing of our planned audit procedures as described above. Our fee analysis has been reviewed with and agreed upon by management.

Our fees are estimated as follows:

	Current period (budget)	Prior period (actual)
Audit of the annual financial statements	$66,500	$65,000
French translation services for financial statements	$7,000	$7,000
Compilation of Corporate Tax Returns	$1,400	$1,400
Audit of Pension Plan financial statements	$16,500	$16,000

Matters that could impact our fee

The proposed fees outlined above are based on the assumptions described in the engagement letter. The critical assumptions, and factors that cause a change in our fees, include:

- Significant changes in the nature or size of the operations of the Company beyond those contemplated in our planning processes;
- Changes in professional standards or requirements arising as a result of changes in professional standards or the interpretation thereof;
- Changes in the time of our work;

Audit cycle and timetable

Our key activities during the year are designed to achieve our one principal objective:

To provide a robust audit, efficiently delivered by a high quality team focused on key issues.

Our timeline is in line with prior year.

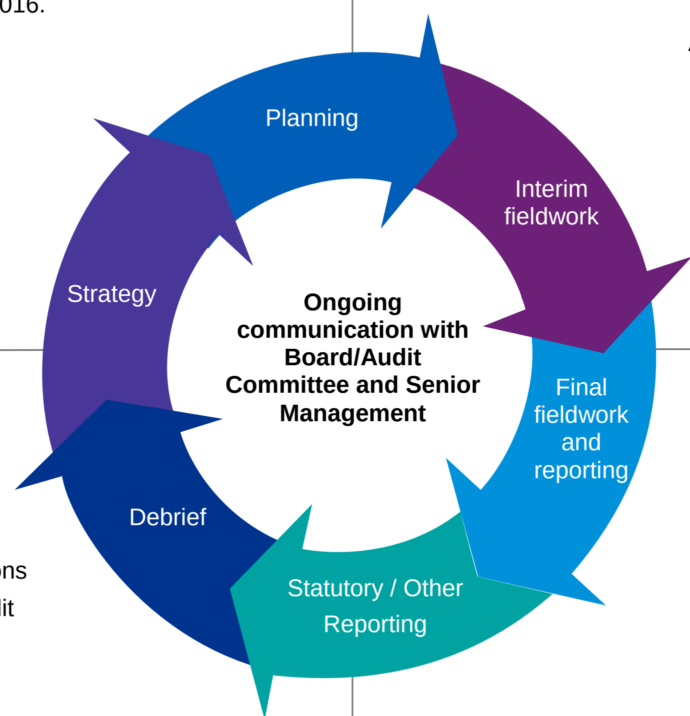
Planning meeting with management August 2016.

October/November

Audit plan discussion October 25

Interim fieldwork – December 5

September



Final fieldwork: Weeks of January 23 and 30

Closing meetings: early February

Audit findings discussion: February 28, 2017

Issuance of audit report on financial statements: March 1, 2017

Audit strategy discussions based on debrief of audit April/May

March

Appendices

Appendix 1: Audit quality and risk management

KPMG maintains a system of quality control designed to reflect our drive and determination to deliver independent, unbiased advice and opinions, and also meet the requirements of Canadian professional standards.

Quality control is fundamental to our business and is the responsibility of every partner and employee. The following diagram summarises the six key elements of our quality control systems.

Visit our [Audit Quality Resources] page for more information including access to our audit quality report, [Audit quality: Our hands-on process.]

- Other controls include:
  - Before the firm issues its audit report, Engagement Quality Control Reviewer reviews the appropriateness of key elements of publicly listed client audits.
  - Technical department and specialist resources provide real-time support to audit teams in the field.
- We conduct regular reviews of engagements and partners. Review teams are independent and the work of every audit partner is reviewed at least once every three years.
- We have policies and guidance to ensure that work performed by engagement personnel meets applicable professional standards, regulatory requirements and the firm's standards of quality.

- All KPMG partners and staff are required to act with integrity and objectivity and comply with applicable laws, regulations and professional standards at all times.
- We do not offer services that would impair our independence.
- The processes we employ to help retain and develop people include:
  - Assignment based on skills and experience;
  - Rotation of partners;
  - Performance evaluation;
  - Development and training; and
  - Appropriate supervision and coaching.
- We have policies and procedures for deciding whether to accept or continue a client relationship or to perform a specific engagement for that client.
- Existing audit relationships are reviewed annually and evaluated to identify instances where we should discontinue our professional association with the client.

Appendix 2: KPMG's audit approach and methodology

Technology-enabled audit workflow (eAudIT)

Engagement Setup

- Tailor the eAudIT workflow to your circumstances
- Access global knowledge specific to your industry
- Team selection and timetable

Completion

- Tailor the eAudIT workflow to your circumstances
- Update risk assessment
- Perform completion procedures and overall evaluation of results and financial statements
- Form and issue audit opinion on financial statements
- Obtain written representation from management
- Required Audit Committee communications
- Debrief audit process

Risk Assessment

- Tailor the eAudIT workflow to your circumstances
- Understand your business and financial processes
- Identify significant risks
- Plan the use of KPMG specialists and others including auditor's external experts, management experts, internal auditors, service organizations auditors and component auditors
- Determine audit approach
- Evaluate design and implementation of internal controls (as required or considered necessary)

Testing

- Tailor the eAudIT workflow to your circumstances
- Perform tests of operating effectiveness of internal controls (as required or considered necessary)
- Perform substantive tests

Appendix 3: Required communications

In accordance with professional standards, there are a number of communications that are required during the course of our audit. These include:

- **Engagement letter** – the objectives of the audit, our responsibilities in carrying out our audit, as well as management's responsibilities, are set out in the engagement letter and any subsequent amendment letters
- A**udit planning report** – as attached
- **Required inquiries** – professional standards require that during the planning of our audit we obtain your views on risk of fraud and other matters. We make similar inquiries to management as part of our planning process; responses to these will assist us in planning our overall audit strategy and audit approach accordingly
- **Management representation letter** – we will obtain from management certain representations at the completion of the annual audit. In accordance with professional standards, copies of the representation letter will be provided to the Audit Committee
- **Audit findings report** – at the completion of our audit, we will provide a report to the Audit Committee
- **Annual independence letter** – at the completion of our audit, we will provide a letter to the Audit Committee
- **CPAB Big Four Firm Public Report (November 2015)** – Please refer to http://www.cpab-ccrc.ca/Documents/Annual%20Reports/CPAB_2015_Big%20Four_Report_EN_Final.pdf

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