



# 2010 ANNUAL REPORT



Power to Ontario. On Demand.





## CONTENTS

1	Letter to the Minister of Energy	17	Statement of Operations, Loss and Accumulated Deficit
3	Message from the Chair	18	Statement of Financial Position
4	Setting the Stage for an Ongoing Industry Evolution	19	Statement of Cash Flows
15	Management Report	20	Notes to Financial Statements
16	Independent Auditors' Report	31	Executive Compensation at the IESO

# LETTER TO THE MINISTER OF ENERGY

I am pleased to submit the 2010 Annual Report of the Independent Electricity System Operator (IESO).

This report outlines the IESO's key achievements in 2010, with specific emphasis on some of the individual successes that contributed to maintaining the reliability of Ontario's power system.

This past year has challenged the IESO – and the industry as a whole – to accept, embrace and encourage change. The need for change is already permeating every aspect of our market and system operations, and will influence our strategic direction in the months and years to come.

In our capacity as system operator, the IESO plays a vital enabling role – a role that will grow substantially in magnitude as new players enter the market. Over the past 12 months, the IESO has focused on maintaining reliability, preparing for future operations,

efficiently managing the business, and effectively contributing to the development and implementation of government policy, particularly the *Green Energy and Green Economy Act, 2009* (GEGEA) and the Long-Term Energy Plan (LTEP).

By finding efficiencies, engaging in prudent spending and remaining focused on cost management, the IESO continued to demonstrate financial leadership. Despite substantial growth in GEGEA-related work volumes, the IESO kept its fee unchanged for the second consecutive year and finished the year with a surplus. In fact, the 2010 usage fee of \$0.822 per megawatt hour is almost 14 per cent lower than the rate charged in 2003.

With a proven focus on operational efficiency, the IESO remains committed to working with market participants, industry stakeholders and government agencies to ensure the long-term reliability of Ontario's power system.



Paul Murphy  
President and Chief Executive Officer





## MESSAGE FROM THE CHAIR

From my vantage point as a recent appointee to the position of Chair, I have the unique privilege to view Ontario's electricity sector from a different perspective. And what I've seen to date has filled me with a keen anticipation of what lies ahead.

Ontario's power system is undergoing the most significant transformation in its history. The changes underway are challenging every aspect of the industry – generation, transmission, distribution, regulation and even consumption – to evolve.

This is an exciting time to be in the electricity business, as several distinct waves of transformation are converging to reshape the landscape. The IESO plays a critical role in coordinating all the moving parts, ensuring Ontario's electricity market and system are run effectively, efficiently and reliably.

The increasing investment in new renewable generation is being accompanied by the expansion and renewal of Ontario's transmission and distribution systems, the retirement of the province's coal-fired generating fleet, the development of a smart grid, and the introduction of new tools to allow consumers to better monitor and manage their energy use. The challenge going forward will be to efficiently integrate this new infrastructure into the operation of Ontario's power system without compromising reliability.

In the short time that has elapsed since I assumed my role, I've seen the IESO's demonstrated leadership in all aspects of its operations. As the industry pulls together to navigate the changes ahead, I look forward to working through the challenges with the IESO's Board, senior management team, employees and key stakeholders.

Tim O'Neill  
Chair

# SETTING THE STAGE FOR AN ONGOING INDUSTRY EVOLUTION

Ontario's power system is undergoing the most sweeping transformation in its century-long history, fundamentally changing the way electricity is generated, delivered, managed and even consumed in the province. At the heart of this evolution are a supply mix being reinvented, transmission and distribution systems being expanded and modernized, and consumers being enabled to manage when and how they use electricity.

Implementation of the Government of Ontario's *Green Energy and Green Economy Act, 2009* (GEGEA) is driving a broad and comprehensive change in the resources required to meet Ontario's demand for electricity, with an increasing commitment to green generation – predominantly wind, solar, biomass and small-scale hydroelectric projects.

“ On integrating our projects they get an A+ ” GENERATOR

On the heels of the GEGEA, Ontario's Long-Term Energy Plan (LTEP) has reinforced the investment focus on renewable generation. Data from the Ontario Power Authority (OPA) suggest some 5,800 MW of variable generation projects, primarily wind, are now underway

and expected to be in commercial operation by the end of 2012, with 10,700 MW targeted for 2018.

Within the next two years, the IESO needs to be in a position to register and incorporate this variable generation into our operations. To meet this challenge, and maximize the benefits of Ontario's investment in new supply, the IESO is adapting power system operations and the IESO-administered markets to integrate these new resources, whose operating characteristics are significantly different from traditional nuclear, fossil and hydroelectric resources.

Already in 2010 the IESO was laying the foundation for the increased penetration of variable generation by refining its operating tools, processes and protocols. At the same time, the company was confronting the challenge of maintaining reliability in the face of a workforce in transition. Like most organizations in North America's electricity sector, the IESO's labour force is changing as skilled, experienced workers retire, opening the door to talented young people who have strong academic credentials but are new to the sector. Despite these and other challenges, the IESO achieved considerable success in 2010, setting the stage for the ongoing evolution of the industry while demonstrating an enduring commitment to operational reliability and financial prudence.

## Integrating Renewable Generation

In preparation for the expected influx of connection assessment requests associated with the launch of the OPA's landmark Feed-in Tariff (FIT) program, the IESO undertook process changes, enhanced system tools, and amended working protocols with market participants. That preparatory work yielded a significant efficiency increase. In previous years, connection assessments averaged 180 days. Working with Hydro One and local distribution companies (LDCs), the IESO found ways to trim the process substantially. While the company is now subject to a mandated service guarantee of 150 days for the completion of a connection assessment, all assessments performed in 2010 were well within the prescribed limit, coming in at 145 days or less.

### RENEWABLES INTEGRATION INITIATIVE

The IESO launched its Renewables Integration (RI) Initiative in 2010 in an effort to provide the necessary structure

and rigour required to effectively accommodate this new variable generation. After months of research, analysis and discussion, the Design Principles underpinning the project were released in early December 2010.

The principles fall into three main areas – forecasting, visibility and dispatch. The RI Initiative has been broken down into five related projects: centralized forecasting, real-time integration, control room visibility enhancements, operational support integration and future markets for renewables.

Given the breadth and scope of its expected impacts, this initiative will reach into all corners of Ontario's electricity industry. LDCs, generators of all types (particularly wind and solar), energy agencies, employees in the electricity industry, and consumers have already expressed an interest in the discussion paper and the policies, standards and market rule changes that will follow.





## Connecting with Consumers

### OUTREACH PROGRAM

The IESO's outreach program was very successful in 2010, helping to position the IESO as a leader in the electricity sector. Interaction with customers, stakeholders, opinion leaders and end-use consumers is essential to engage audiences in IESO initiatives and electricity sector issues. The broad objectives of the outreach program include:

- Strengthening and enhancing key relationships
- Achieving broader recognition of the roles and responsibilities of the various agencies operating in Ontario's electricity sector
- Helping end-use consumers – industrial, commercial, institutional and residential – understand the changes underway in the electricity sector
- Providing these end-use consumers with the information and tools they require to more actively manage their electricity consumption
- Engaging in targeted communications efforts with market participants, industry stakeholders, government, media, trade and business associations, and designated consumer groups to drive awareness of – and support for – the IESO's efforts to evolve the market

Outreach activities for the year included speeches and presentations; meetings and site visits; conferences and trade shows; and other activities requiring direct interaction with identified target audiences, including online tools, print publications and hosted workshops.

### TIME-OF-USE RATES AT WORK

Mid-way through the year the IESO introduced Time-of-Use Rates at Work. This online tool is designed to help small business owners understand time-of-use (TOU) electricity rates and identify potential savings opportunities resulting from load shifting and/or conservation efforts. By seeing exactly how they consume energy in their business operations, users are in a much better position to manage their costs. By inputting some basic information about their type of business, equipment and hours of operation, users build a tailored load profile. Page by page, the profile builds, allowing users to see the impact each piece of equipment has on their monthly electricity consumption. Once a full profile has been built, the tool identifies simple, relatively low cost savings opportunities. The final screen includes a "before and after" view that captures the potential impacts of users' conservation efforts.



10 Smart Meter Lane and Time-of-Use Rates at Work are two interactive tools that encourage users to learn more about electricity consumption, time-of-use prices and conservation opportunities.

## 10 SMART METER LANE

Time-of-Use Rates at Work builds on the foundation of 10 Smart Meter Lane, another online tool developed by the IESO and designed to help residential consumers understand dynamic pricing and the impact of running appliances at different times of the day. By year-end, more than 135,000 visitors had used 10 Smart Meter Lane – representing roughly 10 per cent of all customers on TOU rates – where they spent an average of four minutes learning how to use TOU rates to their advantage. Both initiatives are part of the IESO’s market education work, which is intended to foster the emergence of a more engaged, informed, energy-aware consumer.

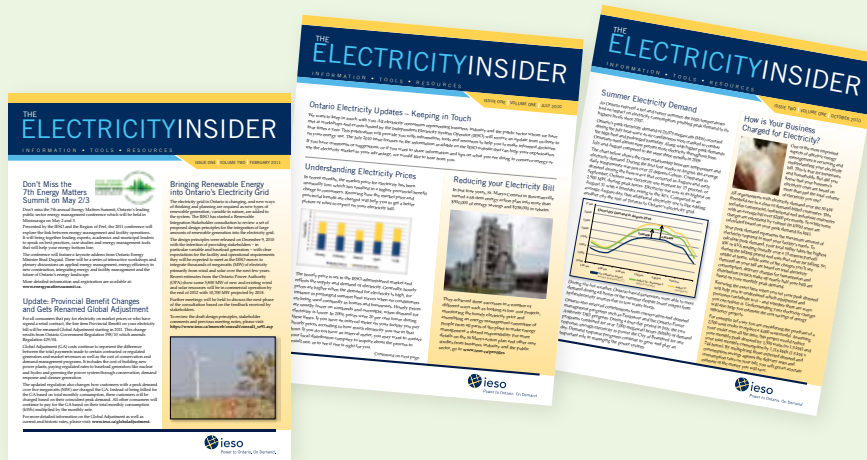
## MARKET EDUCATION

Other market education successes for 2010 include partnership with the Region of Peel on the Energy Matters Summit, Ontario’s leading public sector energy conference; presentation of nine energy management workshops – four with the long-term care sector, three with the hospital sector and two with the hotel sector; partnership with the Centre for Environmental Sustainability in Healthcare, a not-for-profit organization seeking to improve environmental performance in Ontario’s healthcare sector through energy conservation; participation in several trade shows and conferences in different industry sectors to educate end-use customers about electricity pricing, conservation programs and energy management; co-hosting seven Consumer Forum events with LDCs in Sarnia, Kitchener-Waterloo-

Cambridge, Cobourg, North Bay, Ottawa, Woodstock and Niagara; and creation of an informative new quarterly publication known as *The Electricity Insider*, aimed at small and mid-sized industrial, commercial and institutional electricity consumers.

# REDEFINING THE ROLE OF CONSUMERS

Electricity consumers are starting to play an increasingly important role in the management of Ontario’s power system. Building on this momentum, the IESO selected two companies in June 2010 to participate in an innovative project that would allow large industrial, commercial and institutional electricity users to provide a grid-balancing service usually supplied by generators. Regulation service acts to match total system generation to total system demand on a second-by-second basis. By helping to correct variations in power system frequency, it reinforces the stability and reliability of the power system. Once launched, the Alternative Technologies for Regulation Demonstration Project will test new ways to provide regulation service to Ontario’s electricity market and determine if consumers can provide some of the ancillary services we require, eventually resulting in greater competition, flexibility and reliability.



The *Electricity Insider* provides small and mid-sized industrial, commercial and institutional electricity consumers with useful, easy-to-implement tips on energy management.

The IESO also revamped its key customer outreach strategy in 2010. Results seen during the year include:

- Increased customer confidence in the IESO's ability to resolve their issues
- Increased engagement and information sharing with the solar and biogas industries
- Increased awareness and interest in IESO operations among LDCs
- Enhanced engagement with non-traditional customer groups by targeting industry associations

**“ Well done. (*The Electricity Insider*) is a good resource for companies to use. ”**

ENERGY CONSULTANT

The year 2010 also marked the launch of the IESO's social media strategy, which represents a significant step forward for the organization. The rising popularity of social media has changed how people share and consume information. With this in mind, the IESO has incorporated social media into its communications toolkit to help the company reach a wider Ontario audience. Social media is already helping the IESO promote electricity literacy among consumers, raise awareness about the changes that are taking place within the system, and profile the IESO's critical responsibilities in Ontario's electricity sector.

The Electricity Outlet on Facebook is intended for the general electricity user and is an information hub for a wide range of electricity news, discussions, widgets and photos of interest and educational value. The IESO's Twitter account is aimed toward a more involved electricity consumer and provides a behind-the-scenes

look and commentary about IESO activities. By providing engaged electricity consumers and participants with information at the source, the IESO is starting to build a trusted Twitter following. During significant system events – such as the Manby transformer fire – the IESO used both traditional media outlets and social media channels to share essential information with journalists as well as the general public.

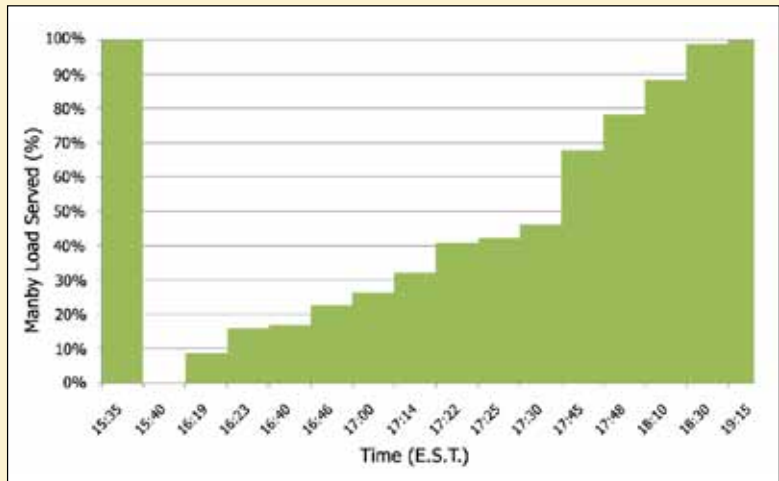
## PREPARING FOR THE G20 SUMMIT

In 2009, the federal government announced the 2010 G20 Summit would be held in Toronto on June 26-27, immediately following the G8 Summit in Huntsville. With the eyes of the world trained on Toronto, a secure, reliable and continuous supply of electricity was essential. A G20 Planning Team, led by the IESO, was struck six months before the Summit. With representation from key stakeholders – including Hydro One, Toronto Hydro, the Portlands Energy Centre and the Ministry of Energy – the team developed a detailed, comprehensive, integrated plan to ensure the resilience of electricity supply before and during the Summit. The plan comprised equipment testing, inspection and maintenance; outage management; security and staffing needs; assessment of potential contingencies and associated mitigation plans; and other areas. Working closely with federal, provincial and municipal law enforcement agencies, the team focused on processes and protocols with respect to information sharing, risk management and emergency response. While protests took place during the Summit, everything went smoothly and seamlessly from an electricity supply perspective.

# RESTORING THE BALANCE BETWEEN SUPPLY AND DEMAND

Just one degree shy of an all-time record for that day in Toronto's history, it was 34 degrees Celsius on the afternoon of July 5, 2010 when air conditioners in the city stopped humming. A 230 kV oil-filled breaker at the Manby Transformer Station had exploded, spraying oil and debris across the yard, triggering a power surge as far away as Michigan and New York, and leaving nearly 250,000 customers without power. IESO control room operators took immediate action, manually dispatching generation and reactive resources to reduce the Area Control Error (ACE) to zero, and returning system voltages to normal ranges within 12 minutes. By receiving the sudden surge of power as a result of the loss of load, Ontario's interconnections with neighbouring jurisdictions played an important role in limiting the impacts of the outage, allowing IESO operators to restore the delicate balance between supply and demand. As Hydro One proceeded with the inspections and repairs on the faulted equipment, IESO operators directed load

transfers to alternate supply points and gradually power was restored to pockets of the city. Effective communication and cooperation among all the involved companies ensured service was restored to all customers in 3.5 hours or less.



The IESO took a phased approach to restoration after a breaker explosion at the Manby Transformer Station triggered a major outage in the western GTA on July 5, 2010. Total load restoration was completed in 3.5 hours or less.

## Harnessing Innovation to Find Efficiencies

The IESO made considerable progress on the multi-year On-Line Limit Derivation (OLLD) project, which has already begun to yield significant productivity gains and market efficiencies by changing how the IESO develops and uses operating limits to manage grid operating security. These limits, or parameters, determine the maximum power flow through a particular point on the grid, thereby ensuring the reliable operation of Ontario's power system.

### BRUCE READINESS PROGRAM

A willingness to do things differently has translated into substantial savings, which stem, in part, from automating certain processes that typically required considerable human intervention and analysis. The Bruce Readiness Program, the second stage of the OLLD project, was an important milestone in the IESO's ongoing efforts to modernize the management of Ontario's power system. By taking a fresh and innovative approach to conventional engineering theory, and by tapping into employees' creativity and resourcefulness, the company has identified ways to improve operations and alleviate congestion.

The Bruce Readiness Program involved changes in three main areas – people, processes and tools – and the work completed in 2010 will underpin the next phases of the OLLD project. There were numerous benefits stemming from the project in 2010:

- Substantially increased energy transfers (approximately 500 MW higher than before)
- Reduced operating reserve requirements, reducing costs to energy consumers
- Increased coincidence of critical element outages, which facilitates more efficient maintenance and capital work programs by generators and transmitters
- Total market savings in excess of \$2 million per year
- Mitigation of the need to hire four additional staff

### ENHANCED DAY-AHEAD COMMITMENT

Considerable progress was made in 2010 on another major IESO initiative: the Enhanced Day-Ahead Commitment (EDAC) project, which is designed to enhance the efficiency of the electricity market through the advanced

scheduling and commitment of generation resources required to provide electricity on a daily basis. At the end of the year, the project team was in the later stages of the IT Design and Build stage, preparing for the transition into User Acceptance Testing and finally Market Trials with market participants – and, ultimately, on budget and on schedule for implementation in fall of 2011.

Implementation is expected to deliver benefits to the market in the following areas:

- The three-part offer and 24-hour optimization process will improve the efficiency of unit commitment decisions
- Resulting unit commitment will allow gas-fired generators to take actions with increased certainty, allowing for the purchase of gas supply in a more efficient manner and increased operating consistency
- Increased assurance that the reliability of Ontario's power system will be maintained

**“ I use (the IESO website) daily. I use the market tools – I'm in real-time operations – so I want to read the prices and capacity reports for the day on primary demand. The tools are working very well for me. It's one of the first things I look at each day. I can see what my competitors are doing too. ”** GENERATOR

## ENROLMENT AUTOMATION PROJECT

Another priority project, the customer-focused Enrolment Automation Project will provide a flexible and expandable central repository of customer information, replacing a number of stand-alone and outdated systems and providing a web-based interface for registration and connection assessments. The project consists of three main phases: Customer Information and Data Efficiency (CIDE), Registration Automation and Grid Assessments Automation.

The first stage, CIDE, was delivered on time and on budget at the end of 2010. It includes the master database for the data considered essential to market systems and will eventually replace the existing Participant Lifecycle (PLC) system – a web-based tool used for providing market participant information to the IESO that is near

## PANDEMIC PLANNING PAYS OFF

As the H1N1 influenza outbreak swept across the globe in 2009, the IESO updated and refined its pandemic plan. For its efforts, the company received the APEX Award for Pandemic Planning Excellence in the Small/Medium Organization category in June 2010. The APEX Awards are a national initiative created to recognize Canadian businesses for the creation, development and execution of a comprehensive pandemic preparedness program. Award submissions were judged against a broad range of criteria including pandemic core values; planning assumptions, policies, practices, and protocols; risk assessment; recovery objectives; information and communication; control activities; and monitoring practices. The IESO's central role within the province's energy sector required the company to minimize the risks associated with the H1N1 virus and develop strategies to ensure the reliable delivery of electricity, whatever the circumstances – and this award is testament to the industry's confidence in those strategies.

its end of life. The two subsequent stages will automate all aspects of the Registration and Connection Assessment processes for both proponents and the IESO, yielding improvements and efficiencies necessary for managing the renewable generation coming online. The project is expected to be completed by the end of 2012.

## IESO PORTAL UPGRADES

The IESO completed 44 key information technology projects in 2010. Among the projects with greatest impact are an upgrade to the IESO Portal and the replacement of the Operational Data Store (ODS). The portal upgrade provides market participants with a high availability platform for access to IESO applications such as the Transmission Rights Auction and, in 2011, the Market Participant Interface. The IESO also uses the Portal to host collaboration communities such as the Market Surveillance Panel and EDAC. The ODS is a source of data for many reports and the IESO website. The new ODS provides higher reliability and performance as well as a more flexible environment that can enable changes to the information displayed on the website.

# Reputation and Relationships

The IESO's technical capability supports planning and policy development by government and industry associations in Ontario and beyond. The IESO was heavily engaged on many fronts and contributed to a broad range of policy items. In 2010, for example, the technical support provided by the IESO to the OPA jumped by 89 per cent. This support included: transmission assessments; active participation in the FIT transmission availability test; consultation on planning standards; technical assessments and analysis for potential enabler transmission lines; engagement with non-traditional market participants lacking familiarity with the rules and processes governing Ontario's electricity industry; and advice on how to manage other potential transmission issues such as congestion.

## GLOBAL ADJUSTMENT

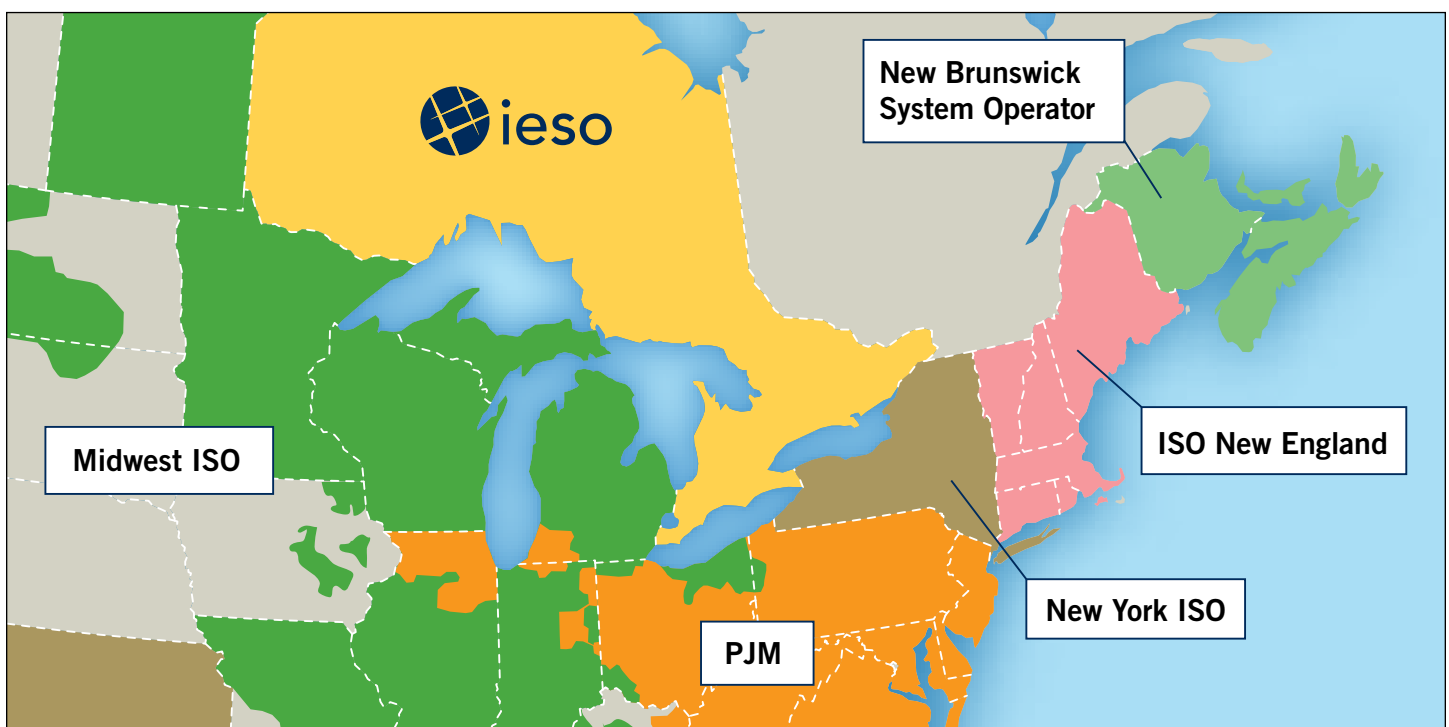
The IESO promoted the importance of wholesale market price signals for consumers through its involvement in the amendments to Ontario Reg. 429/04 relating to the allocation of the Global Adjustment (GA). This regulation directs an approach to GA cost recovery based on each affected customer's share of total demand during five peak system hours in a year. This new mechanism should restore the relevance of the market price (the Hourly Ontario Energy Price, or HOEP) to large consumers,

promoting efficient consumption decisions; encourage better utilization of Ontario's generation fleet by lowering the average unit cost of supply; reduce surplus baseload generation; and reward large consumers for reducing consumption at times when the grid is most strained.

## CROSS-BORDER COOPERATION

The IESO's role extends far beyond the borders of the province. The IESO, like other Reliability Coordinators in the North American electricity sector, is managing its reliability and compliance responsibilities in an increasingly complex and constantly evolving regulatory environment.

The IESO advocates and influences the development of reliability standards to ensure Ontario's interests are considered in the context of a broader, North America-wide interconnected electricity grid. The company is heavily involved in the working groups, committees and – in some cases – boards of organizations such as the North American Electric Reliability Corporation (NERC), the Northeast Power Coordinating Council (NPCC), the North American Energy Standards Board (NAESB), and the Independent System Operator/Regional Transmission Organization (ISO-RTO) Council, otherwise known as the IRC.



By working closely with neighbouring jurisdictions, the IESO is helping to ensure energy adequacy and security across North America.



By actively participating in various industry forums, the IESO coordinates with neighbouring regional entities on market and reliability matters to develop operational and planning standards. These reliability standards incorporate emerging technologies including renewable resources, storage technology, smart grid applications and demand response resources.

**“ They have a (stakeholder engagement process) that is viewed as a model by other jurisdictions. Other jurisdictions, other ISOs, have myopic views...relative to other jurisdictions, the IESO is second to none.”** LDC

In addition to providing regular guidance and feedback to these organizations, the IESO was also subject to a spot audit in 2010, which it passed without any qualifiers. NPCC conducted this audit, which assessed the IESO's compliance with 33 requirements of NERC standards. The NPCC audit found the IESO to be in full compliance with the audited requirements, which means not only had the IESO adequately developed and implemented the required processes, policies and procedures but it had also provided evidence that these policies and procedures are routinely applied in accordance with the requirements of the audited standards.

### **NERC COMPLIANCE TOOL**

2010 also saw the IESO develop a NERC Compliance Tool. This unique and innovative application provides the IESO with an effective tool for monitoring compliance, ensuring appropriate follow-up actions and prompt reporting to

all authorities concerned. Further it provides a means for IESO departments and market participants to better monitor their specific compliance reporting obligations with respect to reliability standards and their associated submission due dates, and provides a readily available history of submission data for audit purposes.

## **PRIVATE SECTOR INSIGHTS INTO SMART GRID PLANNING**

The overarching goal of a smart electricity grid is to use advanced information and communications technologies to increase grid efficiency, reliability and flexibility. Since its inception in 2008, the 14-member Ontario Smart Grid Forum has focused on defining how a smart grid in Ontario could deliver significant operational, environmental and consumer benefits. The forum has helped shape the direction and priorities for smart grid development in Ontario. In 2010, the forum created a Corporate Partners Committee to bring a private sector rigour and perspective to the forum's discussions by providing insights into what is needed, what is available, and what is affordable. Members of the committee reflect a cross-section of industry, including systems integration and consulting; distribution system components; communications networks; distributed generation; in-home applications; electric vehicles and related services; and advanced metering infrastructure. The committee is administratively supported by the Ontario Energy Association (OEA) on behalf of the forum.

# Smart Metering and Data Management

Considerable progress was made in 2010 on the Government of Ontario's Smart Metering Initiative, which saw the IESO tasked with procuring and managing the centralized Meter Data Management Repository (MDM/R) that handles all the data flowing from smart meters installed in residences and small businesses across Ontario.

When the year started, there were just eight LDCs integrated with the MDM/R and nearly 300,000 smart meters enrolled in the MDM/R. Over the course of 2010, however, the number of smart meters enrolled in the MDM/R grew by more than 800 per cent – and by year-end, there were more than 2 million smart meters enrolled in the system, representing nearly 50 per cent of the 4.5 million smart meters installed in the province.

## SMART METERING ENTITY

In its role as the Smart Metering Entity (SME), the IESO also introduced new tools and services to further enhance customer service and MDM/R support capabilities. The tools and services include an online MDM/R service desk to improve the incident response and reporting process,

a new website, and an online newsletter, *Toward Time-of-Use*, developed for LDCs and service agents working with the SME as they deploy smart meters, integrate them with the MDM/R, and implement time-of-use (TOU) billing.

Developing a meter data management system that meets the needs of Ontario consumers and nearly 80 utilities has been a unique challenge but the system now in place has become an important element of the province's electricity infrastructure. The efforts of the SME, LDCs and two of the world's leading smart grid vendors have led to the development of a meter data management system that will ultimately process hourly consumption data for all Ontario homes and small businesses – more than 4.7 million consumers – daily. The MDM/R will be processing an estimated 112 million transactions every day, which is just under the 130 million average daily transactions of Visa's VisaNet, the world's largest retail electronic payment processing network.

The costs associated with the delivery and operation of the MDM/R remain in line with the Ministry of Energy-approved budget of \$89 million.



The IESO provides training and support to employees of local distribution companies as the utilities implement smart meter programs and time-of-use prices.



## Financial Prudence in a Time of Change

The IESO has a proven track record when it comes to financial leadership. In recognition of the impact that difficult economic conditions had on customers and stakeholders, the IESO held its fee flat in 2010 by finding efficiencies and focusing on priorities, consistent with the

2009 organizational realignment. While demands on the business have continued to grow, the IESO kept its fee unchanged for the second consecutive year. In fact, the 2010 usage fee of \$0.822 per megawatt hour is almost 14 per cent lower than the rate charged in 2003.

## MEASURING SUCCESS

When it comes to a reliable supply of electricity, consumers have justifiably high standards. One standard indicator of power system reliability is the cumulative amount of load that is interrupted each year due to planned or unplanned outages – a metric known as unsupplied energy. The IESO assesses the overall performance of Ontario’s power system with respect to unsupplied energy, which is expressed in “system minutes” and represents the extent to which energy is not supplied to a customer (or group of customers) due to transmission outages. Consistent with benchmarks established with Ontario’s transmitters for comparison purposes, Ontario’s current limit of unsupplied energy is 15.75 system minutes. In 2010, however, unsupplied energy was very low, coming in at just 11.03 system minutes – a hallmark of the fundamental reliability of Ontario’s power system.

In 2010, the IESO was focused on maintaining reliability, preparing for future operations, efficiently managing the business, and effectively contributing to the development and implementation of government policy. Delivering on the expectations associated with the GEGEA has already added to the IESO’s work volumes, and will continue to do so in the coming years. However, by reviewing and revising existing processes, practices and tools, the IESO has achieved efficiencies across the organization, including in the areas of Settlements, Information Technology, Control Room Support, Market Information, Marketplace Training, Stakeholder Engagement, Market Entry and Finance, among others.

Despite the financial challenges, the IESO ended 2010 with a surplus of \$18.3 million resulting primarily from prudent spending and cost management, along with higher than planned export levels. As a result, the company has proposed to the Ontario Energy Board to issue a rebate to market participants of \$10.2 million, benefiting electricity consumers today while also leaving the IESO and the sector well-positioned for the future.

# MANAGEMENT REPORT

## Management's Responsibility for Financial Reporting

The accompanying financial statements of the Independent Electricity System Operator are the responsibility of management and have been prepared in accordance with accounting principles generally accepted in Canada. The significant accounting policies followed by the Independent Electricity System Operator are described in the Summary of Significant Accounting Policies contained in Note 2 in the financial statements. The preparation of financial statements necessarily involves the use of estimates based on management's judgment, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. The financial statements have been prepared within reasonable limits of materiality and in light of information available up to February 10, 2011.

Management maintained a system of internal controls designed to provide reasonable assurance that the assets were safeguarded and that reliable information was available on a timely basis. The system included formal policies and procedures and an organizational structure that provided for the appropriate delegation of authority and segregation of responsibilities.

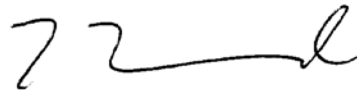
These financial statements have been examined by KPMG LLP, a firm of independent external auditors appointed by the Board of Directors. The external auditors' responsibility is to express their opinion on whether the financial statements are fairly presented in accordance with generally accepted accounting principles in Canada. The Auditors' Report, which follows, outlines the scope of their examination and their opinion.

## INDEPENDENT ELECTRICITY SYSTEM OPERATOR

On behalf of management,



Paul Murphy  
President and Chief Executive Officer  
Toronto, Canada  
February 10, 2011



Ted Leonard  
Vice President, Finance  
Chief Financial Officer and Treasurer  
Toronto, Canada  
February 10, 2011

# INDEPENDENT AUDITORS' REPORT

To the Board of Directors of the Independent Electricity System Operator (IESO):

We have audited the accompanying financial statements of IESO ("the Entity"), which comprise the statement of financial position as at December 31, 2010 and the statement of operations, loss and accumulated deficit, and the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

## Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

## Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform an audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of IESO as at December 31, 2010, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

## Other Matter

The financial statements of the Entity as at and for the year ended December 31, 2009 were audited by another auditor who expressed an unmodified opinion on those statements on February 11, 2010.



KPMG LLP, Chartered Accountants, Licensed Public Accountants  
February 10, 2011  
Waterloo, Canada

# STATEMENT OF OPERATIONS, LOSS AND ACCUMULATED DEFICIT

For the Year Ended December 31 (in thousands of Canadian dollars)	2010 \$	2009 €
<b>REVENUES</b>		
System fees (Note 11)	116,890	119,988
Other revenue (Note 2b)	2,963	1,511
<b>TOTAL REVENUES</b>	<b>119,853</b>	<b>121,499</b>
<b>EXPENSES</b>		
Labour	76,738	74,036
Computer services, support and equipment	8,051	9,275
Contract services and consultants	5,845	6,860
Telecommunications	2,675	2,936
Other costs	6,484	7,255
Smart metering program costs (Note 11)	13,665	9,962
Amortization	15,654	24,319
<b>TOTAL EXPENSES</b>	<b>129,112</b>	<b>134,643</b>
<b>Income/(loss) before interest, financing charges and investment income</b>	<b>(9,259)</b>	<b>(13,144)</b>
Interest and investment income/(loss)	2,378	2,304
Interest expense and financing charges	(1,073)	(3,074)
<b>NET LOSS FOR THE YEAR</b>	<b>(7,954)</b>	<b>(13,914)</b>
<b>ACCUMULATED DEFICIT - BEGINNING OF YEAR</b>	<b>(19,525)</b>	<b>(5,611)</b>
<b>ACCUMULATED DEFICIT - END OF YEAR (Note 11)</b>	<b>(27,479)</b>	<b>(19,525)</b>

See accompanying notes to financial statements.

# STATEMENT OF FINANCIAL POSITION

As at December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	8,609	8,990
Accounts receivable	15,755	13,500
Prepaid expenses	3,769	3,693
	<b>28,133</b>	<b>26,183</b>
<b>Property and equipment (Note 4)</b>		
In service	66,436	74,856
Construction-in-progress	15,262	4,882
	<b>81,698</b>	<b>79,738</b>
<b>Other assets</b>		
Intangible assets (Note 5)	6,844	6,685
Long-term investments (Note 6)	21,816	18,204
Prepaid pension cost (Note 7)	3,073	3,349
	<b>31,733</b>	<b>28,238</b>
<b>TOTAL ASSETS</b>	<b>141,564</b>	<b>134,159</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (Note 8)	22,090	20,073
Accrued interest on debt	161	66
Short-term debt (Note 9)	2,000	-
Current portion long-term debt (Note 9)	78,200	-
Rebates to market participants (Note 11)	10,193	4,324
	<b>112,644</b>	<b>24,463</b>
<b>Long-term liabilities</b>		
Long-term debt (Note 9)	-	78,200
Accrual for employee future benefits other than pensions (Note 7)	56,399	51,021
	<b>56,399</b>	<b>129,221</b>
<b>TOTAL LIABILITIES</b>	<b>169,043</b>	<b>153,684</b>
<b>TOTAL ACCUMULATED DEFICIT (Note 11)</b>	<b>(27,479)</b>	<b>(19,525)</b>
<b>TOTAL LIABILITIES AND ACCUMULATED DEFICIT</b>	<b>141,564</b>	<b>134,159</b>

**Commitments and contingencies (Note 14)**

See accompanying notes to financial statements.

On behalf of the Board:



Tim O'Neill  
Chair  
Toronto, Canada



William Museler  
Director  
Toronto, Canada

# STATEMENT OF CASH FLOWS

For the Year Ended December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
<b>OPERATING ACTIVITIES</b>		
Net loss for the year	(7,954)	(13,914)
Adjustments for non-cash items:		
Amortization	15,654	24,319
Pension cost	15,692	12,524
Other employee future benefits cost	7,147	6,240
Change in fair value of long-term investments held-for-trading	(1,060)	(1,218)
	<b>29,479</b>	<b>27,951</b>
Changes in non-cash balances related to operations:		
Change in accounts payable and accrued liabilities	1,658	(1,760)
Change in rebates to market participants	5,869	2,938
Change in accounts receivable	(2,255)	275
Change in prepaid expenses	(76)	265
	<b>5,196</b>	<b>1,718</b>
Other:		
Contribution to pension fund	(15,416)	(17,712)
Payment of employee future benefits	(1,769)	(1,735)
	<b>(17,185)</b>	<b>(19,447)</b>
<b>Cash provided by operating activities</b>	<b>17,490</b>	<b>10,222</b>
<b>INVESTING ACTIVITIES</b>		
Net purchase of long-term investments	(2,552)	(2,014)
Investment in property and equipment	(14,528)	(8,975)
Investment in intangible assets	(2,791)	(2,934)
<b>Cash used in investing activities</b>	<b>(19,871)</b>	<b>(13,923)</b>
<b>FINANCING ACTIVITIES</b>		
Proceeds from short-term debt	2,000	-
<b>Cash provided by financing activities</b>	<b>2,000</b>	<b>-</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(381)</b>	<b>(3,701)</b>
<b>CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR</b>	<b>8,990</b>	<b>12,691</b>
<b>CASH AND CASH EQUIVALENTS - END OF YEAR</b>	<b>8,609</b>	<b>8,990</b>

See accompanying notes to financial statements.

**Supplementary Information:**  
(in thousands of Canadian dollars)

<b>Interest paid</b>	<b>532</b>	<b>3,279</b>
----------------------	------------	--------------

# NOTES TO FINANCIAL STATEMENTS

## 1. NATURE OF OPERATIONS

Independent Electricity System Operator (IESO) is a not-for-profit, non-taxable corporation, created by statute effective on April 1, 1999 pursuant to Part II of the *Electricity Act, 1998*. As set out in the *Electricity Act, 1998*, the IESO operates pursuant to a licence granted by the Ontario Energy Board (OEB). The objects of the IESO as contained in the *Electricity Act, 1998* and amended, in the *Electricity Restructuring Act, 2004* and Ontario Regulation 452/06, are as follows:

- to exercise the powers and perform the duties assigned to the IESO under the *Electricity Restructuring Act, 2004*, the market rules and its licence;
- to enter into agreements with transmitters giving the IESO the 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 the *Electricity Restructuring Act, 2004*;
- to participate in the development, by any standards authority, of standards and criteria relating to the reliability of the transmission systems;
- to work with the responsible authorities outside Ontario to co-ordinate the IESO's activities with their activities;
- to collect and provide information to the Ontario Power Authority (OPA) and the public relating to the current and short-term electricity needs of Ontario and the adequacy and reliability of the integrated power system to meet those needs;
- to operate the IESO-administered markets to promote the purposes of the *Electricity Restructuring Act, 2004*;
- to plan, manage and implement the smart metering initiative or any aspect of the initiative;
- to oversee, administer and deliver the smart metering initiative or any aspect of the initiative; and
- to establish and enforce standards and criteria relating to the reliability of transmission systems.

The IESO was designated the Smart Metering Entity 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, the OPA 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.

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 accounting principles generally accepted in Canada.

### 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 exports. System fees are recognized as revenue at the time the electricity is withdrawn. Rebates are recognized in the year in which the approved regulatory deferral account, before such rebates, exceeds regulated limits.

These financial statements do not include the financial transactions of market participants within the IESO-administered markets.

Other revenue represents amounts that accrue to the IESO relating to services the IESO performs and charges on a recovery basis, investment income on funds passing through market settlement accounts, as well as fines and penalties. Such revenue is recognized as it accrues.

### c) Financial instruments

#### CLASSIFICATION

- The IESO classified its cash and cash equivalents as “held for trading”. In addition, the IESO designated its investment portfolio as being “held for trading” and classified its accounts receivable as “loans and receivables”.
- Cash and cash equivalents comprise cash, term deposits and other short-term, highly-rated investments with original maturity dates of less than 90 days.
- Accounts payable and debt have been classified as other financial liabilities.

#### RECOGNITION AND MEASUREMENT

- Held for trading investments are recorded at fair value with gains and losses recorded in the statement of operations. Transactions are recorded based on trade dates. Transaction costs are charged to operations as incurred.
- Loans and receivables are initially recorded at fair value and subsequently measured at amortized cost using the effective interest rate method.
- The IESO’s financial liabilities, comprising accounts payable and long-term debt are carried at amortized cost.
- Foreign currency exchange forward contracts are recorded at fair value. Where foreign currency exchange forward contracts meet the criteria for hedge accounting, changes in their values are reflected in accumulated surplus as other comprehensive income. Where such contracts do not meet the criteria for hedge accounting, changes in their value are recognized in the statement of operations.

### d) Construction-in-progress

Construction-in-progress 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 construction-in-progress are transferred to property and equipment in service or intangibles when the asset under construction is deemed to be ready for use.

### e) Property and equipment in service

Property and equipment are capitalized at cost, which comprises materials, labour, external support, overhead, and interest applicable to capital activities.

### f) Amortization

The capital cost of property and equipment and intangible 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 Service Life 2010	Estimated Average Service Life 2009
Facilities	38	38
Meter Data Management/Repository	11	6
Market Systems and Applications	5 to 11	5 to 9
Infrastructure and Other Assets	4 to 7	4 to 7
Intangible Assets	4	4

Gains and losses on sales of property and equipment are charged to operations. Losses on premature retirements for property and equipment and intangible assets are charged to operations.

The estimated service lives of property and equipment and intangible assets are subject to periodic review. The impacts of changes in the estimated lives are amortized on a prospective basis. The most recent review was completed in fiscal 2010.

### g) Intangible assets

Intangible assets are capitalized at cost, which comprises materials, labour, external support, and overhead, applicable to capital activities.

### h) Pension and other post-employment benefits

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 healthcare costs. The discount rate used to value liabilities is based on market rates 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 market-related values for equities (whereby fund assets are calculated using the smoothed value of assets over five years) and market values for fixed income securities, 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 amortization of plan amendments on a straight-line basis over the expected average remaining service life of the employees covered by the plan. 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. The excess, if any, of the cumulative unamortized net actuarial gain or loss over 10% of the greater of the projected benefit obligation and the market-related value of plan assets is also 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 and OPEB plans is 11 years (2009 - 11 years).

### i) 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. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated in Canadian dollars at the rate prevailing at that date. Exchange gains and losses arising on settlement of foreign exchange transactions are reported in the statement of operations at the date at which the transactions are settled.

### j) Use of estimates

The preparation of the financial statements in conformity with Canadian generally accepted accounting principles 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 which involve a greater degree of uncertainty include the carrying values of property and equipment and intangible assets, prepaid pension cost, rebates to market participants, and accrual for employee future benefits other than pensions. Actual results could differ from those estimates.

## 3. FUTURE CHANGE IN ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Part V of the Canadian Institute of Chartered Accountants Handbook (CICA Handbook). As of January 1, 2011, Part V of the CICA Handbook will cease to be a source of Generally Accepted Accounting Principles (GAAP) for the IESO. Accordingly, the IESO will be adopting Public Sector Accounting Board (PSAB) accounting standards as of that date.

## 4. PROPERTY AND EQUIPMENT

As at December 31 (in thousands of Canadian dollars)	2010			2009		
	Costs \$	Accumulated Amortization \$	Net Book Value \$	Costs \$	Accumulated Amortization \$	Net Book Value \$
<b>Property and equipment in service</b>						
Facilities	50,087	15,198	34,889	50,087	13,769	36,318
Meter Data Management/Repository	19,241	7,338	11,903	18,208	5,638	12,570
Market Systems and Applications	208,647	194,562	14,085	207,861	189,620	18,241
Infrastructure and Other Assets	77,284	71,725	5,559	75,178	67,451	7,727
	355,259	288,823	66,436	351,334	276,478	74,856
<b>Construction-in-progress</b>	15,262	-	15,262	4,882	-	4,882
	<b>370,521</b>	<b>288,823</b>	<b>81,698</b>	<b>356,216</b>	<b>276,478</b>	<b>79,738</b>

In 2010, the impact of adjustments to management's estimates of remaining asset service lives was a decrease in amortization expense of \$8,645,343 (2009 - \$390,533).

Interest capitalized to construction-in-progress during 2010 was \$73,197.

## 5. INTANGIBLE ASSETS

	As at December 31 (in thousands of Canadian dollars)					
	2010			2009		
	Costs	Accumulated Amortization	Net Book Value	Costs	Accumulated Amortization	Net Book Value
	\$	\$	\$	\$	\$	\$
Intangible Assets	38,092	32,930	5,162	34,205	29,620	4,585
Construction-in-progress	1,682	-	1,682	2,100	-	2,100
	<b>39,774</b>	<b>32,930</b>	<b>6,844</b>	<b>36,305</b>	<b>29,620</b>	<b>6,685</b>

In 2010, the impact of adjustments to management's estimates of remaining asset service lives was \$nil (2009 - \$13,043).

## 6. 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 \$21,816,000 (2009 - \$17,930,573). As at December 31, the market value allocation of these long-term investments was 60.8% equity securities and 39.2% debt securities (2009 - 60.9% and 39.1% respectively).

### BALANCED PORTFOLIO OF POOLED FUNDS

	As at December 31 (in thousands of Canadian dollars)	
	2010 \$	2009 \$
Opening Balance	17,931	14,502
Purchase of investments	2,825	2,014
Change in fair value	1,060	1,415
Closing balance	<b>21,816</b>	<b>17,931</b>

In its administration of the IESO-Administered Markets, the IESO directs the investment of market funds in highly-rated short-term investments, including previous investments in asset-backed commercial paper (ABCP), 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.

In September 2010, the IESO divested all ABCP holdings. The IESO did not recognize any investment income earned in the market settlement accounts in 2010 (2009 - \$nil).

## 7. 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

	2010 Pension Benefits	2009 Pension Benefits	2010 Other Benefits	2009 Other Benefits
(in thousands of Canadian Dollars)	\$	\$	\$	\$
Accrued benefit obligation	441,351	396,936	75,593	67,630
Fair value of plan assets	293,615	269,791	-	-
Funded status	(147,736)	(127,145)	(75,593)	(67,630)
Employer contribution after measurement date	2,066	2,264	466	467
Unamortized past service costs	1,625	2,323	99	172
Unamortized net actuarial loss	147,118	125,907	18,629	15,970
Prepaid (accrued) benefit cost recognized in the statement of financial position	3,073	3,349	(56,399)	(51,021)

Prepaid benefit cost in 2010 is shown net of a valuation allowance of \$nil.

## REGISTERED PENSION PLAN ASSETS

As at the measurement date of September 30, registered pension plan assets were split by fair value between the following categories:

	2010	2009
Canadian equity securities	21.4%	21.0%
Foreign equity securities	36.7%	39.8%
Canadian debt securities	41.4%	37.5%
Cash equivalents	0.5%	0.7%
Forward foreign exchange contracts	-	1.0%
	<b>100.0%</b>	<b>100.0%</b>

## SUMMARY OF PRINCIPAL ASSUMPTIONS USED TO CALCULATE BENEFIT OBLIGATIONS

	2010 Pension Benefits	2009 Pension Benefits	2010 Other Benefits	2009 Other Benefits
Discount rate at end of the period	5.4%	5.8%	5.4%	5.8%
Rate of compensation increase	4.0%	4.0%	4.0%	4.0%

The assumed hospital and drug cost increase was 9.0% per annum initially. As of October 1, 2010, the assumed rate began its gradual decrease to a rate of 5.0% in 2018; the rate will remain at that level thereafter. Dental costs are assumed to increase by 6.0% per annum initially. As of October 1, 2010, the assumed rate began its gradual decrease to a rate of 4.5% in 2013; the rate will remain at that level thereafter.

## SUMMARY OF BENEFIT COSTS AND PLAN CONTRIBUTIONS

	2010 Pension Benefits	2009 Pension Benefits	2010 Other Benefits	2009 Other Benefits
(in thousands of Canadian Dollars)	\$	\$	\$	\$
Benefit cost	15,692	12,524	7,147	6,240
Employer contributions	15,416	17,603	1,770	1,717
Plan participants' contributions	3,008	2,749	-	-
Benefits paid	15,428	21,458	1,770	1,717

The most recent actuarial valuation of the registered pension plan for funding purposes was at January 1, 2008, and the date of the next required valuation is January 1, 2011.

## SUMMARY OF PRINCIPAL ASSUMPTIONS USED TO CALCULATE BENEFIT COSTS

	2010 Pension Benefits	2009 Pension Benefits	2010 Other Benefits	2009 Other Benefits
Discount rate at the beginning of the period	5.8%	6.1%	5.8%	6.1%
Expected return on plan assets	6.75%	6.75%	-	-
Rate of compensation increase	4.0%	4.0%	4.0%	4.0%
Rate of indexing	2.5%	2.5%	-	-

## 8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

As at December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
Relating to property and equipment	2,771	2,994
Relating to intangibles	920	242
Relating to operations	18,399	16,837
	<b>22,090</b>	<b>20,073</b>

## 9. DEBT

### NOTE PAYABLE TO ONTARIO ELECTRICITY FINANCE CORPORATION (OEFEC)

The note payable to OEFEC is unsecured, bears interest at a per annum rate equal to the yield earned on 90-day Province of Ontario treasury bills on the quarterly reset date plus 25 basis points and is repayable in full on May 1, 2011. Interest accrues daily and is payable in arrears quarterly in February, May, August and November of each year. The fair value of the note payable approximates the carrying value. As of February 10, 2011, the IESO is exploring alternatives, with OEFEC and various Canadian chartered banks, to refinance the \$78.2 million debt. The IESO is confident the refinancing will be in place for May 1, 2011.

### CREDIT FACILITY

The IESO had an unsecured credit facility agreement with a Canadian chartered bank which expired on April 30, 2010. Effective May 1, 2010, the IESO entered into a new unsecured credit facility agreement with OEFEC, which will make available to the IESO an amount up to \$60.0 million. The credit facility expires on April 30, 2013. Advances under this facility are available in Canadian dollars by way of the Province of Ontario's cost of borrowing for a 30-day term plus 25 basis points per annum. As at December 31, 2010, \$2.0 million was drawn on the credit facility, (2009 - \$nil).

## 10. CAPITAL DISCLOSURES

The IESO's primary objectives are to maintain and enhance the reliability of Ontario's power system, administer the wholesale electricity market, and serve the needs of market participants and stakeholders. In order to fulfill its mandate, the IESO receives fees from market participants (Note 1). The IESO has a limited ability to accumulate a surplus from these fees (Note 11).

On April 1, 2010, the Ontario Energy Board (OEB) issued its order approving the IESO's application fee of \$1,000, the usage fee of \$0.822/MWh and the IESO's revenue requirements in the amount of \$122.8 million and capital expenditures in the amount of \$21.6 million.

The IESO submitted the proposed 2011 expenditures, revenue requirements, and fees to the OEB for review on November 2, 2010 after approval by the Minister. The Minister provided formal approval of IESO's business plan on November 1, 2010. As of February 10, 2011, the OEB has not approved the IESO's proposed expenditures, revenue requirements, and fees for 2011.

In addition, the IESO maintains a credit facility for short-term funding to support its various capital requirements. The IESO has customary covenants associated with the credit facility and is in compliance with all of these covenants.

## 11. ACCUMULATED DEFICIT AND REBATES TO MARKET PARTICIPANTS

In its 2011 rate application, the IESO requested to retain \$13.1 million in its approved regulatory deferral account. The IESO proposed that this accumulated surplus be retained in order to maintain rate stabilization over the planning period (2011 to 2013). Accordingly, the IESO recognized \$10,193,142 in rebates to market participants of system fees in 2010 (2009 - \$4,323,840). As at February 10, 2011, the retention of \$13.1 million in accumulated surplus has not yet been approved by the OEB.

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

### Accumulated Deficit

As at December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
Regulatory deferral account (a)	13,100	5,000
Accumulated market penalties and fines (b)	1,134	1,372
Smart Metering Entity - accumulated deficit (c)	(41,713)	(25,897)
	<b>(27,479)</b>	<b>(19,525)</b>

### a) Approved Regulatory Deferral Account

As at December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
Accumulated Surplus – beginning of year	5,000	5,000
Revenues (before rebates to Market Participants)	130,041	125,770
Rebates to Market Participants	(10,193)	(4,324)
Expenses	(99,550)	(99,849)
Amortization	(13,954)	(21,239)
Net interest	1,756	(358)
<b>Accumulated Surplus – end of year</b>	<b>13,100</b>	<b>5,000</b>

### b) Accumulated Market Penalties and Fines

As at December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
Accumulated Surplus – beginning of year	1,372	1,832
Revenue from Penalties and Fines	5	53
Customer Education Expenses	(243)	(513)
<b>Accumulated Surplus – end of year</b>	<b>1,134</b>	<b>1,372</b>

### c) Smart Metering Entity - Accumulated Deficit

As at December 31 (in thousands of Canadian dollars)	2010 \$	2009 \$
Accumulated Deficit – beginning of year	(25,897)	(12,443)
Smart Meter Program Costs	(13,665)	(9,962)
Smart Meter Amortization	(1,700)	(3,080)
Smart Meter Interest Expense	(451)	(412)
<b>Accumulated Deficit – end of year</b>	<b>(41,713)</b>	<b>(25,897)</b>

In his approval letter to proceed to the OEB for approval of the 2010 usage fee, the Minister noted the intention of the IESO to apply to the OEB separately for a smart meter service fee with respect to the costs the IESO has incurred on the smart metering initiative. At that time, the Minister requested, prior to the IESO filing an application to the OEB in respect of a smart meter service fee, the IESO provide him with a detailed implementation plan, and schedule for the integration of the local distribution companies, to enable a broader transition to time-of-use pricing for electricity consumers. The IESO has since provided a plan to the Minister and received approval to proceed with an application before the OEB.

The IESO has been performing its role as SME under the interim SME licence initially issued by the Board on September 14, 2007, with extensions of various lengths granted since that date.

As of February 10, 2011, the IESO's smart meter service fees have not yet been established.

## 12. RELATED PARTY TRANSACTIONS

The Province of Ontario is a related party as it is the controlling entity of the IESO. OEFC, OPA, 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 9). Interest payments made by the IESO in 2010 for the note payable were \$514,128 (2009 - \$3,278,830) and for the credit facility were \$17,878 (2009 - \$nil).

The IESO performs system studies for the OPA in support of their Power System Planning requirements. In addition, the IESO also provides support to the OPA's Demand Response program. In 2010, the IESO invoiced the OPA \$449,897 (2009 - \$356,516) for services associated with these programs. The IESO is participating with the OPA in a Solar Integration Study and has incurred \$23,450 in 2010 (2009 - \$nil). As of December 31, 2010, the IESO had a net receivable balance with the OPA of \$198,271 (2009 - \$51,696).

Under the *Ontario Energy Board Act, 1998*, the IESO incurs registration and licence fees. The total of the transactions with the OEB were \$487,713 in 2010 (2009 - \$526,572).

The IESO performed connection assessment and approvals for Hydro One in 2010 and began performing technical feasibility studies. The IESO invoiced Hydro One \$417,823 in 2010 (2009 - \$361,955). The IESO procures short circuit studies as part of connection assessments and approvals and meter services on IESO owned interconnected revenue meters from Hydro One. In 2010, the IESO incurred costs of \$137,694 (2009 - \$692,733) for these services. As of December 31, 2010, the IESO had a net payable balance with Hydro One of \$40,863 (2009 - net receivable balance of \$46,019).

In 2010, the IESO performed connection assessment and approvals for OPG; administered telecommunication services to market participants to connect to the real-time market systems and began performing technical feasibility studies. In 2010, OPG was invoiced \$409,504 (2009 - \$185,667). OPG provided security clearance services to the IESO, which were discontinued in July 2010. In 2010, the IESO incurred costs of \$11,780 (2009 - \$41,150). As of December 31, 2010, the IESO had a net receivable balance with OPG of \$123,533 (2009 - \$20,737).

## 13. 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 has 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 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 US dollars, primarily related to vendor payments, and maintains a US dollar denominated bank account. From time to time, the IESO uses currency forward purchase contracts to purchase foreign currencies for delivery at a specified date in the future at a fixed exchange rate. In addition, the IESO invests in pooled funds with US dollar and other foreign currency denominated investments. The reasonably possible currency risks associated with these exposures were not material as at December 31, 2010.

#### ii) Interest Rate Risk

The IESO is exposed to changes in interest rates primarily through its variable rate credit facility, cash equivalents, and long-term investments. Long-term investments include investments in a pooled Canadian bond fund. The reasonably possible interest rate risks associated with these exposures were not material as at December 31, 2010.

#### 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 value of equities in the IESO's pooled fund investments as at December 31, 2010 would have resulted in a change for the year (before the impact of adjustments to the approved regulatory deferral account (Note 11) of approximately \$4.0 million (2009 - \$3.3 million).

Financial instruments at fair value as at December 31, 2010 (in thousands of Canadian dollars)	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	8,609	-	-	8,609
Investment in pooled funds	21,816	-	-	21,816
	<b>30,425</b>	-	-	<b>30,425</b>

## 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 and accounts receivable and indirectly through its exposure to bond investments in pooled funds. Direct exposure to credit risk is limited to the carrying amount presented for these assets on the statement of financial position. The IESO manages credit risk associated with cash equivalents (which amounted to \$8.6 million as at December 31, 2010) through approved management policy which limits investments to investment grade investments with counterparty-specific limits of no more than \$20 million. Accounts receivable as at December 31, 2010 included no material items past due and substantially all of the balance was collected as at January 21, 2011. As at December 31, 2010, the Canadian bond fund in which the IESO invests comprised of 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. The IESO manages liquidity risk by forecasting cash flows to identify financing requirements. Cash flows from operations and investment income and maintaining appropriate credit facilities reduce liquidity risk. The IESO's long-term investments in pooled funds are normally able to be redeemed within three business days, however, the 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.

# 14. COMMITMENTS AND CONTINGENCIES

## OPERATING COMMITMENTS

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

As at December 31 (in thousands of Canadian dollars)	2010 \$
2011	1,818
2012	709
2013	596
2014	527
2015	527

## 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.

# EXECUTIVE COMPENSATION AT THE IESO

## COMPENSATION RESTRAINTS

Over the past few years, IESO Management compensation has been significantly influenced by the Ontario government's call for restraint in compensation within Ontario's public sector. Since 2008 the government has asked the public sector and its agencies, including the IESO, to constrain compensation adjustments and workforce growth as part of its economic program following the 2008/2009 recession. In early 2010 the government took the step of enacting the *Public Sector Compensation Restraint to Protect Public Services Act (the Restraint Act)* which constrains adjustments to compensation, as well as to pension and benefit provisions, for all non-unionized employees over the period of March 24, 2010 to March 31, 2012.

The IESO has responded to the government's request and the subsequent legislative requirements. While the legislation was not enacted until March 2010, the IESO met the government's earlier request for constraint by freezing the fixed compensation of its executives at the start of 2010 and constraining variable compensation awards to executives for 2009 performance. For 2011, adjustments for fixed compensation have again been constrained beyond requirements within the recent legislation.

## IESO BOARD OF DIRECTORS INITIATIVE ON MANAGEMENT COMPENSATION PROGRAM DESIGN

As well as the above government initiatives, the IESO Board of Directors (the Board), as reported in last year's disclosure, has undertaken an in-depth review of the IESO Management compensation program design to ensure that it meets the IESO's business needs for the future. The objective of this initiative is consistent with the principles embedded in the previous Agency Review Panel Report of ensuring an effective compensation plan is in place to attract and to retain high calibre individuals, to reinforce effective performance and to reflect future market and government expectations. The current program was put in place in 2000 when the expectations for future needs were different from today's realities. This redesign is a work in progress and the intent is to make any changes on or after April 1, 2012 following the period of *the Restraint Act*. The following sections contain descriptions of the programs existing at the time when decisions for 2010 compensation were undertaken along with explanations of the impact of government restraint on the application of those affected programs.

## PROGRAM OBJECTIVES

The current IESO compensation program is an integrated program for all Management Group staff and was designed to attract, retain and motivate the calibre of executives required to support the achievement of our statutory mandate, business objectives and corporate vision. Accordingly, the compensation philosophy and programs were built on the following objectives:

- To focus executives on meeting the IESO's business objectives
- To attract qualified and talented staff needed to carry out the IESO's mandate
- To be able to retain valued staff
- To have the flexibility to reward results and demonstrated competencies
- To have compensation levels which are responsible and defensible to stakeholders and customers.

The philosophy underlying these objectives is that total compensation for senior management should be sufficient, but not overly sufficient, to attract and retain the skills and competencies necessary to carry out the IESO's mandate.

## PROGRAM GOVERNANCE

In the past, including the 2010 program, the IESO Board established the compensation objectives for the following year's program. They delegated the responsibility to thoroughly review the compensation objectives, policies and programs to the Human Resources and Governance Committee of the Board (HRGC) which made recommendations to the full Board for approval. The Board is composed of ten independent, external Directors, appointed by the Minister of Energy, with broad experience in both industry and public sector organizations, plus the Chief Executive Officer. In carrying out their mandate, the Board members had access to Management's perspectives as well as those of expert consultants in the compensation field (including experts at various times from Towers Watson, Mercer and Hay). These programs were reviewed at least annually regarding business needs, program objectives and design, industry compensation trends, internal compensation relativities, and external market relativities.

In addition to the formal governance and oversight structure in place for compensation matters, the IESO, then as well as now, discloses compensation levels annually for staff earning \$100,000 or more as part of its public sector salary disclosure. For the IESO, a further level of public review and assurance is provided through a statutorily required annual review of the IESO's expenditures, revenue requirements and fees. Information related to compensation matters, including Management compensation and market relativities, are subjects of the Ontario Energy Board review. A range of small and large consumers, assisted by their legal and professional advisors, are represented in these public proceedings. The IESO is also responsive to various requests by the Ministry of Energy in relation to compensation enquiries, such as the Agency Review Panel (ARP) in 2007, which conducted an exhaustive review of senior management compensation for the various agencies in the Ontario electricity sector.

## MARKET COMPARISONS

The IESO regularly benchmarks compensation to similar positions in Canadian industry. The objective of this initiative is to determine how IESO Management compensation levels compare to those in the marketplace particularly in relation to the 50th percentile or median of the market.

The comparator group used in the past included fifteen mid-size to smaller Canadian energy sector companies with care taken to assess positions of similar size, scope and complexity. These comparators were segmented into government and non-government categories and market compensation data was gathered for each segment. A 50/50 weighting was applied to each of the government and non-government market results to reflect an overall comparator market for executive compensation at the IESO. The list of comparators is outlined below:

Government Comparators	Non-Government Comparators
<ul style="list-style-type: none"> <li>Alberta Electric System Operator</li> </ul>	<ul style="list-style-type: none"> <li>Alliance Pipeline Limited</li> </ul>
<ul style="list-style-type: none"> <li>Atomic Energy of Canada Limited</li> </ul>	<ul style="list-style-type: none"> <li>ATCO Ltd. &amp; Canadian Utilities Limited*</li> </ul>
<ul style="list-style-type: none"> <li>Enmax Corporation</li> </ul>	<ul style="list-style-type: none"> <li>Bruce Power</li> </ul>
<ul style="list-style-type: none"> <li>EPCOR*</li> </ul>	<ul style="list-style-type: none"> <li>Emera Inc.</li> </ul>
<ul style="list-style-type: none"> <li>New Brunswick Power Corporation</li> </ul>	<ul style="list-style-type: none"> <li>FortisAlberta</li> </ul>
<ul style="list-style-type: none"> <li>Newfoundland &amp; Labrador Hydro Electric Corporation</li> </ul>	<ul style="list-style-type: none"> <li>Kinder Morgan Canada Inc. (Pipelines)</li> </ul>
<ul style="list-style-type: none"> <li>Saskatchewan Power Corporation</li> </ul>	<ul style="list-style-type: none"> <li>Spectra Energy Transmission*</li> </ul>
	<ul style="list-style-type: none"> <li>TransAlta Corporation*</li> </ul>

*\*For these large organizations a full level downward adjustment has been made for compensation comparison purposes (e.g. the IESO CEO level is compared to the SVP/EVO level for the external firm).*

Market data was gathered for various components of compensation including fixed compensation and total cash compensation but with emphasis on total rewards, including the sum of fixed and variable compensation, benefits and pension. The IESO undertook such a study in 2008 and the results indicated that total rewards for the Management Group overall were at the median of the market.

As indicated above during 2010, the IESO Board engaged Mercer to review the design of its Management Compensation Program for the future. One of the aspects of this work includes reviewing the criteria for future benchmarking analysis. While Mercer has carried out some of this analysis, the final results will be integrated within the overall redesign of the IESO Management Compensation Program for implementation on or after April 1, 2012.

## PROGRAM DESCRIPTION - ROLES

The current IESO program includes fixed and variable compensation, core and flex benefit plans, and pension provisions. IESO Human Resources staff participates in and reviews results from various compensation surveys and monitors economic trends such as compensation trends, inflation and unemployment rates which impact on compensation, as well as monitoring internal compensation relativities. Based on this data and the IESO business priorities, Human Resources staff develops recommendations on compensation programs for all Management staff. External specialized compensation, benefit and pension consultants are utilized to ensure accurate, representative market compensation data is obtained, that current industry compensation trends are being utilized, as well as to provide insight and recommended adjustments to current programs. An expert, external consultant also reviews the recommendations as to the reasonableness and appropriateness of Management's recommendations.

Senior Management then reviews the recommendations and provides advice to the CEO who determines whether the recommendations should be advanced to the HRGC and the IESO Board. The Chair of the HRGC reviews the recommendations and supporting data prior to submission to the HRGC, along with input from an expert, external consultant. The Chair determines if additional external expertise is required. The analysis and conclusions from these external experts are provided to the HRGC members for their consideration. The HRGC reviews in detail the recommendations, the supporting data and advice from the expert external consultant(s), and decides on the recommendations to go to the full Board. The Board reviews the submissions and makes a final determination on the recommendations.

For the 2010 review, the above steps were undertaken and data provided to the HRGC. However, the overriding concern on the part of Management and the IESO Board related to uncertainty in general economic conditions, the record provincial deficit and signals from the Ontario government concerning the need for continued cost control. These factors strongly influenced the decisions of the IESO Board relating to Management compensation.

## PROGRAM DESCRIPTION - FIXED COMPENSATION

Historically, broad salary ranges were put in place for each level of executive taking into account comparable market relativities. Within these bands individuals were assessed as developmental, mature or expert in their position relative to an established competency model. This model consisted of behavioural competencies, such as customer focus, drive for results, teamwork, leadership, and strategic business sense. Assessments were based upon demonstrated competency. Each individual was awarded a fixed compensation level within their band based upon their assessed competency.

In the fall of 2009, unfavourable economic conditions as a result of significant downturns in the major global economies were expected to continue into 2010. The Government of Ontario responded to these conditions by calling for compensation restraint within the public sector. The IESO applied the spirit of the government's guidelines by limiting 2009 salary increases for Management staff earning \$150,000 or more annually to 1.5%. For 2010, the IESO again responded to the ongoing concerns about the economy and the government's continued need for restraint by freezing Management pay ranges, limiting increases within the Management Group to a few anomaly situations and providing zero fixed compensation increases to all senior executives at the IESO.

## PROGRAM DESCRIPTION - VARIABLE COMPENSATION

In order to promote a results orientation in the senior team, the variable pay plan is a significant component of the total compensation of executives. The IESO Board annually establishes a robust set of performance measures which are evaluated each year and these results carry a 70% weight within each executive's variable compensation award. The remaining 30% results from the assessment of predetermined measures/targets established for each individual executive. The CEO's variable compensation award for achieving the targets was set at 65% of fixed compensation in 2010 and the Vice Presidents' award levels were set at 50% of fixed compensation. The plan provides for awards above or below these target amounts depending on the performance results achieved. To address retention, 50% of the earned variable compensation is deferred and paid out over the subsequent two-year period, with accrued but unpaid amounts forfeited in the event of termination with cause or voluntary resignation. The above applies to the named executives with the exception of Mr. Leonard whose target award in 2010 was 40% and his deferral rate was 33%.

Under the provisions of the government's *Restraint Act*, the design and operation of this program is to continue in place until at least March 31, 2012.

## PROGRAM DESCRIPTION - GROUP BENEFITS

The group benefit plan provides a core level of health and dental benefits, life insurance, disability coverage and vacation which can be adjusted by the executives through a flexible component within the plan. The flexible element provides executives the option of adjusting their benefits to meet their individual/family needs including vacation above core amounts, levels of life insurance, health coverage and other components. Under the government's *Restraint Act* this program, as existed on March 24, 2010, is also to continue in place until March 31, 2012.

## PROGRAM DESCRIPTION - PENSION PLAN

A defined benefit pension plan provides annual retirement income calculated as 2% of fixed compensation and one-half of variable compensation paid during the highest paid 36 consecutive months of service multiplied by years of service, to a maximum of thirty-five years. The pension formula is integrated with the Canada Pension Plan (CPP) to provide a level income stream before and after age 65, when the IESO pension is reduced to reflect benefits from CPP. The Plan also has early retirement provisions as well as commuted value, pension deferral and reciprocal transfer options.

The plan provides a maximum benefit of 70% of highest paid, pre-retirement earnings. As the Canadian Revenue Agency limits the amount of pension payable from a registered plan, the IESO has a supplemental employee retirement plan (SERP) to provide required pension income above that payable from the registered plan. Pension funding is a combination of employer and employee contributions.

The plan also provides several options including member's life only or joint and survivor pensions, as well as pre-retirement death provisions to provide benefits to surviving spouses or beneficiaries.

Under the government's *Restraint Act*, the IESO pension plan for Management staff cannot be changed beyond provisions which existed on March 24, 2010 until after March 31, 2012.

## PERFORMANCE MEASURES & IMPACT ON COMPENSATION

The IESO annually establishes corporate performance measures relating to its business priorities during the business planning process. These are approved, monitored and assessed by the IESO Board of Directors each year. Individual performance measures supporting one or more corporate performance measure are also developed for each executive.

As outlined above, the results achieved each year impact on each executive's variable pay. The following chart highlights each of the business perspectives where measures are established and provides a brief description of the type of measurement which was approved by the IESO Board for 2010.

Business Perspective	Areas of Measurement
<b>Reliability (30% Weight)</b>	<ul style="list-style-type: none"> <li>• Ontario's annual unsupplied energy is within acceptable limits</li> <li>• Compliance by the IESO and market participants with applicable reliability operating standards, market rules and regulatory requirements</li> </ul>
<b>Customers &amp; Stakeholders (25% Weight)</b>	<ul style="list-style-type: none"> <li>• The market responsiveness of suppliers and consumers to the price of electricity</li> <li>• Customer satisfaction with the IESO and the market</li> <li>• Adaption of IESO's actions to support the objectives of the <i>Green Energy and Green Economy Act</i> and the obligations prescribed within its regulations</li> </ul>
<b>Operational Effectiveness (20% Weight)</b>	<ul style="list-style-type: none"> <li>• IESO's capacity to undertake and complete change initiatives</li> <li>• Employee engagement</li> <li>• Delivery on the business plan both capital and OM&amp;A</li> </ul>
<b>Reputation &amp; Relationships (25% Weight)</b>	<ul style="list-style-type: none"> <li>• Reputation amongst customers and stakeholders</li> <li>• Strategic engagement with government regulators and stakeholders to advance the IESO's objectives</li> <li>• IESO's technical capability supports government policy in the planning activities</li> </ul>

A rating scale ranging from unsatisfactory to exceeding expectations is used to assess the results for both corporate and individual performance objectives and is used to calculate the associated variable pay amount. According to this scale, corporate results and individual results may be rated from zero to 1.5 times the target variable amount (the table below outlines the ratings in detail). A payout factor is then determined and applied to the target variable pay amount for each executive.

Type of Performance	Corporate Rating	Individual Rating
Exceeding expectations	1.3 – 1.5	1.2 – 1.5
Meeting expectations	0.8 – 1.2	0.8 – 1.1
Approaching expectations	0.3 – 0.7	0.4 – 0.7
Unsatisfactory/below expectations	0.0	0.0

## OTHER CONSIDERATIONS

Compensation decisions may at times be impacted by market factors – such as the recruitment of an executive with specialized skills/competencies or possessing unique talents within the industry. To this end, individual incumbent arrangements are sometimes established relating to terms of employment and the possibility of future termination. The CEO has an employment agreement which outlines terms and conditions for a five and one-half year period of employment and includes termination provisions of 24 months for severance. Some Vice-Presidents also have provisions which provide 24 months or less of severance for termination without cause. In addition, two Vice Presidents (Mr. Campbell and Mr. Limbrick) have agreements to provide accelerated pension provisions such that, at age 65, they will each have twenty-five years of credited service.

## EXECUTIVE COMPENSATION AND PENSION STATEMENTS

The first table on page 36 details the annual compensation for the year ended December 31, 2010 for the Executives listed. The information provided in the Summary Compensation Table differs from the information published under the *Public Sector Salary Disclosure Act (Ontario)* for the indicated period due to the timing of payment of variable pay. Disclosures under the *Public Sector Salary Disclosure Act* are limited to amounts listed on T4 taxation forms for each year (i.e. includes variable pay paid out in 2010), whereas, information in the summary compensation table is based on the year for which the variable pay was earned. Variable pay is determined early in the year following the year assessed. Under the IESO plan, 50% of that amount is then paid early in the year following the assessed year and 50% is deferred for payment in future years.

The second table on page 36 outlines pension plan participation and benefits for each of the Executive Officers listed. Specifically detailed are:

- total years of credited service in the pension plan
- the increase in the compensatory value of the pension (due to increased service and pensionable earnings, if applicable) during 2010
- the increase in the non-compensatory value of pension (due to a decrease in the pension discount rate) during 2010
- the estimated annual pension payable at age 65 based upon the executive's service and pensionable earnings as of December 31, 2010
- the estimated annual pension with service credits projected to age 65 using actual pensionable earnings as of December 31, 2010.

Various factors have an impact on the pension calculations displayed in the 2010 Pension Benefits Table. Should interest or discount rates vary significantly from one year to the next, there will be volatility in year over year pension amounts reported.

## 2010 SUMMARY COMPENSATION TABLE

Name & Position	Salary	Variable Pay <sup>1</sup>		Other Annual Compensation <sup>2</sup>	Total Cash Compensation	Amounts Reported Under Public Sector Salary Disclosure
		Paid	Deferred			
Paul Murphy President & CEO	\$331,397	\$124,183	\$124,183	\$26,850	\$606,613	\$601,892
Ted Leonard VP Finance & CFO	\$185,000	\$52,704	\$25,958	\$3,899	\$267,561	\$259,385
Ken Kozlik VP Operations & COO	\$228,375	\$62,404	\$62,404	\$9,931	\$363,114	\$329,618
Bill Limbrick VP Organizational Development & CIO	\$269,705	\$73,697	\$73,697	\$0	\$417,099	\$414,016
Bruce Campbell VP Resource Integration	\$275,063	\$77,224	\$77,224	\$180	\$429,691	\$426,548

1. Reflects variable pay earned in 2010 and subsequently paid out to each executive in early 2011 (50%) with deferred amounts (50%) to be paid over the subsequent 2 years with interest. (All except Mr. Leonard whose award is paid out at 67% with 33% deferred).

2. Includes residual payout from IESO's flex benefit plan.

## 2010 PENSION BENEFITS TABLE

Name & Position	Number of Years Credited Service	Increased Pension Value During 2010		Annual Benefits Payable Upon Retirement	
		Compensatory Amount During Year \$	Non Compensatory Amount During Year \$	At Year-End (2010) <sup>1</sup> \$	At Age 65 <sup>2</sup> \$
Paul Murphy President & CEO	33.3	\$121,000	\$655,000	\$291,000	\$305,000
Ted Leonard VP Finance & CFO	14.8	\$49,000	\$175,000	\$58,000	\$138,000
Ken Kozlik VP Operations & COO	32.1	\$37,000	\$380,000	\$165,000	\$180,000
Bill Limbrick VP Organizational Development & CIO	17.7	\$102,000	\$192,000	\$119,000	\$168,000
Bruce Campbell VP Resource Integration	21.9	\$142,000	\$236,000	\$151,000	\$172,000

1. Payable at age 65 assuming no increase in pensionable earnings and service beyond year-end 2010.

2. Payable at age 65 assuming no increase in pensionable earnings beyond year-end 2010 and service credit continues until age 65.





Power to Ontario. On Demand.

Independent Electricity System Operator  
655 Bay Street, Suite 410  
P.O. Box 1  
Toronto, ON M5G 2K4  
[www.ieso.ca](http://www.ieso.ca)

Phone: 905.403.6900  
Toll-free: 1.888.448.7777  
E-mail: [customer.relations@ieso.ca](mailto:customer.relations@ieso.ca)

