Memorandum

Independent Electricity System Operator
1600-120 Adelaide Street West
Toronto, ON M5H 1T1
t 416.967.7474
www.ieso.ca

To: THE AUDIT COMMITTEE OF THE BOARD
of the Independent Electricity System Operator

From: Susan Nicholson
Corporate Controller

Date: August 29, 2017

Re: Q2 Statutory Statements and Market Accounts with Fair Hydro Plan Impacts

The recognition of the market accounts assets and liabilities on the statement of financial position were effective for 2016 and the accounts have been included in detail in the notes for the second quarter statutory statements. These statements and notes will be published on our internet site on August 31, 2017. These statements and notes have been appended for your information. In addition, there is a detailed description of each of the accounts attached.

The introduction of the Fair Hydro Plan (FHP) results in a number of changes to the market accounts. The accounting for these changes is already underway as some of these program changes were effective on May 1, 2017 and therefore are reflected in these second quarter results.

The changes to the Rate Regulated Plan (RPP) or Global Adjustment smoothing are by far the largest changes to our accounting but the FHP will also change the Rural or Remote electricity Rate Protection (RRRP) program to provide distribution charge relief for the customers of the costliest LDCs. It will enhance the Ontario Electricity Support Program (OESP) and work to ensure the program uptake is as close as possible to 100%. And it will establish a new First Nations On-Reserve Delivery Credit.

The changes to the OESP are designed to expand eligibility and increase credits to cover more low income Ontarians and became effective May 1, 2017. Although the OESP will eventually be funded by the provincial revenues, the initial funding from the IESO will come from the OESP variance account in the market books. The balance in the variance account was a liability $97.2 million as of June 30, 2017 ($110.9 million as of March 31, 2017).

The changes to the RRRP will split the current program into three programs, two of which will be paid by provincial revenues and the third will be paid through a new RRRP rate. The new RRRP rate was effective on July 1, 2017. The variance account for RRRP will continue but only for the portion of the program that is financed through the rate set by the Ontario Energy Board (OEB). The portion that will be paid through provincial revenues will be settled in same invoicing period and therefore will not impact the variance account. The balance in the variance account was an asset of $6.6 million as of June 30, 2017 (liability of $2.7 million as of March 31, 2017).

The First Nations On-Reserve Delivery Credit is part of the vulnerable consumer programs and started on July 1. The program will be paid through provincial revenue and settled in the same invoicing period resulting in no new variance account on the IESO market books.

Although a reduced RPP rate was introduced on May 1, 2017, the actual changes for the RPP or Global Adjustment smoothing program were effective on July 1, 2017, as per the OEB's Decision and Order dated June 22, 2017.

The account entitled Regulated Price Plan Variance will be renamed to Unrecovered Global Adjustment Expenses as of July 1st to reflect the regulated asset nature of the account. This aligns with the two regulated assets which were established in 2016; namely, Unrecovered Smart Metering Expenses and Unrecovered PSAB Transition Items.

Discussions to date with KPMG indicate that there will be very little change to the audited financial statements and notes from those prepared in 2016. The notes for market accounts will include a description of the Fair Hydro Plan impacts with specific language on the Unrecovered Global Adjustment Expenses account. It is anticipated that note will read something like:

``The unrecovered global adjustment expenses result from the implementation of the Ontario Fair Hydro Plan and by their nature is a regulated asset. For the year ended 2017, the total amount of the variance collected from the market is $... million, the amount of interest and expenses is $...million and the financing entity has purchased $...million of the regulated asset. ``

Lastly, global adjustment continues to be a significant portion of the market invoices. Attached for your information is an excerpt taken from the June Monthly Market Report. Finance and Corporate Relations are investigating different options for ensuring market information is transparent and available to our stakeholders as appropriate.

Regards,

Susan Nicholson