

***Independent Electricity System Operator  
Statements of Financial Position***

| As at (in thousands of Canadian dollars)                                   | December 31, 2016 | December 31, 2015<br>(restated Note 3) |
|----------------------------------------------------------------------------|-------------------|----------------------------------------|
|                                                                            | \$                | \$                                     |
| <b>FINANCIAL ASSETS</b>                                                    |                   |                                        |
| Cash and cash equivalents                                                  | 33,005            | 14,715                                 |
| Accounts receivable                                                        | 31,103            | 33,199                                 |
| Regulated assets (Note 3)                                                  | 65,064            | 88,202                                 |
| Long-term investments (Note 4)                                             | 40,355            | 37,318                                 |
| Market accounts - assets (Note 3)                                          | 1,636,201         | 1,443,121                              |
| <b>TOTAL FINANCIAL ASSETS</b>                                              | <b>1,805,728</b>  | <b>1,616,555</b>                       |
| <b>LIABILITIES</b>                                                         |                   |                                        |
| Accounts payable and accrued liabilities (Note 5)                          | 38,963            | 48,868                                 |
| Accrued interest on debt                                                   | 315               | 315                                    |
| Rebates due to market participants (Note 6)                                | 12,551            | 9,595                                  |
| Debt (Note 7)                                                              | 90,000            | 90,000                                 |
| Accrued pension liability (Note 8)                                         | 34,620            | 36,062                                 |
| Accrued liability for employee future benefits other than pension (Note 8) | 90,251            | 84,501                                 |
| Market accounts - liabilities (Note 3)                                     | 1,636,201         | 1,443,121                              |
| <b>TOTAL LIABILITIES</b>                                                   | <b>1,902,901</b>  | <b>1,712,462</b>                       |
| <b>NET DEBT</b>                                                            | <b>(97,173)</b>   | <b>(95,907)</b>                        |
| <b>NON-FINANCIAL ASSETS</b>                                                |                   |                                        |
| Net tangible capital assets (Note 9)                                       | 105,047           | 103,716                                |
| Prepaid expenses                                                           | 6,614             | 6,197                                  |
| <b>TOTAL NON-FINANCIAL ASSETS</b>                                          | <b>111,661</b>    | <b>109,913</b>                         |
| <b>ACCUMULATED SURPLUS</b>                                                 |                   |                                        |
| Accumulated surplus from operations (Note 6)                               | 6,582             | 6,348                                  |
| Accumulated remeasurement gains                                            | 7,906             | 7,658                                  |
| <b>ACCUMULATED SURPLUS</b>                                                 | <b>14,488</b>     | <b>14,006</b>                          |

On behalf of the Board:

**Tim O'Neill**  
Chair  
Toronto, Canada

**Carole Workman**  
Director  
Toronto, Canada

*Independent Electricity System Operator*  
*Statement of Operations and Accumulated Surplus*

For the year ended December 31 (in thousands of Canadian dollars)

|                                                                          | 2016<br>Budget   | 2016<br>Actual   | 2015<br>Actual<br>(restated Note 3) |
|--------------------------------------------------------------------------|------------------|------------------|-------------------------------------|
| <b>IESO CORE OPERATIONS</b>                                              | <b>\$</b>        | <b>\$</b>        | <b>\$</b>                           |
| System fees                                                              | 177,219          | 185,531          | 186,187                             |
| Other revenue (Note 10)                                                  | 1,000            | 2,531            | 5,377                               |
| Interest and investment income                                           | -                | 2,157            | 1,430                               |
| <b>Core operation revenues</b>                                           | <b>178,219</b>   | <b>190,219</b>   | <b>192,994</b>                      |
| Compensation and benefits                                                | (106,361)        | (105,570)        | (104,994)                           |
| Professional and consulting                                              | (20,118)         | (16,844)         | (21,461)                            |
| Operating and administration                                             | (33,502)         | (34,336)         | (35,005)                            |
| <b>Core operating expenses</b>                                           | <b>(159,981)</b> | <b>(156,750)</b> | <b>(161,460)</b>                    |
| Amortization                                                             | (17,500)         | (19,577)         | (17,933)                            |
| Interest                                                                 | (738)            | (1,341)          | (1,610)                             |
| <b>Core expenses</b>                                                     | <b>(178,219)</b> | <b>(177,668)</b> | <b>(181,003)</b>                    |
| <b>Core operations annual surplus before rebates</b>                     | <b>-</b>         | <b>12,551</b>    | <b>11,991</b>                       |
| Rebates due to market participants                                       | -                | (12,551)         | (9,595)                             |
| <b>Core operations annual surplus</b>                                    | <b>-</b>         | <b>-</b>         | <b>2,396</b>                        |
| <b>MARKET SANCTIONS AND PAYMENT ADJUSTMENTS</b>                          |                  |                  |                                     |
| <b>Market sanctions and payment adjustments</b>                          | <b>4,341</b>     | <b>3,889</b>     | <b>6,021</b>                        |
| Compensation and benefits                                                | (2,981)          | (2,180)          | (3,094)                             |
| Professional and consulting                                              | (1,515)          | (770)            | (1,351)                             |
| Operating and administration                                             | (150)            | (705)            | (114)                               |
| <b>Customer education and market enforcement expenses</b>                | <b>(4,646)</b>   | <b>(3,655)</b>   | <b>(4,559)</b>                      |
| <b>Market sanctions and payment adjustments annual surplus/(deficit)</b> | <b>(305)</b>     | <b>234</b>       | <b>1,462</b>                        |
| <b>SMART METERING ENTITY</b>                                             |                  |                  |                                     |
| <b>Smart metering charge</b>                                             | <b>32,244</b>    | <b>27,426</b>    | <b>26,185</b>                       |
| Compensation and benefits                                                | (3,567)          | (2,661)          | (2,607)                             |
| Professional and consulting                                              | (18,763)         | (14,659)         | (14,902)                            |
| Operating and administration                                             | (2,364)          | (5,705)          | (4,200)                             |
| <b>Smart metering operating expenses</b>                                 | <b>(24,694)</b>  | <b>(23,025)</b>  | <b>(21,709)</b>                     |
| Amortization                                                             | (4,491)          | (3,861)          | (3,524)                             |
| Interest                                                                 | (3,059)          | (540)            | (952)                               |
| <b>Smart metering expenses</b>                                           | <b>(32,244)</b>  | <b>(27,426)</b>  | <b>(26,185)</b>                     |
| <b>Smart metering entity annual surplus</b>                              | <b>-</b>         | <b>-</b>         | <b>-</b>                            |
| <b>ANNUAL SURPLUS/(DEFICIT)</b>                                          | <b>(305)</b>     | <b>234</b>       | <b>3,858</b>                        |
| ACCUMULATED SURPLUS FROM OPERATIONS, BEGINNING OF PERIOD                 | 6,348            | 6,348            | 2,490                               |
| <b>ACCUMULATED SURPLUS FROM OPERATIONS, END OF PERIOD</b>                | <b>6,043</b>     | <b>6,582</b>     | <b>6,348</b>                        |

*Independent Electricity System Operator*  
*Statement of Remeasurement Gains and Losses*

For the year ended December 31 (in thousands of Canadian dollars)

|                                                             | 2016<br>Actual | 2015<br>Actual<br>(restated Note 3) |
|-------------------------------------------------------------|----------------|-------------------------------------|
|                                                             | \$             | \$                                  |
| <b>ACCUMULATED REMEASUREMENT GAINS, BEGINNING OF PERIOD</b> | <b>7,658</b>   | <b>6,362</b>                        |
| <b>UNREALIZED GAINS ATTRIBUTABLE TO:</b>                    |                |                                     |
| Foreign exchange - other                                    | 477            | 515                                 |
| Portfolio investments (Note 4)                              | 286            | 1,372                               |
| <b>AMOUNTS RECLASSIFIED TO THE STATEMENT OF OPERATIONS:</b> |                |                                     |
| Foreign exchange - other                                    | (515)          | (591)                               |
| <b>NET REMEASUREMENT GAINS FOR THE PERIOD</b>               | <b>248</b>     | <b>1,296</b>                        |
| <b>ACCUMULATED REMEASUREMENT GAINS, END OF PERIOD</b>       | <b>7,906</b>   | <b>7,658</b>                        |

*Independent Electricity System Operator*  
*Statements of Change in Net Debt*

For the year ended December 31 (in thousands of Canadian dollars)

|                                               | 2016<br>Budget   | 2016<br>Actual  | 2015<br>Actual<br>(restated Note 3) |
|-----------------------------------------------|------------------|-----------------|-------------------------------------|
|                                               | \$               | \$              | \$                                  |
| <b>ANNUAL SURPLUS</b>                         | <b>(305)</b>     | <b>234</b>      | <b>3,858</b>                        |
| <b>CHANGE IN NON-FINANCIAL ASSETS</b>         |                  |                 |                                     |
| Acquisition of tangible capital assets        | (30,706)         | (24,769)        | (25,624)                            |
| Amortization of tangible capital assets       | 21,991           | 23,438          | 21,457                              |
| Change in prepaid expenses                    | -                | (417)           | (27)                                |
| <b>TOTAL CHANGE IN NON-FINANCIAL ASSETS</b>   | <b>(8,715)</b>   | <b>(1,748)</b>  | <b>(4,194)</b>                      |
| <b>NET REMEASUREMENT GAINS FOR THE PERIOD</b> | <b>-</b>         | <b>248</b>      | <b>1,296</b>                        |
| <b>CHANGE IN NET DEBT</b>                     | <b>(9,020)</b>   | <b>(1,266)</b>  | <b>960</b>                          |
| <b>NET DEBT, BEGINNING OF PERIOD</b>          | <b>(95,907)</b>  | <b>(95,907)</b> | <b>(96,867)</b>                     |
| <b>NET DEBT, END OF PERIOD</b>                | <b>(104,927)</b> | <b>(97,173)</b> | <b>(95,907)</b>                     |

*Independent Electricity System Operator*  
*Statements of Cash Flows*

For the year ended December 31 (in thousands of Canadian dollars)

|                                                         | 2016            | 2015              |
|---------------------------------------------------------|-----------------|-------------------|
|                                                         |                 | (restated Note 3) |
|                                                         | \$              | \$                |
| <b>OPERATING TRANSACTIONS</b>                           |                 |                   |
| Change in accumulated deficit                           |                 |                   |
| Annual surplus                                          | 234             | 3,858             |
|                                                         | 234             | 27,800            |
| Changes in non-cash items                               |                 |                   |
| Amortization                                            | 23,438          | 21,457            |
| Pension expense                                         | 11,610          | 11,970            |
| Other employee future benefits expense                  | 8,127           | 6,901             |
|                                                         | 43,175          | 40,328            |
| Changes in non-cash balances related to operations:     |                 |                   |
| Change in accounts payable and accrued liabilities      | (7,495)         | (775)             |
| Change in accounts receivable                           | 2,096           | (10,145)          |
| Change in rebates due to market participants            | 2,956           | 9,595             |
| Change in regulated assets                              | 23,138          | 23,942            |
| Change in prepaid expenses                              | (417)           | (27)              |
|                                                         | 20,278          | 22,590            |
| Other:                                                  |                 |                   |
| Contribution to pension fund                            | (13,052)        | (12,851)          |
| Payment of employee future benefits                     | (2,377)         | (2,314)           |
|                                                         | (15,429)        | (15,165)          |
| <b>Cash provided by operating transactions</b>          | <b>48,258</b>   | <b>75,553</b>     |
| <b>CAPITAL TRANSACTIONS</b>                             |                 |                   |
| Acquisition of tangible capital assets                  | (24,769)        | (25,624)          |
| Change in accounts payable and accrued liabilities      | (2,410)         | (1,569)           |
| <b>Cash applied to capital transactions</b>             | <b>(27,179)</b> | <b>(27,193)</b>   |
| <b>INVESTING TRANSACTIONS</b>                           |                 |                   |
| Purchase of long-term investments                       | (2,751)         | (1,967)           |
| <b>Cash applied to investing transactions</b>           | <b>(2,751)</b>  | <b>(1,967)</b>    |
| <b>FINANCING TRANSACTIONS</b>                           |                 |                   |
| Debt repayment                                          | -               | (39,000)          |
| <b>Cash applied to financing transactions</b>           | <b>-</b>        | <b>(39,000)</b>   |
| <b>INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS</b> | <b>18,328</b>   | <b>(16,549)</b>   |
| <b>CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD</b>  | <b>14,715</b>   | <b>31,340</b>     |
| Unrealized foreign exchange losses for the period       | (38)            | (76)              |
| <b>CASH AND CASH EQUIVALENTS - END OF PERIOD</b>        | <b>33,005</b>   | <b>14,715</b>     |

# Notes to Financial Statements

## 1. NATURE OF OPERATIONS

- a) The Independent Electricity System Operator (IESO) is a not-for-profit, non-taxable, corporation established pursuant to Part II of the *Electricity Act, 1998*. The predecessor Independent Electricity System Operator and the Ontario Power Authority (OPA) were amalgamated by statute effective on January 1, 2015, and continued as the Independent Electricity System Operator. As set out in the *Electricity Act, 1998*, the IESO operates pursuant to a licence granted by the Ontario Energy Board (OEB). The amalgamation was effected pursuant to Bill 14, *Building Opportunity and Securing Our Future Act (Budget Measures), 2014*, which received Royal Assent on July 24, 2014. Schedule 7 of the Bill amended the *Electricity Act, 1998*, by amalgamating the two predecessor corporations and by continuing them as the Independent Electricity System Operator. The transitional provision, dealing with corporate matters, provides, among other things, that the predecessor IESO and OPA cease to exist as entities separate from the amalgamated IESO and all their rights, properties and assets become the rights, properties and assets of the amalgamated IESO, as do all outstanding debts, liabilities and obligations of the predecessor IESO and OPA. Schedule 7 of Bill 14 came into force on January 1, 2015. The objects of the IESO as contained in the *Electricity Act, 1998*, and Ontario Regulation 288/14 are as follows:
- ∞ to exercise the powers and perform the duties assigned to it under this Act, the regulations, directions, the market rules and its licence;
  - ∞ to enter into agreements with transmitters to give it authority to direct the operation of their transmission systems;
  - ∞ to direct the operation and maintain the reliability of the IESO-controlled grid to promote the purposes of this Act;
  - ∞ to participate in the development by any standards authority of criteria and standards relating to the reliability of the integrated power system;
  - ∞ to establish and enforce criteria and standards relating to the reliability of the integrated power system;
  - ∞ to work with the responsible authorities outside of Ontario to co-ordinate the IESO's activities with the activities of those authorities;
  - ∞ to operate the IESO-administered markets to promote the purposes of this Act;
  - ∞ to engage in activities related to contracting for the procurement of electricity supply, electricity capacity and conservation resources;
  - ∞ to engage in activities related to settlements, payments under a contract entered into under the authority of this Act and payments provided for under this Act or the *Ontario Energy Board Act, 1998*;
  - ∞ to engage in activities in support of the goal of ensuring adequate, reliable and secure electricity supply and resources in Ontario;
  - ∞ to forecast electricity demand and the adequacy and reliability of electricity resources for Ontario for the short term, medium term and long term;
  - ∞ to conduct independent planning for electricity generation, demand management, conservation and transmission;
  - ∞ to engage in activities to facilitate the diversification of sources of electricity supply by promoting the use of cleaner energy sources and technologies, including alternative energy sources and renewable energy sources;
  - ∞ to engage in activities in support of system-wide goals for the amount of electricity to be produced from different energy sources;
  - ∞ to engage in activities that facilitate load management;
  - ∞ to engage in activities that promote electricity conservation and the efficient use of electricity;
  - ∞ to assist the Board by facilitating stability in rates for certain types of consumers;
  - ∞ to collect and make public information relating to the short-term, medium-term and long-term electricity needs of Ontario and the adequacy and reliability of the integrated power system to meet those needs; and

- ∞ to engage in such other objects as may be prescribed by the regulations.
- b) The IESO was designated the Smart Metering Entity (SME) by Ontario Regulation 393/07 under the *Electricity Act, 1998*, on March 28, 2007. The regulation came into effect on July 26, 2007.

The objects of the Smart Metering Entity, as contained in the *Electricity Act, 1998*, are as follows:

- ∞ to plan and implement and, on an ongoing basis, oversee, administer and deliver any part of the smart metering initiative as required by regulation under this or any Act or directive made pursuant to sections 28.3 or 28.4 of the *Ontario Energy Board Act, 1998*, and, if so authorized, to have the exclusive authority to conduct these activities;
- ∞ to collect and manage and to facilitate the collection and management of information and data and to store the information and data related to the metering of consumers' consumption or use of electricity in Ontario, including data collected from distributors and, if so authorized, to have the exclusive authority to collect, manage and store the data;
- ∞ to establish, to own or lease and to operate one or more databases to facilitate collecting, managing, storing and retrieving smart metering data;
- ∞ to provide and promote non-discriminatory access, on appropriate terms and subject to any conditions in its licence relating to the protection of privacy, by distributors, retailers and other persons,
  - i. to the information and data referred to above, and
  - ii. to the telecommunication system that permits the Smart Metering Entity to transfer data about the consumption or use of electricity to and from its databases, including access to its telecommunication equipment, systems and technology and associated equipment, systems and technologies
- ∞ to own or to lease and to operate equipment, systems and technology, including telecommunication equipment, systems and technology that permit the Smart Metering Entity to transfer data about the consumption or use of electricity to and from its databases, including owning, leasing or operating such equipment, systems and technology and associated equipment, systems and technologies, directly or indirectly, including through one or more subsidiaries, if the Smart Metering Entity is a corporation;
- ∞ to engage in such competitive procurement activities as are necessary to fulfill its objects or business activities;
- ∞ to procure, as and when necessary, meters, metering equipment, systems and technology and any associated equipment, systems and technologies on behalf of distributors, as an agent or otherwise, directly or indirectly, including through one or more subsidiaries, if the Smart Metering Entity is a corporation;
- ∞ to recover, through just and reasonable rates, the costs and an appropriate return approved by the Ontario Energy Board associated with the conduct of its activities; and
- ∞ to undertake any other objects that are prescribed by associated regulation.
- c) The IESO is required to submit its proposed expenditures, revenue requirements and fees for the coming year to the OEB for review and approval. The submission may be made only with the approval or deemed approval of the IESO business plan by the Minister of Energy (Minister).

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### a) Basis of financial statement preparation

The accompanying financial statements have been prepared on a going concern basis and in accordance with Canadian public sector accounting standards (PSAB) and reflect the following significant accounting policies.

## **b) Revenue recognition**

System fees earned by the IESO are based on approved rates for each megawatt of electricity withdrawn from the IESO-controlled grid (including scheduled exports) and embedded generation. System fees are recognized as revenue at the time the electricity is withdrawn. Rebates are recognized in the year in which the regulatory deferral account, before such rebates, exceeds regulated limits.

For 2015, the system fee for the then newly amalgamated IESO was comprised of the combined rate calculations of the respective pre-amalgamation entities. Specifically, the former IESO rate base was calculated on electricity withdrawn from the IESO-controlled grid (including scheduled exports and embedded generation), whereas the former OPA rate base only considered Ontario electricity consumers. The OEB approved the continued use of this combined rate calculation for 2016 in an interim order issued on December 22, 2015.

These financial statements do not include the revenue and expenses of the financial transactions of market participants within the IESO-administered markets (IAM).

Other revenue represents amounts that accrue to the IESO relating to investment income on funds passing through market settlement accounts, as well as application fees. Such revenue is recognized as it is earned.

Interest and investment income represents realized interest income and investment gains or losses on cash, cash equivalents, short-term investments and long-term investments.

Market sanctions represent funds received to offset payments disbursed related to penalties, damages, fines and payment adjustments arising from resolved settlement disputes.

## **c) Financial instruments**

The IESO records cash and cash equivalents, investment portfolio and foreign currency exchange forward contracts at fair value. The cumulative change in fair value of these financial instruments is recorded in accumulated surplus as remeasurement gains and losses and is included in the value of the respective financial instrument shown in the statement of financial position and the statement of remeasurement gains and losses. Upon disposition of the financial instruments, the cumulative remeasurement gains and losses are reclassified to the statement of operations and all other gains and losses associated with the disposition of the financial instrument are recorded in the statement of operations. Transaction costs are charged to operations as incurred.

Cash and cash equivalents comprise cash, term deposits and other short-term, highly rated investments with original maturity dates of less than 90 days.

The IESO records accounts receivable, accounts payable and debt at amortized cost.

## **d) Regulated assets and liabilities**

As a rate-regulated entity, the IESO, in appropriate circumstances establishes regulated assets or liabilities and thereby defers the impact on the statement of operations of certain expenses or revenues because they are probable to be collected or refunded to market participants through future billings. The IESO has applied guidance from United States Generally Accepted Accounting Principles (US GAAP) Topic 980, *Regulated Operations*, in this policy.

## **e) Market accounts – assets and liabilities**

The IESO records the market accounts assets, liabilities and amounts due to and from market participants held on behalf of the IESO-administered markets in its statements of financial position. The IESO-administered markets is a balancing system, and as such, the net position of market accounts will settle to a \$nil balance in accordance with market rules.



#### **f) Tangible capital assets**

Tangible capital assets are recorded at cost, which includes all amounts directly attributable to the acquisition, construction, development or betterment of the asset. The IESO capitalizes applicable interest as part of the cost of tangible capital assets.

#### **g) Assets under construction**

Assets under construction generally relates to the costs of physical facilities, hardware and software, and includes costs paid to vendors, internal and external labour, consultants and interest related to funds borrowed to finance the project. Costs relating to assets under construction are transferred to tangible capital assets when the asset under construction is deemed to be ready for use.

#### **h) Amortization**

The capital cost of tangible capital assets in service is amortized on a straight-line basis over their estimated service lives.

The estimated service lives in years, from the date the assets were acquired, are:

| Class                            | Estimated Average<br>Service Life 2016 | Estimated Average<br>Service Life 2015 |
|----------------------------------|----------------------------------------|----------------------------------------|
| Facilities                       | 37                                     | 37                                     |
| Market systems and applications  | 4 to 12                                | 4 to 12                                |
| Infrastructure and other assets  | 4 to 10                                | 4 to 7                                 |
| Meter data management/repository | 10                                     | 10                                     |

Gains and losses on sales or premature retirements of tangible capital assets are charged to operations.

The estimated service lives of tangible capital assets are subject to periodic review. The effects of changes in the estimated lives are amortized on a prospective basis. The most recent review was completed in fiscal 2016.

#### **i) Pension, other post-employment benefits and compensated absences**

The IESO's post-employment benefit programs include pension, group life insurance, health care, long-term disability and workers' compensation benefits.

The IESO accrues obligations under pension and other post-employment benefit (OPEB) plans and the related costs, net of plan assets. Pension and OPEB expenses and obligations are determined annually by independent actuaries using the projected benefit method and management's best estimate of expected return on plan assets, salary escalation, retirement ages of employees, mortality and expected health-care costs. The discount rate used to value liabilities is based on the expected rate of return on plan assets as at the measurement date of September 30.

The expected return on plan assets is based on management's long-term best estimate using a market-related value of plan assets. The market-related value of plan assets is determined using the average value of assets over three years as at the measurement date of September 30.

Pension and OPEB expenses are recorded during the year in which employees render services. Pension and OPEB expenses consist of current service costs, interest expense on liabilities, expected return on plan assets and the cost of plan amendments in the period. Actuarial gains/(losses) arise from, among other things, the difference between the actual rate of return on plan assets for a period and the expected long-term rate of return on plan assets for that period or from changes in actuarial assumptions used to

determine the accrued benefit obligations. Actuarial gains/(losses) are amortized over the expected average remaining service life of the employees covered by the plan.

The expected average remaining service life of employees covered by the pension plans is 15 years (2015 – 15 years) and OPEB plan is 16.2 years (2015 – 14.7 years).

The IESO sick pay benefits accumulate but do not vest. The IESO accrues sick pay benefits based on the expectation of future utilization and records the accrual within accounts payable and accrued liabilities.

#### **j) Foreign currency exchange**

Transactions denominated in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing on the date of the transaction. Items on the statement of financial position denominated in foreign currency are translated to Canadian dollars at the rate of exchange as of the financial statements date. The cumulative unrealized foreign currency exchange gains and losses of items continuing to be recognized on the statement of financial position are recorded in accumulated deficit as remeasurement gains and losses and shown in the statement of financial position and the statement of remeasurement gains and losses. Upon settlement of the item denominated in a foreign currency, the cumulative remeasurement gains and losses are reclassified to the statement of operations, and all other gains and losses associated with the disposition of the financial instrument are recorded in the statement of operations.

#### **k) Use of estimates**

The preparation of the financial statements in conformity with Canadian public sector accounting standards requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities and the disclosure of contingent assets and liabilities as at the date of the financial statements. The IESO's accounts that involve a greater degree of uncertainty include the carrying values of tangible capital assets, accrued pension liability and accrual for employee future benefits other than pensions. Actual results could differ from those estimates.

### **3. NEW ACCOUNTING POLICIES**

As of January 1, 2016, the IESO changed its accounting policy regarding the recognition of assets and liabilities subject to rate regulation. The change was made to better reflect the economic substance of certain types of expenses that may not be directly recovered through the normal revenue requirement model. This change has been applied retroactively and has increased amounts previously unrecorded for regulatory assets and decreased amounts previously reported for accumulated deficit.

The IESO recognizes two regulated assets: 1) unrecovered smart metering expenses and 2) unrecovered PSAB transition items.

The smart metering expenses result from the IESO's role as the Smart Metering Entity. As such, the IESO funds its SME operating costs and capital investment in the meter data management/repository (MDM/R) through fees from users of smart meters in Ontario. The OEB approves the Smart Metering Entity charge and the charge is intended to cover the costs of developing and operating the MDM/R.

The unrecovered PSAB transition items result from the IESO's adoption of Canadian public sector accounting standards effective January 1, 2011. The adoption of PSAB was accounted for by retroactive application with restatement of prior periods subject to the requirements in Section PS 2125, *First-time Adoption by Government Organizations*. The corresponding change to pension and other post-employment benefits resulted in previously unrecognized actuarial losses and past service costs of \$80,617 thousand at the date of transition.

**Regulated assets consist of the following:**

| As of December 31 (in thousands of Canadian dollars) | 2016          | 2015          |
|------------------------------------------------------|---------------|---------------|
|                                                      | \$            | \$            |
| Unrecovered smart metering expenses                  | 21,623        | 40,849        |
| Unrecovered PSAB transition items                    | 43,441        | 47,353        |
| <b>Closing balance</b>                               | <b>65,064</b> | <b>88,202</b> |

In addition, as of January 1, 2016, the IESO changed its accounting policy regarding the recognition of market accounts assets and liabilities on the statement of financial position. The change was made to better reflect the assets and liabilities and amounts due to and from market participants held by the IESO on behalf of the IAM at year end. This change has been applied retroactively and has increased amounts previously unrecorded for market accounts assets and liabilities. There is no impact to the accumulated deficit or revenues and expenses as the IESO is not party to these transactions as per the market rules.

**Components of the market accounts are as follows:**

| As of December 31 (in thousands of Canadian dollars) | 2016        | 2015        |
|------------------------------------------------------|-------------|-------------|
|                                                      | \$          | \$          |
| Cash, restricted for market activities               | 244,755     | 271,574     |
| Amounts due from market participants                 | 1,391,260   | 1,171,389   |
| Interest receivable                                  | 186         | 158         |
| Revolving line of credit                             | (150,501)   | (12,739)    |
| HST receivable                                       | 25,531      | 20,247      |
| Amounts due to market participants                   | (1,392,643) | (1,380,086) |
| Other liabilities                                    | (118,588)   | (70,543)    |
| <b>Closing balance</b>                               | <b>-</b>    | <b>-</b>    |

**Comparative figures**

A detailed reconciliation of the IESO's restated statement of financial position as at December 31, 2015, as follows:

| As of (in thousands of Canadian dollars)                          | December 31, 2015<br>(as reported) | December 31, 2015<br>adjustments | December 31, 2015<br>(as restated) |
|-------------------------------------------------------------------|------------------------------------|----------------------------------|------------------------------------|
|                                                                   | \$                                 | \$                               | \$                                 |
| <b>FINANCIAL ASSETS</b>                                           |                                    |                                  |                                    |
| Cash and cash equivalents                                         | 14,715                             |                                  | 14,715                             |
| Accounts receivable                                               | 33,199                             |                                  | 33,199                             |
| Long-term investments                                             | 37,318                             |                                  | 37,318                             |
| Regulated assets                                                  | -                                  | 88,202                           | 88,202                             |
| Market accounts - assets                                          | -                                  | 1,443,120                        | 1,443,120                          |
| <b>TOTAL FINANCIAL ASSETS</b>                                     | <b>85,232</b>                      | <b>1,531,323</b>                 | <b>1,616,554</b>                   |
| <b>LIABILITIES</b>                                                |                                    |                                  |                                    |
| Accounts payable and accrued liabilities                          | 48,868                             |                                  | 48,868                             |
| Accrued interest on debt                                          | 315                                |                                  | 315                                |
| Rebates due to market participants                                | 9,595                              |                                  | 9,595                              |
| Debt                                                              | 90,000                             |                                  | 90,000                             |
| Accrued pension liability                                         | 36,062                             |                                  | 36,062                             |
| Accrued liability for employee future benefits other than pension | 84,501                             |                                  | 84,501                             |
| Market accounts - liabilities                                     | -                                  | 1,443,120                        | 1,443,120                          |
| <b>TOTAL LIABILITIES</b>                                          | <b>269,341</b>                     | <b>1,443,121</b>                 | <b>1,712,461</b>                   |
| <b>NET DEBT</b>                                                   | <b>(184,109)</b>                   | <b>88,202</b>                    | <b>(95,907)</b>                    |
| <b>NON-FINANCIAL ASSETS</b>                                       |                                    |                                  |                                    |
| Net tangible capital assets                                       | 103,716                            |                                  | 103,716                            |
| Prepaid expenses                                                  | 6,197                              |                                  | 6,197                              |
| <b>TOTAL NON-FINANCIAL ASSETS</b>                                 | <b>109,913</b>                     |                                  | <b>109,913</b>                     |
| <b>ACCUMULATED SURPLUS/(DEFICIT)</b>                              |                                    |                                  |                                    |
| Accumulated surplus/(deficit) from operations                     | (81,854)                           | 88,202                           | 6,348                              |
| Accumulated remeasurement gains                                   | 7,658                              |                                  | 7,658                              |
| <b>ACCUMULATED SURPLUS/(DEFICIT)</b>                              | <b>(74,196)</b>                    | <b>88,202</b>                    | <b>14,006</b>                      |

A detailed reconciliation of the IESO's restated statement of operations for the year ended December 31, 2015, is as follows:

| For the year ended (in thousands of Canadian dollars)               | December 31,<br>2015<br>(as reported) | December 31,<br>2015<br>adjustments | December 31,<br>2015<br>(as restated) |
|---------------------------------------------------------------------|---------------------------------------|-------------------------------------|---------------------------------------|
|                                                                     | \$                                    | \$                                  | \$                                    |
| <b>IESO CORE OPERATIONS</b>                                         |                                       |                                     |                                       |
| System fees                                                         | 190,099                               | (3,912)                             | 186,187                               |
| Other revenue                                                       | 5,377                                 |                                     | 5,377                                 |
| Interest and investment income                                      | 1,430                                 |                                     | 1,430                                 |
| <b>Core operations revenues</b>                                     | <b>196,906</b>                        | <b>(3,912)</b>                      | <b>192,994</b>                        |
| Compensation and benefits                                           | (104,994)                             |                                     | (104,994)                             |
| Professional and consulting                                         | (21,461)                              |                                     | (21,461)                              |
| Operating and administration                                        | (35,005)                              |                                     | (35,005)                              |
| <b>Core operating expenses</b>                                      | <b>(161,460)</b>                      |                                     | <b>(161,460)</b>                      |
| Amortization                                                        | (17,933)                              |                                     | (17,933)                              |
| Interest                                                            | (1,610)                               |                                     | (1,610)                               |
| <b>Core expenses</b>                                                | <b>(181,003)</b>                      |                                     | <b>(181,003)</b>                      |
| <b>Core operations annual surplus before rebates</b>                | <b>15,903</b>                         | <b>(3,912)</b>                      | <b>11,991</b>                         |
| Rebates due to market participants                                  | (9,595)                               |                                     | (9,595)                               |
| <b>Core operations annual surplus</b>                               | <b>6,308</b>                          | <b>(3,912)</b>                      | <b>2,396</b>                          |
| <b>MARKET SANCTIONS AND PAYMENT ADJUSTMENTS</b>                     |                                       |                                     |                                       |
| <b>Market sanctions and payment adjustment</b>                      | <b>6,021</b>                          |                                     | <b>6,021</b>                          |
| Compensation and benefits                                           | (3,094)                               |                                     | (3,094)                               |
| Professional and consulting                                         | (1,351)                               |                                     | (1,351)                               |
| Operating and administrative                                        | (114)                                 |                                     | (114)                                 |
| <b>Customer education and market enforcement expenses</b>           | <b>(4,559)</b>                        |                                     | <b>(4,559)</b>                        |
| <b>Market sanctions and payment adjustments annual surplus</b>      | <b>1,462</b>                          |                                     | <b>1,462</b>                          |
| <b>SMART METERING ENTITY</b>                                        |                                       |                                     |                                       |
| <b>Smart metering charge</b>                                        | <b>46,215</b>                         | <b>(20,030)</b>                     | <b>26,185</b>                         |
| Compensation and benefits                                           | (2,607)                               |                                     | (2,607)                               |
| Professional and consulting                                         | (14,902)                              |                                     | (14,902)                              |
| Operating and administration                                        | (4,200)                               |                                     | (4,200)                               |
| <b>Smart metering operating expenses</b>                            | <b>(21,709)</b>                       |                                     | <b>(21,709)</b>                       |
| Amortization                                                        | (3,524)                               |                                     | (3,524)                               |
| Interest                                                            | (952)                                 |                                     | (952)                                 |
| <b>Smart metering expenses</b>                                      | <b>(26,185)</b>                       |                                     | <b>(26,185)</b>                       |
| <b>Smart metering entity annual surplus</b>                         | <b>20,030</b>                         | <b>(20,030)</b>                     | <b>-</b>                              |
| <b>ANNUAL SURPLUS</b>                                               | <b>27,800</b>                         | <b>(23,942)</b>                     | <b>3,858</b>                          |
| ACCUMULATED DEFICIT FROM OPERATIONS, BEGINNING OF PERIOD            | (109,654)                             | 112,144                             | 2,490                                 |
| <b>ACCUMULATED SURPLUS/(DEFICIT) FROM OPERATIONS, END OF PERIOD</b> | <b>(81,854)</b>                       | <b>88,202</b>                       | <b>6,348</b>                          |

#### 4. LONG-TERM INVESTMENTS

Long-term investments in a balanced portfolio of pooled funds are valued by the pooled funds manager based on published price quotations and amount to \$39,972 thousand (2015 – \$37,019 thousand). As at December 31, the market value allocation of these long-term investments was 62.3% equity securities and 37.7% debt securities (2015 – 56.0% and 44.0% respectively).

##### Balanced portfolio of pooled funds

|                                                      |               |               |
|------------------------------------------------------|---------------|---------------|
| As at December 31 (in thousands of Canadian dollars) | 2016          | 2015          |
|                                                      | \$            | \$            |
| Opening balance                                      | 37,019        | 33,758        |
| Net purchase of investments                          | 2,667         | 1,889         |
| Change in fair value                                 | 286           | 1,372         |
| <b>Closing balance</b>                               | <b>39,972</b> | <b>37,019</b> |

In addition to the balanced portfolio of pooled funds, the IESO has a long-term deposit with Canada Revenue Agency in the amount of \$383 thousand (2015 – \$299 thousand) pertaining to the Retirement Compensation Arrangements Trust (Note 6).

## 5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

| As at December 31 (in thousands of Canadian dollars) | 2016          | 2015          |
|------------------------------------------------------|---------------|---------------|
|                                                      | \$            | \$            |
| Relating to operations                               | 35,630        | 43,125        |
| Relating to tangible capital assets                  | 3,333         | 5,743         |
| <b>Closing balance</b>                               | <b>38,963</b> | <b>48,868</b> |

## 6. REBATES DUE TO MARKET PARTICIPANTS AND ACCUMULATED SURPLUS

In 2016, the IESO recognized \$12,551 thousand in rebates due to market participants of system fees (2015 – \$9,595). As at December 31, 2016, rebates due to market participants were \$22,146 thousand, with the 2015 portion of \$9,595 thousand rebated in January 2017.

The IESO's approved regulatory deferral account balance has been historically maintained at a maximum of \$10.0 million. The 2016 approved regulatory deferral account balance at \$10.0 million was approved by the OEB on December 1, 2016.

Prior to 2014, unrealized gains and losses from portfolio investments and foreign exchange were included in the balance of the regulatory deferral account (life-to-date total \$4,144 thousand). As of January 1, 2014, only realized gains and losses are included in this balance.

As at December 31, the components of the accumulated surplus were as follows:

### Accumulated Surplus

| As at December 31 (in thousands of Canadian dollars)     | 2016          | 2015          |
|----------------------------------------------------------|---------------|---------------|
|                                                          | \$            | \$            |
| Regulatory deferral account (a)                          | 10,000        | 10,000        |
| Accumulated market sanctions and payment adjustments (b) | 726           | 492           |
| Remeasurement gains                                      | 3,762         | 3,514         |
| <b>Accumulated surplus – end of year</b>                 | <b>14,488</b> | <b>14,006</b> |

### a) Regulatory Deferral Account

| As at December 31 (in thousands of Canadian dollars) | 2016          | 2015          |
|------------------------------------------------------|---------------|---------------|
|                                                      | \$            | \$            |
| Accumulated surplus – beginning of year              | 10,000        | 7,604         |
| Revenues (before rebates due to market participants) | 190,219       | 192,994       |
| Rebates due to market participants                   | (12,551)      | (9,595)       |
| Core operation expenses                              | (177,668)     | (181,003)     |
| <b>Accumulated surplus – end of year</b>             | <b>10,000</b> | <b>10,000</b> |

## **b) Accumulated Market Sanctions and Payment Adjustments**

| As at December 31 (in thousands of Canadian dollars) | 2016       | 2015       |
|------------------------------------------------------|------------|------------|
|                                                      | \$         | \$         |
| Accumulated surplus/(deficit) – beginning of year    | 492        | (970)      |
| Market sanctions and payment adjustments             | 3,889      | 6,021      |
| Customer education and market enforcement expenses   | (3,655)    | (4,559)    |
| <b>Accumulated surplus – end of year</b>             | <b>726</b> | <b>492</b> |

## **7. DEBT**

### **Note payable to Ontario Electricity Financial Corporation (OEFC)**

In April 2014, the IESO entered into a three-year note payable with the OEFC. The note payable is unsecured, bears interest at a fixed rate of 2.046% per annum and is repayable in full on April 30, 2017. Interest accrues daily and is payable in arrears semi-annually in April and October of each year. As at December 31, 2016, the note payable to the OEFC was \$90.0 million (December 31, 2015 – \$90.0 million).

For the year ended December 31, 2016, the interest expense on the note payable was \$1,841 thousand (2015 – \$1,841 thousand).

### **Credit facility**

The IESO has an unsecured credit facility agreement with the OEFC, which will make available to the IESO an amount up to \$95.0 million. Advances are payable at a variable interest rate equal to the Province of Ontario's cost of borrowing for a 30-day term plus 0.50% per annum, with draws, repayments and interest payments due monthly. The credit facility expires April 30, 2017. As at December 31, 2016, no amount was drawn on the credit facility (December 31, 2015 – \$nil).

For the year ended December 31, 2016, the interest expense on the credit facility was \$nil (2015 – \$279 thousand).

### **Retirement Compensation Arrangements Trust**

In July 2013, the IESO established a Retirement Compensation Arrangements (RCA) Trust to provide security for the IESO's obligations under the terms of the supplemental employee retirement plan for its employees. As at December 31, 2016, the IESO has provided the RCA trustee with a bank letter of credit of \$30,466 thousand (2015 – \$28,408 thousand) the trustee can draw on if the IESO is in default under the terms of this plan.

## **8. POST-EMPLOYMENT BENEFIT PLANS**

The IESO provides pension and other employee post-employment benefits, comprising group life insurance, long-term disability and group medical and dental plans, for the benefit of current and retired employees.

### **Pension plans**

The IESO provides a contributory defined benefit, indexed, registered pension plan. In addition to the funded, registered pension plan, the IESO provides certain non-registered defined benefit pensions through an unfunded, indexed, non-registered plan.

## Other employee future benefits

The group life insurance, long-term disability and group medical and dental benefits are provided through unfunded, non-registered defined benefit plans.

### Summary of accrued benefit obligations and plan assets

| (in thousands of Canadian dollars)                                         | 2016<br>Pension<br>Benefits | 2015<br>Pension<br>Benefits | 2016<br>Other<br>Benefits | 2015<br>Other<br>Benefits |
|----------------------------------------------------------------------------|-----------------------------|-----------------------------|---------------------------|---------------------------|
|                                                                            | \$                          | \$                          | \$                        | \$                        |
| Accrued benefit obligation                                                 | 507,724                     | 482,994                     | 91,014                    | 83,455                    |
| Fair value of plan assets                                                  | 523,756                     | 475,714                     | -                         | -                         |
| Funded status as of measurement date                                       | 16,032                      | (7,280)                     | (91,014)                  | (83,455)                  |
| Employer contribution/other benefits payments after measurement date       | 2,416                       | 427                         | 588                       | 582                       |
| Unrecognized actuarial (gain)/loss                                         | (53,068)                    | (29,209)                    | 175                       | (1,628)                   |
| <b>Accrued liability recognized in the statement of financial position</b> | <b>(34,620)</b>             | <b>(36,062)</b>             | <b>(90,251)</b>           | <b>(84,501)</b>           |

### Registered pension plan assets

As at the measurement date of September 30, the proportion of the fair value of registered pension plan assets held in each asset class was as follows:

|                                    | 2016          | 2015          |
|------------------------------------|---------------|---------------|
| Canadian equity securities         | 20.2%         | 19.9%         |
| Foreign equity securities          | 39.9%         | 41.8%         |
| Canadian debt securities           | 39.8%         | 39.0%         |
| Cash equivalents                   | 0.4%          | 0.6%          |
| Forward foreign exchange contracts | (0.3%)        | (1.3%)        |
|                                    | <b>100.0%</b> | <b>100.0%</b> |

Principal assumptions used to calculate benefit obligations at the end of the year are determined at that time and are as follows:

|                                        | 2016<br>Pension<br>Benefits | 2015<br>Pension<br>Benefits | 2016<br>Other<br>Benefits | 2015<br>Other<br>Benefits |
|----------------------------------------|-----------------------------|-----------------------------|---------------------------|---------------------------|
| Discount rate at the end of the period | 5.75%                       | 6.00%                       | 5.75%                     | 6.00%                     |
| Rate of compensation increase          | 3.50%                       | 3.75%                       | 3.50%                     | 3.75%                     |
| Rate of indexing                       | 2.00%                       | 2.25%                       | 2.00%                     | 2.25%                     |

The assumed prescription drug inflation was 8.00% for 2016, grading down to an ultimate rate 4.50% per year in 2030. Dental costs are assumed to increase by 4.00% per year.

Benefit costs and plan contributions for pension and other plans are summarized as follows:

| (in thousands of Canadian dollars) | 2016<br>Pension<br>Benefits | 2015<br>Pension<br>Benefits | 2016<br>Other<br>Benefits | 2015<br>Other<br>Benefits |
|------------------------------------|-----------------------------|-----------------------------|---------------------------|---------------------------|
|                                    | \$                          | \$                          | \$                        | \$                        |
| Current service cost (employer)    | 11,117                      | 10,547                      | 3,107                     | 2,857                     |
| Interest cost                      | 29,292                      | 28,143                      | 5,120                     | 4,797                     |
| Expected return on plan assets     | (27,626)                    | (26,053)                    | -                         | -                         |
| Amortization of net actuarial loss | (1,173)                     | (667)                       | (100)                     | (753)                     |
| <b>Benefit cost</b>                | <b>11,610</b>               | <b>11,970</b>               | <b>8,127</b>              | <b>6,901</b>              |

| (in thousands of Canadian dollars)           | 2016<br>Pension<br>Benefits | 2015<br>Pension<br>Benefits | 2016<br>Other<br>Benefits | 2015<br>Other<br>Benefits |
|----------------------------------------------|-----------------------------|-----------------------------|---------------------------|---------------------------|
|                                              | \$                          | \$                          | \$                        | \$                        |
| Employer contribution/other benefit payments | 13,052                      | 12,851                      | 2,377                     | 2,314                     |
| Plan participants' contributions             | 5,811                       | 5,162                       | -                         | -                         |
| Benefits paid                                | 23,317                      | 21,155                      | 2,377                     | 2,314                     |

The most recent actuarial valuation of the registered pension plan for funding purposes was at January 1, 2014, and the next required valuation is to be effective January 1, 2017.

Principal assumptions used to calculate benefit costs for the year are determined at the beginning of the period and are as follows:

|                                              | 2016<br>Pension<br>Benefits | 2015<br>Pension<br>Benefits | 2016<br>Other<br>Benefits | 2015<br>Other<br>Benefits |
|----------------------------------------------|-----------------------------|-----------------------------|---------------------------|---------------------------|
| Discount rate at the beginning of the period | 6.00%                       | 6.15%                       | 6.00%                     | 6.15%                     |
| Rate of compensation increase                | 3.75%                       | 3.75%                       | 3.75%                     | 3.75%                     |
| Rate of indexing                             | 2.25%                       | 2.25%                       | 2.25%                     | 2.25%                     |

## 9. TANGIBLE CAPITAL ASSETS

Net tangible capital assets consist of the following:

### Tangible Capital Assets

| (in thousands of Canadian dollars) | As at<br>Dec. 31, 2015 | Additions     | Disposals | As at<br>Dec. 31, 2016 |
|------------------------------------|------------------------|---------------|-----------|------------------------|
|                                    | \$                     | \$            | \$        | \$                     |
| Facilities                         | 52,281                 | 3,692         | -         | 55,973                 |
| Market systems and applications    | 278,458                | 28,535        | -         | 306,993                |
| Infrastructure and other assets    | 60,180                 | 3,175         | -         | 63,355                 |
| Meter data management/repository   | 35,900                 | 1,011         | -         | 36,911                 |
| <b>Total cost</b>                  | <b>426,819</b>         | <b>36,413</b> |           | <b>463,232</b>         |

### Accumulated Amortization

| (in thousands of Canadian dollars)    | As at<br>Dec. 31, 2015 | Amortization<br>Expense | Disposals | As at<br>Dec. 31, 2016 |
|---------------------------------------|------------------------|-------------------------|-----------|------------------------|
|                                       | \$                     | \$                      | \$        | \$                     |
| Facilities                            | (22,604)               | (1,697)                 | -         | (24,301)               |
| Market systems and applications       | (251,210)              | (12,336)                | -         | (263,546)              |
| Infrastructure and other assets       | (47,228)               | (5,544)                 | -         | (52,772)               |
| Meter data management/repository      | (25,329)               | (3,861)                 | -         | (29,190)               |
| <b>Total accumulated amortization</b> | <b>(346,371)</b>       | <b>(23,438)</b>         |           | <b>(369,809)</b>       |



## Net Book Value

| (in thousands of Canadian dollars) | As at<br>December 31, 2015 | As at<br>December 31, 2016 |
|------------------------------------|----------------------------|----------------------------|
|                                    | \$                         | \$                         |
| Facilities                         | 29,677                     | 31,672                     |
| Market systems and applications    | 27,248                     | 43,447                     |
| Infrastructure and other assets    | 12,952                     | 10,583                     |
| Meter data management/repository   | 10,571                     | 7,721                      |
| <b>Total net book value</b>        | <b>80,448</b>              | <b>93,423</b>              |
| Assets under construction          | 23,268                     | 11,624                     |
| <b>Net tangible capital assets</b> | <b>103,716</b>             | <b>105,047</b>             |

In 2016, there were no adjustments to management's estimates of remaining asset service lives (2015 – decrease of \$653 thousand).

Interest capitalized to assets under construction during 2016 was \$260 thousand (2015 – \$263 thousand).

## 10. OTHER REVENUE

In its administration of the IESO-administered markets, the IESO directs the investment of market funds in highly rated, short-term investments throughout the settlement cycle. The IESO is entitled to receive the investment interest and investment gains, net of investment losses earned on funds passing through the real-time market settlement accounts. The IESO is not entitled to the principal on real-time market investments.

The IESO recognized investment income earned in the market settlement accounts of \$2,508 thousand in 2016 (2015 – \$3,212 thousand).

## 11. RELATED PARTY TRANSACTIONS

The Province of Ontario is a related party as it is the controlling entity of the IESO. The OEFC, OEB, Hydro One and Ontario Power Generation Inc. (OPG) are related parties of the IESO, through the common control of the Province of Ontario. Transactions between these parties and the IESO were as follows:

The IESO holds a note payable and an unsecured credit facility agreement with the OEFC (Note 6). Interest payments made by the IESO in 2016 for the note payable were \$1,841 thousand (2015 – \$1,841 thousand) and for the credit facility were \$nil (2015 – \$328 thousand). As of December 31, 2016, the IESO had an accrued interest payable balance with the OEFC of \$315 thousand (2015 – \$315 thousand).

Under the *Ontario Energy Board Act, 1998*, the IESO incurs registration and license fees. The total of the transactions with the OEB was \$1,747 thousand in 2016 (2015 – \$1,671 thousand).

The IESO performed connection and bulk electric system exception assessments for Hydro One in 2016. In 2016, the IESO invoiced Hydro One \$610 thousand (2015 – \$310 thousand).

The IESO procures short circuit studies and protection impact assessments as part of connection assessments, approvals and meter services on IESO-owned interconnected revenue meters from Hydro One. Additionally, the IESO paid Hydro One for the removal of the microwave tower at the Clarkson location. In 2016, the IESO incurred costs of \$188 thousand (2015 – \$525 thousand) for these services. As of December 31, 2016, the IESO had a net payable balance with Hydro One of \$4 thousand (2015 – \$149 thousand).

The IESO performed connection assessment and approvals for OPG, administered telecommunication services to market participants to connect to the real-time market systems and provides market-related training courses. In 2016, OPG was invoiced \$124 thousand (2015 – \$137 thousand). As of December 31, 2016, the IESO had a net receivable balance with OPG of \$5 thousand (2015 – \$4 thousand).

## 12. FINANCIAL RISK MANAGEMENT

The IESO is exposed to financial risks in the normal course of its business operations, including market risks resulting from volatilities in equity, debt, and foreign currency exchange markets, as well as credit risk and liquidity risk. The nature of the financial risks and the IESO's strategy for managing these risks have not changed significantly from the prior year.

### a) Market Risk

Market risk refers to the risk that the fair value or future cash flows of a financial instrument will fluctuate to cause changes in market prices. The IESO is primarily exposed to three types of market risk: currency risk, interest rate risk and equity risk. The IESO monitors its exposure to market risk fluctuations and may use financial instruments to manage these risks as it considers appropriate. The IESO does not use derivative instruments for trading or speculative purposes.

#### i) Currency Risk

The IESO conducts certain transactions in U.S. dollars, primarily related to vendors' payments, and maintains a U.S. dollar-denominated bank account. From time to time, the IESO may utilize forward purchase contracts to purchase U.S. dollars for delivery at a specified date in the future at a fixed exchange rate. In addition, the IESO utilizes U.S. dollar spot rate purchases in order to satisfy any current accounts. As at December 31, 2016, the IESO did not have any outstanding forward purchase contracts.

#### ii) Interest Rate Risk

The IESO is exposed to movements or changes in interest rates primarily through its short-term variable rate credit facility, cash equivalents' securities and long-term investments. Long-term investments include investments in a pooled Canadian bond fund. The potential impact to the securities' value had the prevailing interest rates changed by 25 basis points, assuming a parallel shift in the yield curve with all other variables held constant, is estimated at \$0.6 million as at December 31, 2016 (2015 – \$0.6 million).

#### iii) Equity Risk

The IESO is exposed to changes in equity prices through its long-term investments. Long-term investments include investments in pooled equity funds. A 30% change in the valuation of equities as at December 31, 2016, would have resulted in a change for the year of approximately \$7.5 million (2015 – \$6.8 million). The fair values of all financial instruments measured at fair value are derived from quoted prices (unadjusted) in active markets for identical assets.

b) Credit Risk

Credit risk refers to the risk that one party to a financial instrument may cause a financial loss for the other party by failing to meet its obligations under the terms of the financial instrument. The IESO is exposed directly to credit risk related to cash equivalents' securities and accounts receivable, and indirectly through its exposure to the long-term investments in a Canadian bond pooled fund. The IESO manages credit risk associated with cash equivalents' securities through an approved management policy that limits investments to primarily investment-grade investments with counterparty-specific limits. The accounts receivable balance as at December 31, 2016, included no material items past due and substantially all of the balance was collected within 30 days from December 31, 2016. The long-term Canadian bond pooled fund is comprised of primarily investment-grade securities.

c) Liquidity Risk

Liquidity risk refers to the risk that the IESO will encounter financial difficulty in meeting obligations associated with its financial liabilities when due. The IESO manages liquidity risk by forecasting cash flows to identify cash flows and financing requirements. Cash flows from operations, short-term investments, long-term investments and maintaining appropriate credit facilities help to reduce liquidity risk. The IESO's long-term investments are normally able to be redeemed within three business days; however, the investment manager of the pooled funds has the authority to require a redemption in-kind rather than cash and has the ability to suspend redemptions if deemed necessary.

### 13. COMMITMENTS

#### Operating commitments

The obligations of the IESO with respect to non-cancellable operating leases over the next four years are as follows:

As at December 31 (thousands of Canadian dollars)

|      | \$    |
|------|-------|
| 2017 | 5,489 |
| 2018 | 5,004 |
| 2019 | 3,919 |
| 2020 | 3,195 |

### 14. CONTINGENCIES

The IESO is subject to various claims, legal actions and investigations that arise in the normal course of business. While the final outcome of such matters cannot be predicted with certainty, management believes that the resolution of such claims, actions and investigations will not have a material impact on the IESO's financial position or results of operations.

### 15. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted in 2016.