2017 REGISTRATION FEES, THE FORECAST VARIANCE DEFERRAL ACCOUNT, AND CAPITAL EXPENSES

2017 Registration Fees

The IESO proposes to continue charging the registration and application fees as previously approved by the Board and as described below:

a) Approval to continue to charge registration fees of up to $10,000 per proposal for electricity supply and capacity procurements, including conservation and load management procurements.

b) Approval to continue to charge non-refundable application fees for the Feed-in-Tariff ("FIT") program of $0.50/kW of proposed Contract Capacity, having a minimum of $500 and to a maximum of $5,000.

c) Approval to continue charging $1,000 for the IESO's market participation application fee.

All fees listed above received approval through a Board decision dated December 1, 2016 (EB-2015-0275).

The IESO is not seeking to continue the Large Renewable Procurement fee in 2017.

The Forecast Variance Deferral Account

In its 2016 Revenue Requirement Submission, the IESO sought, and the Board approved, the continuation of the Forecast Variance Deferral Account ("FVDA").

The IESO requests approval to continue to use the FVDA. The IESO's revenue requirement is a fixed amount approved by the Board with the IESO usage fees determined based on a forecast of withdrawals from the IESO controlled grid, embedded generation and exports. While the IESO provides a forecast of these withdrawals, there is inherently a variance between the forecast withdrawals and actual withdrawals. Similarly, it is to be expected that there will generally be some variance between actual revenues and expenses and the Board-approved revenue requirement. The IESO proposes to continue to track these variances through the FVDA.

Retaining revenues received in 2017 above the proposed 2017 Revenue Requirement

In addition to the $10 million operating reserve, the IESO is seeking approval to retain up to $5 million in excess revenues received in 2017. These excess revenues would include those above the proposed 2017 net revenue requirement of $190.8 million as allocated by Elenchus to each customer, or underspent in 2017. Any retained revenues or underspend would be used to minimize potential fee increases for domestic and export usage fees in 2018. As this is not intended to result in a cross subsidy, any retained 2017 revenues or underspend would be tracked for each customer type, domestic and export, and applied only to their respective 2018 usage fee. The 2017 allocated revenue requirement for each customer class as calculated by Elenchus is shown in Table 1 below:

Table 1: 2017 Allocated Revenue Requirement by customer class

	2017 allocated revenue requirement as calculated by Elenchus

Domestic	$171.6 million
Export	$19.2 million

Any 2017 funds retained or underspent will be tracked in the FVDA and reported on in the IESO's next Revenue Requirement Submission. As stated earlier, any retained funds will be used to minimize fee increases related to the Market Renewal Program in 2018. As shown in Table 2 below, the projected operating costs for the Market Renewal Program are forecast to increase in 2018 over 2017 costs:

Table 2: Market Renewal forecast operating costs

	2016	**2017**	**2018**	**2019**
Market Renewal ($ millions)	$0	$12	$14	$6

The $5 million the IESO is proposing to retain represents approximately 3% of the IESO's 2017 revenue requirement and if returned to customers would be less than $0.0001/KWh as shown in Table 3 below, which is substantially lower than the $0.001/KWh threshold the OEB has set for the clearance of LDCs Group 1 audited account balances[1]. Additionally, while the Board's filing requirements place the onus on LDCs as to why any account balance in excess of the threshold should not be

[1] Ontario Energy Board, Filing Requirements For Electricity Distribution Rate Applications - 2016 Edition for 2017 Rate Applications - Chapter 3, Incentive Rate-Setting Applications, Pg 10 http://www.ontarioenergyboard.ca/oeb/_Documents/2017EDR/OEB_Filing_Requirements_2017Rates_Chapter03.pdf

disposed, there does not appear to be any provision for an LDC to clear the accounts when the balance is lower than the threshold.

Table 3: $5 million represented as IESO usage fee/KWh

	Proposed usage Fee/KWh	3% of the proposed fee/KWh
Domestic	$ 0.001220	$ 0.00003660
Export	$ 0.000990	$ 0.00002970

The IESO recognizes that this request is unusual. However, as described in Section B-1-1, in the IESO's approved 2017-2019 Business Plan and on the IESO's website, the Market Renewal Program is a multi-year project benefitting all customers with a net efficiency benefit of up to $3.5 billion from 2021 to 2030, including $3.0 billion net consumer benefit, as explained below. Given the long term benefits that are forecast to result from the Market Renewal Program, the IESO believes it is efficient and fair to customers to retain funds received in 2017 in order to minimize rate increases in 2018. As the IESO is proposing that a finite amount of any excess revenues collected or any underspend in one year be used to minimize an increase in usage fees in only the following year, the IESO believes that this proposal does not represent rate inequity and will not create subsidization between customer classes.

Expected Benefit of the Market Renewal Program

In a February 1, 2017 presentation to the IESO's SAC, (available at www.ieso.ca/-/media/files/ieso/document.../sac-20160201-market-renewal.pdf?la=en) some of the initial findings on the projected benefits of Market Renewal were :

- $3.5 billion net efficiency benefit (2021-2030) including $3.0 billion net consumer benefit

- The majority of the net benefits ($3.0 B) will flow to consumers but other market participants will be better off as well ($500 M)

On March 6th, 2017, a report prepared by the Brattle Group titled "The Future of Ontario's Electricity Market, A Benefits Case Assessment of the Market Renewal Program" was shared and posted on the IESO's website. With the publication of this report, as had been discussed with the IESO's SAC, the IESO began transition to Market Renewal design work. [2]

In the report, the Brattle group described some of the project benefits that will result from the Market Renewal Program as:

> … quantifiable impacts of Market Renewal's energy, operability, and capacity reforms would yield expected gross efficiency benefits of hundreds of millions of dollars per year. Furthermore, the benefits of Market Renewal would pay back its implementation cost in just over a year. Benefits would continue to increase and accrue in subsequent years.

> And

> For any given market participant the impact of Market Renewal will not be just a proportional share of the societal efficiency gains, but a combined effect of efficiency gains, positive revenue impacts that favor more economically competitive resources, negative net revenue impacts that disfavor less valuable resources, and changes in wealth transfers. It is outside the scope of this study to

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[2] The report is available at http://www.ieso.ca/sitecore/content/ieso/home/sector-participants/engagement-initiatives/engagements/market-renewal See March 6, 2017 Draft Agenda Minutes, and click on Market Renewal Draft Benefits Case Report

estimate the net effects of these changes on individual classes of market participants, but we are able to comment on likely high-level impacts for customers and other market participants.[3]

Capital Expenses

The IESO is seeking approval of its proposed 2017 capital expenditure envelope of $25 million for capital projects. A summary of capital spending and associated project descriptions is included in Appendix 4 of the IESO's approved 2017 – 2019 Business Plan and the forecast 2017 capital envelope compared to 2015 and 2016 is shown in Table 4 below:

Table 4: 2017 Capital Envelope compared to 2015 and 2016

Planned Projects ($ Millions)	2015	2016	2017
Total Capital Projects	29.4	28.4	23.4

The IESO utilizes the four strategic goals described in its 2016 – 202 Strategic Plan, which is available at http://www.ieso.ca/sector-participants/ieso-news/2016/06/ieso-releases-its-2016-2020-strategic-plan, to determine capital project priorities. The IESO's four strategic goals are:

- Deliver superior reliability performance in a changing environment
- Drive to a more efficient and sustainable marketplace
- Be recognized as a trusted advisor, informed by engagement

[3] **The Future of Ontario's Electricity Market,** A Benefits Case Assessment of the Market Renewal Program. March 3, 2017. Prepared by the Brattle Group. Pgs 95 & 102

- Invest in our people and processes to meet the needs of the sector

Accounting Change

The IESO has made changes to its accounting policies to increase transparency and to report certain costs as regulated assets, consistent with the accounting policies of other regulated entities in North America. These changes are reflected in Note 3 on page 13 of the IESO's 2016 Annual Report, which is filed with this application as Exhibit A-3-1. The changes include the recognition of rate regulated assets as well as the recognition of market accounts assets and liabilities on the statement of financial positions.

The IESO operates and settles the electricity market, where sums of money are constantly flowing to and from market participants, such as consumers and generators. The IESO is not party to these market transactions but facilitates them, which requires it to temporarily hold and move funds. These financial transactions in no way impact the IESO's accumulated deficit or revenues and expenses. After a review of its accounting practices, the IESO decided to include year-end market account balances on its financial statements in an effort to increase transparency.

Additionally, the IESO has changed its accounting policy to report certain costs as regulated assets, specifically unrecovered smart metering expenses and unrecovered PSAB transition items, to be consistent with the accounting policies of other regulated entities in North America. These are costs that are being recovered through Board approved fees and it is common practice among regulated entities to treat such costs as regulatory assets for accounting purposes. It`s important to note that no matter which way you report these costs, the cost and the impact on ratepayers does not change. These costs have been in the IESO's publicly issued audited financial statements for years and the decision to move to the new accounting policy was made to better reflect the nature of these costs. The reporting of these costs has always been public and the new reporting is simply a function of change in accounting policy.