2008 – 2010
BUSINESS PLAN

ieso
Power to Ontario. On Demand.

CONTENTS

MESSAGE FROM THE PRESIDENT & CHIEF EXECUTIVE OFFICER

I am pleased to provide the Independent Electricity System Operator's (IESO) 2008-2010 Business Plan, which identifies our opportunities and outlines our plan of action over the next three years.

At the core of the IESO's responsibilities is the continued reliable operation of Ontario's interconnected power system and administration of its $10 billion wholesale electricity market. We are proud to provide these critical services while at the same time supporting the largest electricity infrastructure upgrade that Ontario has ever seen.

Two thousand and seven has been a year marked by familiar accomplishments and new opportunities. A major accomplishment for the entire North American electricity industry was the adoption of mandatory and enforceable reliability standards. These have been in place in Ontario since the market opened in 2002 but their broader application will strengthen reliability across the continent and address a primary recommendation that emerged from the 2003 blackout. On the new opportunity front, the Province's commitment to smart meters will allow residential customer conservation and demand management to be driven through prices that vary with time of use. The IESO has been appointed Ontario's Smart Metering Entity (SME) to administer and operate the central meter data repository and to develop communications in support of the Ontario-wide roll-out of smart meters. We are excited to be working in support of an Ontario culture of energy conservation and awareness.

Looking forward, I am pleased to report that our customers will continue to see reduced costs from the IESO. We are proposing a fee reduction of two per cent in 2008, the third consecutive year our fees will have been reduced, with a further fee reduction, barring fluctuations in long-term interest rates and energy demand, expected later in the business planning period. Over the course of the business planning period, these fee reductions translate to projected savings to customers of approximately $22 million on top of the $49 million in costs savings that we will have helped customers realize over the past two years. Supported by a strong fiscal governance framework, we will continue to demonstrate financial prudence while maintaining the high level of service that our customers expect and deserve.

Like many other companies within our industry, a large number of our employees are approaching retirement. The IESO operates within a highly sophisticated and complex environment that is characterized by a high proportion of well-educated, professional employees with a heavy concentration towards experienced operators, electrical engineers and information technology professionals. One of our key priorities over the planning period is to successfully address this challenge and ensure a seamless transition to the next generation of IESO employees.

A recent Reliability Readiness Audit by the North American Electric Reliability Corporation (NERC) commended the IESO on our foresight and investment in our student cooperative program. This recognition comes on the heels of a 2005 NERC report that identified our structured training program as an "example of excellence" for other North American electric organizations. Supported by these and other strong programs, we will maintain and enhance our core competencies around our existing complement of 422 regular employees.

Stakeholder input will continue to guide the IESO decision-making process over the next three years. We regularly solicit stakeholder feedback and advice through a number of committees, working groups and forums through the stakeholder engagement process we introduced two years ago. Through these processes we have addressed a wide variety of stakeholder interests. Yet we also recognize the need to continuously ensure that our stakeholdering efforts reflect best practices and help facilitate effective stakeholder input. As such, the IESO is conducting a review of its stakeholdering processes, principles and practices to ensure that issues are heard and appropriately addressed.

Our continuing efforts to drive improvements in the market will follow the step-by-step approach we introduced in last year's Business Plan. Each step will be designed to take advantage of opportunities to improve the efficiency of the market, to improve how the market facilitates the business of our stakeholders, and to encourage the competitiveness of the market. Demonstrating value for consumers and market participants will be a key criterion for market evolution initiatives.

All of our activities are carried out within the broader context of achieving our strategic priorities of reliability, value, market evolution, responsiveness and trust. Our strategic priorities are approved by our independent Board of Directors and provide us with high-level organizational direction.

This Business Plan has been developed to meet our strategic business priorities.

Paul Murphy
President & Chief Executive Officer

VISION, MISSION & STRATEGIC PRIORITIES

VISION

A vibrant Ontario economy supported by
a reliable and competitive electricity market.

MISSION

To act in the interests of the people of Ontario to enable reliable, competitively-priced and sustainable electricity service.

STRATEGIC PRIORITIES

- Delivering a reliable supply of electricity on demand;
- Providing value in the IESO's services and products;
- Developing Ontario's market through the evolution of the IESO-administered markets;
- Responding to the needs and concerns of stakeholders; and
- Earning the trust of all stakeholders as a just administrator and capable advisor.

ABOUT THE IESO

The IESO is a non-profit, corporate entity without share capital established in 1998 by the Electricity Act of Ontario. Independent of all other electricity marketplace participants, the IESO is governed by a Board of Directors, appointed by the Minister of Energy to oversee the management of the organization's business and affairs.

Bringing together almost 300 generators, traders, local distribution companies (LDC), transmitters and large volume consumers, the IESO oversees the reliable operation of the provincial electricity grid and settles Ontario's $10 billion wholesale electricity market.

The IESO is responsible for managing Ontario's smart metering meter data and repository systems, which includes the collection, validation, and estimation of energy consumption data from all of Ontario's smart meters. The IESO's successes in this area resulted in its appointment as Ontario's Smart Metering Entity in 2007.

The IESO is committed to maintaining strong corporate governance. Compliance with regulations, laws, and policies is at the forefront of its practices. Such a commitment requires allocation of the necessary time and resources while allowing the flexibility to respond to shifting priorities. The IESO will continue to optimize the use of both its financial and human resources to provide the electricity sector with trusted services while demonstrating appropriate accountability, comparability, transparency and value.

RELIABLE ELECTRICITY SUPPLY ON DEMAND

At the core of the IESO's mandate is its responsibility to continuously monitor and direct the operation of Ontario's power system. Balancing Ontario's electricity demand with supply is a highly complex process. Every five minutes, the IESO forecasts electricity demand throughout the province and directs generators to provide the required amount of electricity to meet that demand. To keep the system in balance, the IESO control room processes on average between 15,000 and 20,000 intertie transactions and fields approximately 30,000 telephone calls per month. Reliably balancing supply and demand is a continuous process that repeats itself 24 hours a day, seven days a week, 365 days a year.

Every five minutes, the IESO forecasts electricity demand throughout the province and directs generators to provide the required amount of electricity to meet that demand.

Ontario's transmission system is part of a larger connection of continental transmission systems. This connection to a large, stable, continental power system enhances the reliability of electricity delivery in Ontario and allows for economic imports and exports that benefit the province. To enhance overall performance, the IESO maintains operating agreements with neighbouring power system operators that formalize common operating practices. These agreements, combined with regular coordination of activities among the IESO and its neighbours, are critical to maintaining region-wide reliability.

In addition to the continuous operation of Ontario's power system, the IESO monitors the power system to identify what actions are required to maintain bulk electrical system adequacy. Through regular publications, the IESO apprises stakeholders of system developments and needs. For example, the quarterly 18-Month Outlook forecasts the short-term adequacy of generation and transmission facilities to meet projected energy demand. The semi-annual Ontario Reliability Outlook reports on the progress of interrelated generation, transmission and demand-side projects underway and identifies the requirements needed to meet Ontario's short-term reliability requirements.

Highlights from 2007

In 2007, the IESO's most significant and enduring achievement was the continued reliable operation of Ontario's integrated power system. Customers have consistently recognized IESO achievements in this area. In its most recent customer survey, the IESO received an excellent assessment on its ability to direct the reliable supply and delivery of electricity.

In addition to formal customer surveys, IESO performance is regularly audited by NERC and the Northeast Power Coordinating Council (NPCC). The IESO consistently receives excellent results on these and other audits that assess IESO compliance with required criteria and standards. In the most recent NERC Reliability Readiness Audit, the IESO was recognized with three noteworthy "examples of excellence." These included the IESO's gas-electric interdependency assessment, its cooperative education program, and the Ontario Reliability Outlook and 18-Month Outlook documents, which were described as "model documents for presenting reliability assessments." The election of senior-level IESO representatives to NERC and North American Energy Standards Board (NAESB) committees further highlighted the IESO's reputation for excellence in power system reliability.

In support of the reliable operation of Ontario's integrated power system, the IESO undertook a number of actions as part of its summer seasonal preparations. These included: conducting various emergency preparedness exercises and workshops in various cities across the province, modifying emergency preparedness actions, conducting generator reactive testing of large generator units, providing seasonal specific training, and participating in regional seasonal planning studies. In addition, during the summer the IESO issued precautionary power advisories to encourage consumers to reduce consumption in order to assure reliability during hot weather conditions. Lower actual demand relative to forecasted demand suggests that consumers heard and responded to the IESO advisories.

The IESO offers stakeholders a number of different in-person and on-line training seminars.

From an external compliance perspective, the IESO operated Ontario's power system in accordance with stringent NERC and regional NPCC reliability standards. These reliability standards also form the basis for the reliability requirements set out in the rules governing participation in Ontario's electricity market. In late 2006, Ontario recognized NERC as having authority, as the Electric Reliability Organization (ERO), to develop and enforce continent-wide reliability standards. Ontario's transition to mandatory NERC standards was seamless. This was due in large part to the fact that Ontario has held NERC standards as mandatory and enforceable since market opening in May, 2002.

From an internal compliance perspective, IESO reliability-related services and functions continue to be held to rigorous standards and performance metrics. Challenging corporate performance measures and strong internal controls drove the IESO to maintain and enhance reliability of Ontario's integrated power system.

Looking Forward

Ontario is undergoing the largest electricity infrastructure upgrade in over a century. The Integrated Power System Plan (IPSP), prepared by the Ontario Power Authority (OPA), identifies conservation, generation, and transmission investments needed over the next 20 years. This power system upgrade will include the development of additional natural gas generation and new clean energy projects, such as wind turbines, and the launch of major conservation and demand response programs. To ensure reliability the IESO will continue to monitor wind power performance and conduct studies and assessments that enable the integration of new generation and demand response programs into the power system. The OPA's conservation targets of 1,350 megawatts (MW) reduction in peak demand by the end of 2007 and a further 1,350 MW reduction by 2010 is expected to add forecasting complexity to the management of Ontario's electricity system. In response the IESO has begun to take steps to upgrade its forecasting tools and prepare for the impact of these programs on the power system.

At the time of publication, the IESO had approximately 590 MW of voluntary demand response registered through the Emergency Load Reduction Program (ELRP) and the Emergency Demand Response Program (EDRP). These registered loads are capable of reducing consumption upon IESO request, which improves the reliability of Ontario's power system. Looking forward, the IESO will work with LDCs to incorporate demand response programs not currently under the IESO's control. For example, the IESO and Toronto Hydro recently developed the ability to activate Toronto Hydro's Peak Saver program over and above the prescribed framework of the current ELRP parameters. Additionally, the IESO will continue to work with the OPA to include its demand management programs among the suite of IESO control actions. Specifically, the IESO would be responsible for activating the OPA's Demand Response 3 program that will provide 100 or 200 hours per annum of curtailment, per participant.

Improving the reliability of the power system will also be achieved through the first major upgrade to the IESO control room's Energy Management System and Market Information System (EMS/MIS). The EMS/MIS upgrade, which is planned to come on-line in the latter part of 2007 and in 2008, will increase the IESO's ability to maintain these critical systems that support IESO reliability and market responsibilities. Specifically, the upgrade will improve the IESO's demand forecasting capabilities and options, enhance protection against cyber security threats and more generally provide the IESO with increased flexibility to accommodate further system upgrades and improvements.

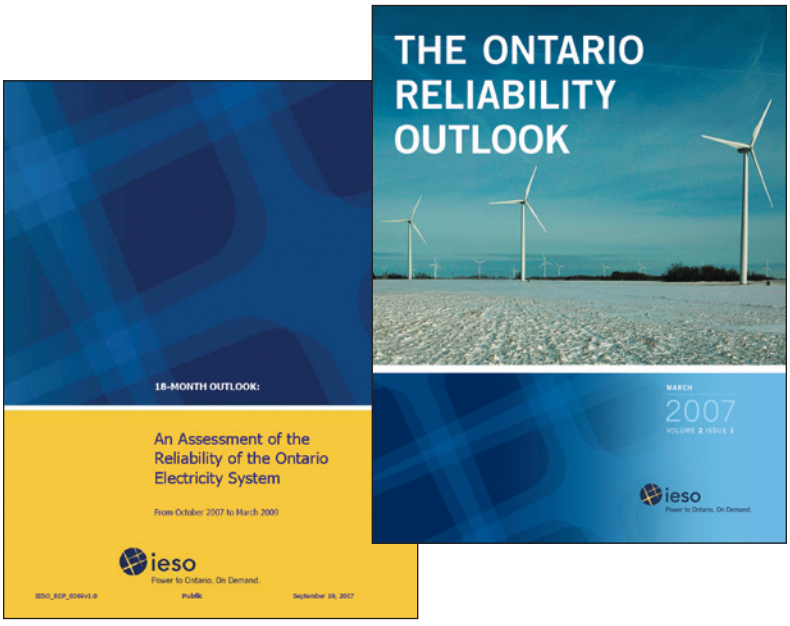
On the regulatory side, the IESO will work with NERC as it expands its activities. The IESO will continue to review new NERC reliability standards and provide feedback on the implications for Ontario. Of particular note are the NERC Critical Infrastructure Protection (CIP) reliability standards. These standards provide a comprehensive set of requirements to protect the North American bulk power system from malicious cyber attacks. They require bulk power system users, owners, and operators to establish a risk-based vulnerability assessment methodology and use that methodology to identify and prioritize critical physical and cyber assets. Once these critical cyber

assets are identified, the CIP reliability standards require, among other things, that the responsible entities establish plans, protocols, and controls to safeguard physical and electronic access, to train personnel on security matters, to report security incidents, and to be prepared for recovery actions.

The IESO commented on these standards while they were still in draft form to help establish requirements that were reasonable as well as robust. Due to the scope of facilities and entities covered by the CIP reliability standards NERC has an implementation plan that provides for a three-year phase-in to achieve full compliance with all requirements. In keeping with its leadership role, the IESO is not only ensuring its own compliance with the CIP standards but is also facilitating the compliance activities of those Ontario market participants identified as having critical assets.

To better enable compliance with all NERC reliability standards, the IESO recently initiated a project that maps the NERC reliability standards and requirements for each of its market participants. This innovative project will provide all market participants with a clear understanding of their reliability responsibilities and obligations. Similarly, through its leadership of the provincial Emergency Preparedness Task Force, the IESO is coordinating the Ontario electricity sector's pandemic-related business continuity planning.

Finally, over the course of the business planning period, stakeholders can remain updated on the forecasted security and adequacy of Ontario's integrated power system through IESO publications such as the Ontario Reliability Outlook , the 18-Month Outlook, interim updates, daily Security and Adequacy Assessments (SAA) and System Status Reports (SSR). As project commitments are made by the OPA, or included in the IPSP, the Ontario Reliability Outlook will continue to monitor and report on the progress of these infrastructure developments and their impact on future reliability.



Over the course of the business plan, stakeholders can remain informed through a number of IESO publications including the Ontario Reliability Outlook and the 18-Month Outlook.

PROVIDING VALUE IN THE IESO'S PRODUCTS AND SERVICES

The IESO manages the integrated power system and the bulk electricity market on behalf of Ontario. In carrying out these crucial responsibilities Management is focused on ensuring that ratepayers receive value for their money. Providing value requires a fiscally conservative approach to management while at the same time recognizing and acting upon those opportunities that will provide a net benefit to the people of Ontario.

This approach can be distilled into a simple financial objective – to demonstrate continued prudent financial management while meeting the IESO's corporate objectives.

Highlights from 2007

The IESO demonstrated value through the wide range of products and services that it offers on an ongoing basis. These products and services enable Ontario to benefit from the reliable and economic dispatch of resources to satisfy electricity demand. IESO products and services support the real-time operation and settlement of the IESO-controlled grid and the IESO-administered markets. The IESO provides around the clock operation and support of the integrated power system and provides the information technology infrastructure needed to support continuous market and system operations.

Over time, the IESO has worked with stakeholders to enhance and streamline its products and services. The following are among the many valued offerings provided to IESO customers:

- Active stakeholdering on market and operational issues;
- Direction and operation of the IESO controlled-grid;
- Scheduling and dispatch services;
- Metering services;
- Market settlement services;
- Connection assessments;
- Reliability assessments;
- Information services;
- Customer support;
- Monitoring of demand response programs;
- Market participant training;
- Emergency preparedness services;
- Ancillary service contracting;
- Compliance monitoring and enforcement; and
- Coordination with neighbouring jurisdictions.

From a financial standpoint, in 2007 the IESO was able to reduce its fee by over 10 per cent to 0.815 dollars per megawatt hour ($/MWh). This represented the second successive year in which the IESO has been able to reduce its fee. In addition, the IESO provided a rebate to customers of $12.7 million. This combination of a rebate and lower fees translated to 2007 projected customer savings of almost $28 million.

The IESO's prudent financial management has helped customers achieve savings through fee reductions and rebates.

The IESO's fee is based on projected demand and anticipated IESO total costs. Through prudent financial management the IESO has reduced its total costs every year since 2003. This has contributed to the IESO's ability to reduce its fee and to project future fee reductions. The IESO's ability to reduce total costs is supported by a robust system of internal financial governance.

This strong financial performance has been recognized by customers through their positive rating of the IESO in the area of financial management in its most recent customer survey. The strong financial outlook for 2008 is expected to further increase the level of stakeholder satisfaction and confidence in the IESO's management of its finances.

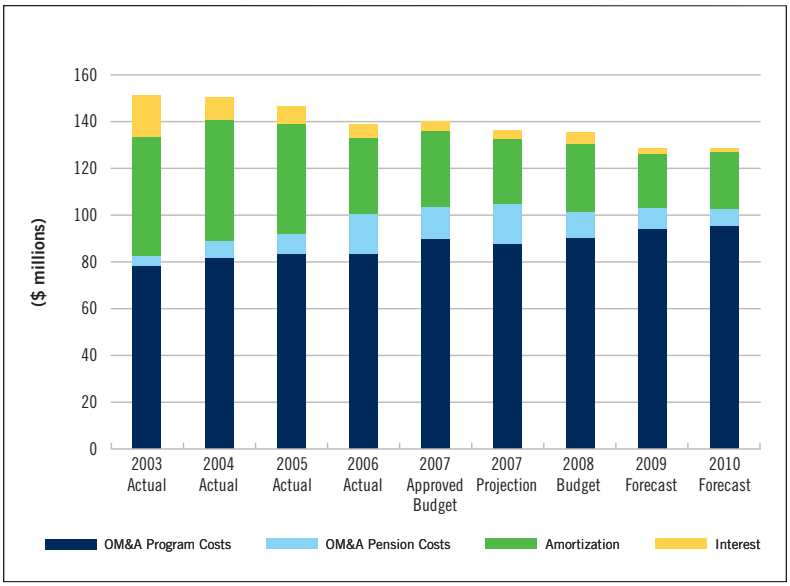
Looking Forward

Over the course of the business planning period the IESO will continue to deliver valuable services and products efficiently. Most significantly, the IESO will continue to manage Ontario's integrated power system and wholesale electricity market.

IESO analyses will provide the OPA with support in planning for generation and transmission additions. Over the longer term, the government's plan to phase out coal by 2014 will provide environmental benefits to the people of Ontario through a significant reduction in greenhouse gas emissions. The IESO will play a significant supportive role in enabling this transition.

Over the planning period, the IESO will work to improve the reliability and security of the integrated power system while continuing to work with stakeholders to address improvements to the existing market processes and procedures.

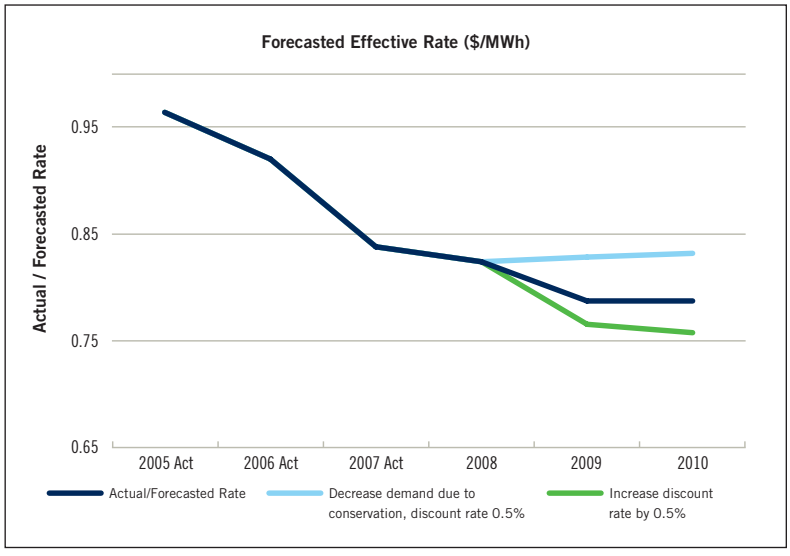
Financially, management practices will continue to be based on the objective of demonstrating prudent financial management while achieving the IESO's corporate objectives. Based on current projections, the IESO anticipates that its total costs will go down moderately in 2008. This would mark the fifth consecutive year that the IESO will have reduced its total costs. It is in part due to these total cost reductions that the IESO is proposing: a further two per cent fee reduction in 2008, to 0.799 $/MWh. This will represent a tangible and direct increase in value for money for IESO customers.



IESO total costs have declined each year since 2003 and are forecasted to further decline over the business planning period.

In 2009 the IESO predicts a reduction in total costs of approximately $7 million. Based on these total cost reductions and current demand forecasts the IESO is currently forecasting that it will be able to make a further fee reduction over the course of the business planning period. Based on current projections, the IESO forecasts projected customer savings from fee reductions of almost $22 million over the course of the three-year business planning period.

It is important to note that forecasts, by their nature, rarely reflect actual results. Certain factors that contribute to the IESO's forecasted revenues and costs are beyond Management's control. For example fluctuations in long-term interest rates and equity market returns can either positively or negatively impact IESO revenues and costs. Similarly deviations in actual energy demand from forecasted energy demand has a direct impact on IESO revenues. To better manage these fluctuations, the IESO maintains a surplus account of up to $5 million, refunding any excess to ratepayers in the form of a market rebate. The surplus account allows the IESO to provide customers with a higher degree of rate stability.



Fluctuations in external factors such as total demand and long-term interest rates may have an impact on the IESO's fee in 2009 and 2010.

DEVELOPING ONTARIO'S ELECTRICITY MARKET

The IESO operates and settles Ontario's $10 billion electricity market, bringing together almost 300 buyers and sellers of electricity. Every five minutes, the IESO balances the supply and demand for electricity across the province and establishes a market clearing price. In addition, the IESO is responsible for procuring a wide range of ancillary services to manage power quality, load following and contingency needs. In support of this service the IESO issues approximately 165,000 settlement statements each year.

The IESO issues approximately 165,000 settlement statements each year as part of clearing Ontario's $10 billion electricity market.

Ontario's electricity market is a means to promote economic efficiency by pricing and supplying electricity in a competitive manner and publishing price signals to guide consumption and production decisions. Competitive markets also promote reliability. The evolution of the electricity market will help determine how the province meets its needs for sustainable and reliable electricity service. To this end, the IESO is committed to making ongoing market improvements while also building toward a future where consumers will assume fewer financial and development risks associated with generation investments than they do today. At the same time, it will be important to ensure that the Ontario market structure remains compatible with the broad regional markets within which Ontario resides, maintaining the benefits of interconnected operation.

Highlights from 2007

The IESO continued to work to ensure that the market evolved in a manner that encouraged reliable supply and improved economic efficiency.

A significant undertaking in 2007 has been the IESO's acquisition and deployment of the smart metering meter data management and repository systems (MDM/R). Smart meters, a major government initiative, will provide the bridge connecting consumers to pricing that better reflects system and market conditions. In its recently-named capacity as the SME, the IESO will have responsibility for the administration and operation of the MDM/R, including the collection, validation, and estimation of energy consumption data. The IESO will also work with the Ministry of Energy and LDCs to develop communications to support the Ontario-wide roll-out of smart

meters, which is scheduled to be completed by the end of 2010. SME funding, together with the IESO internal and contracted expenses, will be recovered through a separate regulatory mechanism from the IESO usage fee for managing Ontario's integrated power system. This mechanism will be independent of the IESO's usage fee that is charged to wholesale market participants.

Smart meters will allow residential customers to conserve energy and adjust consumption based on price signals.

Photo courtesy of Hydro One.

As of August 1, 2007, the IESO Board of Directors had approved four amendments to the market rules in the following areas: reducing market participant prudential support requirements, relaxing restrictions on revisions to dispatch data submissions, clarifying market participant reliability standards obligations, and aligning market participant emergency preparedness obligations with industry practice. These amendments reflect the IESO's ongoing work to make business simpler and less expensive for market participants. In September 2007, the IESO implemented a rule amendment reducing generator ramping rates assumed in the Ontario uniform price calculation from 12 times to three times. This was done to provide more accurate signals for consumers and producers and to reduce uneconomic exports out of Ontario. As part of the implementation, the IESO will review the effect of the ramp rate change as compared to the expected benefits. In addition, by the end of 2007, the IESO expects to amend the market rules governing operating reserve requirements, which would improve market efficiencies.

Another achievement in 2007 was the release of the inaugural edition of the Ontario Market Outlook. Released at the time of the five-year anniversary of the opening of the Ontario electricity market, the Ontario Market Outlook provided stakeholders with an overview of market conditions as well as future market opportunities. A key finding of the report was that Ontario's annual wholesale electricity price has declined since the market opened, after adjusting for fuel price increases – one potential outcome of improved efficiency.

Looking Forward

Over the course of the business planning period, the IESO will work closely with stakeholders, government, and the OPA to chart out a path that will see the market evolve for the benefit of stakeholders and the province. Future enhancements will be driven by stakeholder views on how the market can provide value and facilitate their activities, and will focus on strengthening the ability of the market to signal economically efficient decisions within the industry. Initiatives are

aimed at providing improvements over the status quo that represent valuable additions when implemented, while also providing enduring value in light of potential market evolution.

The most significant initiative underway for the business planning period is the design and implementation of a day-ahead market (DAM). The IESO is currently examining the benefits and costs of developing a DAM in Ontario's current electricity industry environment, and is expected to have a recommended path forward established. The development of DAM is expected to be the main focus of IESO market evolution initiatives over the first two years of this Plan, involving significant stakeholder consultation and efforts.

Market evolution initiatives that could follow the DAM would fall under two broad categories. The first category relates to improvements in real-time operation and market signals; the second focuses on market drivers going forward in time - the longer-term reliability-based market mechanisms that might be used to address resource adequacy. Whether the focus will be on moving "in" from day-ahead to real time, or moving "out" from day-ahead to how the market prepares for the future will depend on many factors. They include experience gained throughout DAM development, OPA and industry progress on the development of load serving entities (LSE), results from the Ontario Energy Board (OEB) review of the IPSP, recommendations and findings of the Market Surveillance Panel, and most importantly, stakeholders' expressions of how the market can be made to better meet their business needs.

Moving "in" from day-ahead to real time: a DAM should enable changes to the real-time market. Operation under a DAM would decrease the focus on the real-time price for much of the industry, including the vast majority of consumers and would represent a major shift in the market. Today's real-time market would assume the role of a balancing function and would be the primary driver for the relatively small subset of stakeholders who have the flexibility to respond to real-time conditions. It would also provide incentives for less flexible participants to operate reliably in real-time, consistent with their day-ahead expectations. In such an environment, the real-time market can and should evolve such that it sends strong market signals to those that can respond to them, increasing the efficiency of the industry and aligning market interests with the needs of reliable operation. The two main issues that would be examined in these initiatives would be the extent to which prices should be impacted by transmission congestion, and how real-time prices should react to shortage conditions.

Moving "out" from day-ahead to preparing for the future: a DAM provides a platform to facilitate further evolution of Ontario's electricity market. Most consider DAM as a key enabler of LSEs, which are currently being investigated by the OPA. If LSE development progresses, an important step may have been taken towards creating a self-sustaining market-based industry. In other jurisdictions with LSEs, the responsibility for sufficient forward resource adequacy is apportioned out from a central authority such as the OPA, to the LSEs and those market participants who are willing and able to manage their own electricity procurement. How such forward responsibilities are allocated, whether ancillary market mechanisms such as capacity markets or option contracts are needed to augment whatever bilateral contracts participants have arranged, and how the IESO would be confident that forward commitments were adequately addressed, would be key questions for these market evolution initiatives.

RESPONDING TO THE NEEDS OF IESO STAKEHOLDERS

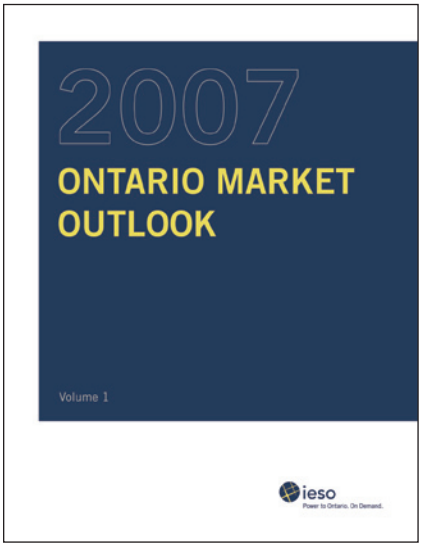
The IESO operates in a complex environment with many stakeholders that often have divergent interests. The need to obtain and consider stakeholder input in a meaningful way is an integral part of the IESO's business strategy and business activities. This is particularly important where IESO decisions and actions can have a significant impact on stakeholders.

IESO actions and decisions must be receptive to views and opinions of its stakeholders, and the process of arriving at these decisions must be accommodating of this. Thus, stakeholder engagement, the process by which stakeholder views and requirements are identified and factored into decisions, is a fundamental component of IESO decision making.

Highlights from 2007

The IESO has made significant efforts to improve stakeholder relations. In 2005, the IESO introduced a new stakeholder engagement process and a set of principles to guide stakeholder engagement activities. Since then, the IESO initiated almost 50 stakeholder engagements resulting in significant stakeholder input on a wide range of initiatives. Two years later, the IESO initiated a review of the process, principles and practices as part of its ongoing commitment to open and effective stakeholder dialogue. The review, to be conducted by an external consultant, will incorporate stakeholder input to identify opportunities for improvement.

IESO stakeholders are increasingly requiring well researched and forward-looking analyses of policies and development of alternatives to support market development proposals. To respond to this need the IESO reallocated existing staff to form a Market Evolution Analysis and Research (MEAR) unit. The MEAR unit provided substantial analysis in support of the three times ramp rate rule change, helped produce the IESO's inaugural edition of the Ontario Market Outlook, which provided stakeholders with a broad assessment of market performance, identified future market opportunities and established a methodology for preparing cost-benefit analyses of initiatives.



The inaugural edition of the Ontario Market Outlook provided stakeholders with a broad assessment of market performance and identified future market opportunities.

The IESO strives to provide stakeholders with access to timely and relevant information. The most recent customer survey recognized IESO achievements in this area, especially in the area

of communications. In 2007 the IESO continued to make improvements to the quality and quantity of information available through its public website.

Ontario electricity stakeholders include market participants, industry associations, neighbouring interconnected systems and markets, government, regulators and every Ontario electricity customer. The needs and expectations of market participants have become increasingly complex and sophisticated as they have gained market experience. This creates additional responsibility for the IESO to develop new processes, expertise and skills to help customers be more successful through market participation.

While some stakeholder sectors are actively involved in IESO stakeholdering, others are not. Consumer representatives have expressed some difficulty in getting meaningful participation from all of their constituents. To address this challenge, the IESO has established a Consumer Forum to create an opportunity for electricity users and associations to provide their input on key electricity market initiatives and to discuss matters of interest with the IESO. The Consumer Forum will also assist the consumer representatives on the IESO's Stakeholder Advisory Committee in representing their sectors at that Committee. The Consumer Forum is intended to help foster open and positive discussion between interested consumers and the IESO.

The IESO has also expanded its customer education efforts designed to help those customers paying the market price for electricity to better manage their electricity costs. Partnerships have been developed with a number of trade and industry associations including municipalities.

Looking Forward

In direct response to the most recent customer survey, the IESO took action to improve its market participant interface. The IESO began to phase-out the old Public Key Infrastructure (PKI) interface and to replace it with a more user-friendly secure log-in.

Over the course of the business planning period, the IESO will continue to periodically review its stakeholder engagement program, seeking stakeholder comment to identify any areas for improvement. Customer education efforts will also continue in 2008 with a focus on those customers who will be introduced to market-based pricing.

JUST ADMINISTRATOR AND CAPABLE ADVISOR

Confidence in the IESO-administered markets is reinforced by the IESO's administration and monitoring of these markets in an accurate and transparent manner. The IESO is charged with the responsibility to ensure that all participants, including the IESO, adhere to the market rules. Participants' confidence in the market is enhanced by knowing there is a level playing field and that the system operator and all participants will be held to the same standard of conduct in the market.

The IESO operates its business within the framework of risk management, which includes the setting of objectives, decision making, and other IESO management responsibilities. It considers external, strategic, operational, and financial risks and opportunities across the business and their potential impact on achieving its corporate objectives. This process enables Management to determine and validate the appropriate actions and initiatives to be undertaken given the risk profile, the business environment and the IESO's corporate objectives and priorities.

Proper corporate governance pervades all aspects of the business. This helps the IESO achieve its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes. The IESO, as a public purpose entity, fully appreciates the importance of accountability, fair dealing, transparency and ethics. Both internal and external audits help the IESO improve and maintain an effective control environment that provides the overall structure and tone within which IESO employees can perform their responsibilities.

Highlights from 2007

Customers have indicated a strong confidence in the IESO's ability to reliably manage the IESO-controlled grid. As mentioned earlier, a 2006 Reliability Readiness Audit conducted by NERC, affirmed the IESO's strength in this area, citing the IESO for three noteworthy "examples of excellence".

In its 2006 Annual Report on Compliance Enforcement, the IESO's arm's-length Market Assessment and Compliance Division reported on the heavy reliance it places on Alternative Case Resolution to promote compliance with the market rules. The Alternative Case Resolution approach to addressing potential breaches is typically less resource intensive for market participants and also leads to quicker resolution than resorting to formal investigations. The approach has been developed over time in partnership with market participants. The report underscored the importance of oversight of the Ontario electricity market in protecting the integrity of the market and ensuring a smooth functioning of the sector to the benefit of all Ontarians.

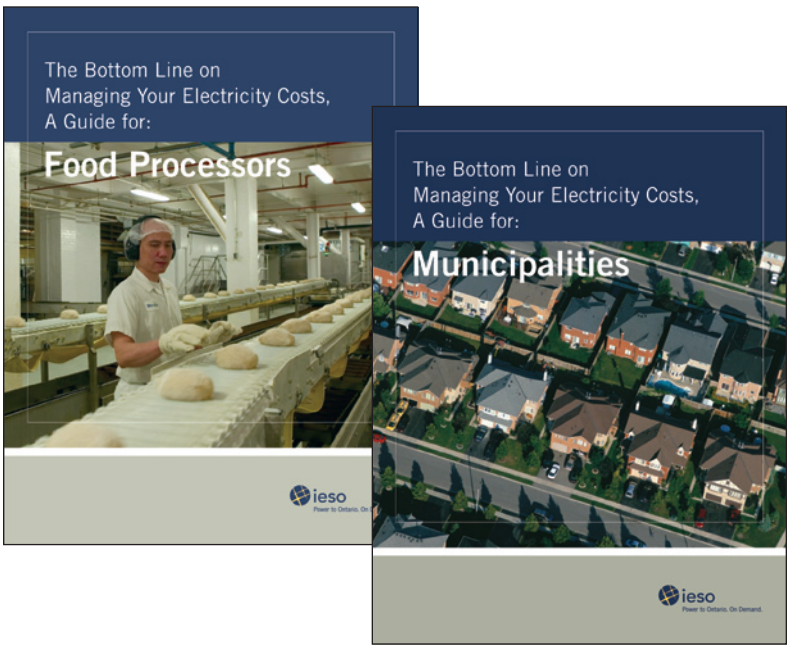
In its role as a capable advisor, the IESO has successfully coordinated activities between the OPA and itself, and its support of OPA procurement initiatives. This has included: providing formal input to the OPA consultation processes, IPSP support, internal and external integrated project tracking (projects of material impact on reliability) and issue identification and management. As well, the IESO has established relationships with proponents who have been selected as part of the government and OPA request for proposal processes.

Looking Forward

The IESO will continue to strive to earn stakeholders' confidence through open, impartial, and timely advice on matters within its mandate. Further, the IESO will build on the existing structural independence provided by an independent board of directors, the arm's-length Market Assessment and Compliance Division, the independent role and instruments set out in the *Electricity Act, 1998*, and the market rules.

In support of this objective, the IESO will:

- Continue to independently make available market and system operations information and analysis so that stakeholders, both government policy makers and market participants, are in a position to make decisions based on the facts;
- Provide timely advice and notice when issues or additional required actions are identified through the monitoring of the progress of infrastructure change;
- Partner with industry and trade associations to provide those customers paying the wholesale price for electricity with the information and tools they need to better manage their electricity costs;



In partnership with industry and trade associations, the IESO provides customers with the information and tools they need to better manage their electricity costs.

- Focus on targeted two-way contact with customers in specific sectors through partnerships with business/trade associations in providing information and interactive forums;
- Intervene in all leave-to-construct applications submitted by market participants to the OEB to provide impartial assessments with respect to reliability and market impacts of proposed projects;
- Communicate openly the IESO's actions taken and concerns on all matters related to the achievement of its goals and objectives;
- Represent and advance IESO and Ontario interests in regulatory proceedings and industry developments, while anticipating and assessing policy developments that will impact the IESO-administered markets, IESO-controlled grid or the IESO's ability to fulfill its obligations; and
- Work closely with the government to contribute to and act on energy policy in a way that serves the long-term interests of Ontario, evolving pragmatically toward the vision for the electricity market.

Achieving recognition as a capable advisor requires capable employees. This is especially true at the IESO, where a large percentage of its employees are highly educated professionals. Over the course of the business planning period many of these employees will become eligible for retirement. The IESO has had in place for some time a number of programs to ensure that its next generation of employees are well-equipped to provide the sophisticated services and advice required by our stakeholders and market participants. The IESO will continue to focus on achieving a work environment that attracts new employees and that provides a stimulating and challenging environment that encourages talented employees to remain with the organization.

The IESO is committed to ensuring that all employees possess the necessary expertise to address the needs of its stakeholders.

FINANCIAL OVERVIEW

The IESO's fiscal management continues to be based on a simple objective – to demonstrate continued prudent financial management while achieving its corporate objectives, including, managing the provision and implementation of Ontario's Smart Meter Data Management and Repository System (MDM/R), as the Smart Metering Entity.

For ease of use the financial section of this business plan has been separated into two sections. Section A contains the financial overview relating to the IESO usage fee, as it relates to the wholesale market, whereas Section B contains the financial outlook relating to the Smart Metering Entity. Consolidated financial statements can be found in Appendix 1.

SECTION A:
FINANCIAL OVERVIEW RELATING TO THE IESO USAGE FEE

PROJECTED 2007 FINANCIAL RESULTS

The second quarter projected 2007 financial results show the continued commitment of management to operate in a financially prudent manner. Overall the 2007 projected results are essentially in line with the budget for the 2007 fiscal year that appeared in last year's Plan. These results reflect lower than expected energy usage levels and long term interest rates which resulted in lower usage fee revenues and higher pension expense. These variances were more than offset by successful management of IESO's operating and capital program, resulting in lower than budgeted total costs.

2007 Projected Operating Results

($ millions)	2007 Projected	2007 Budget	Projected Variance
Usage Fees	131.2	133.4	(2.2)
Market-related Interest Income	4.2	4.6	(0.4)
Cost Recovery for Services	2.0	2.0	–
Total Revenues	**137.4**	**140.0**	**(2.6)**
OM&A Program Costs	87.6	89.4	1.8
OM&A Pension Expense	16.8	13.8	(3.0)
Amortization	28.7	32.9	4.2
Net Interest	3.9	3.9	–
Total Costs	**137.0**	**140.0**	**3.0**
Operating Surplus	**0.4**	**–**	**0.4**
Accumulated Operating Surplus[1]	**5.4**	**5.0**	**0.4**

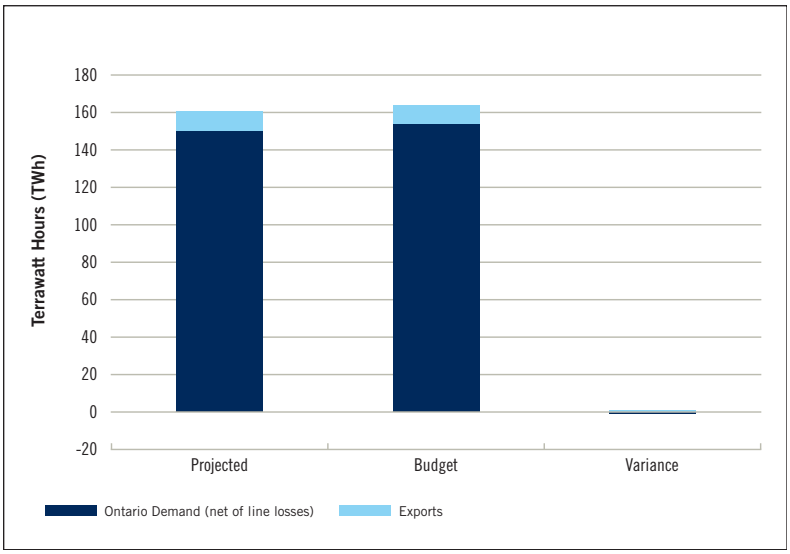
Overall, the 2007 projected operating results would result in an accumulated operating surplus of $5.4 million by year-end. This is determined by taking this year's projected surplus of $0.4 million and adding last year's actual accumulated surplus of $5.0 million.

Consistent with the proposal that was accepted by the OEB in the 2007 rate application, the IESO will rebate to market participants any accumulated surplus over $5.0 million. Accordingly, the IESO is projecting a rebate of approximately $0.4 million, to be distributed to market participants in the first quarter of 2008.

1 The accumulated operating surplus is presented before the rebate of any balance in excess of $5.0 million.

Usage Fees

Projected usage fee revenue for 2007 is $131.2 million, approximately $2.2 million lower than budget. This variance is a result of lower projected energy volumes within the IESO-Administered Markets. The current forecasted energy volumes for 2007 are 161.0 TWh, or a net 2.6 TWh lower than the energy levels used for 2007 planning. The following chart outlines those variances:



TWh	2007 Projected	2007 Budget	Projected Variance
Ontario Demand (net of line losses)	149.8	153.4	(3.6)
Exports	11.2	10.2	1.0
Total[2]	**161.0**	**163.6**	**(2.6)**

As outlined in the table, the projected variance in usage fee revenues is a result of lower projected domestic demand, slightly offset by higher exports.

The 2007 forecast energy volumes are based on the IESO's most recent 18-month outlook and represent actual volumes to the end of July 2007 and forecast amounts for August through December 2007.

2 Transmission line losses are taken as 3% of the Ontario Demand Forecast. The calculation of exports for forecasting purposes is based on a three-year moving average.

Market-related Interest Income

Market-related interest income represents the interest earned through the IESO-Administered Markets settlement clearing bank accounts. There are two ways that interest on market funds can accrue to this IESO account:

- In the settlement of the market, funds collected from owing market participants (i.e., buyers) are then paid to the receiving market participants (i.e., sellers) two business days later. In the period between receipt and disbursement of market funds, the monies are invested. The interest earned accrues in the settlement clearing account.
- Market participants make periodic prepayments and the IESO invests these monies, with interest accruing to the settlement clearing account.

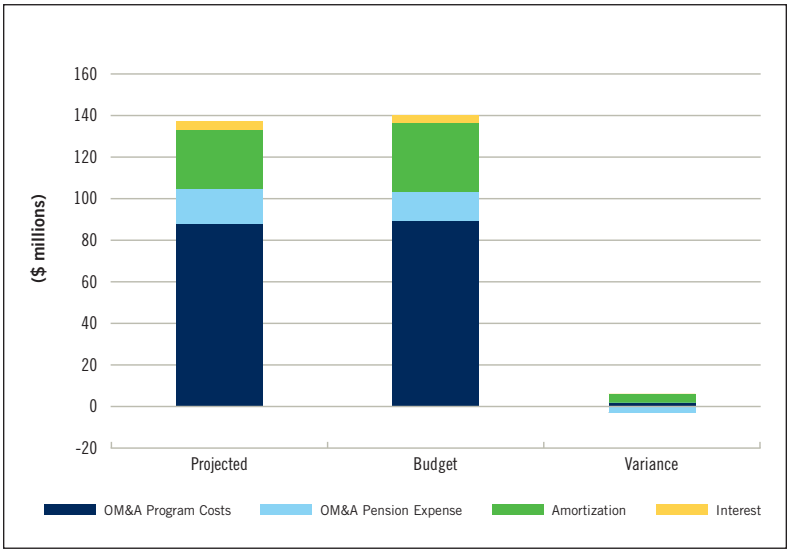
The projected 2007 revenues of $4.2 million are derived from the interest earned on the above-described funds, net of interest paid on borrowings required to settle the market. The unfavourable variance of $0.4 million relative to budget is principally a result of higher than expected interest paid on borrowings.

Cost Recovery for Services

Cost recovery revenue represents fees the IESO charges for services provided that are charged on a cost recovery basis. In 2007, those fees are projected to be $2.0 million and represent work on connection assessments ($1.5 million), support to the OPA ($0.4 million) and training ($0.1 million). Although there has been a minor shift in cost recovery activity from connection assessments to support to the OPA ($0.1 million), there is no projected variance in this revenue account.

TOTAL COSTS

The following chart outlines the projected 2007 total costs, including a comparison to the OEB approved budget:



($ millions)	2007 Projected	2007 Budget	Projected Variance
OM&A Program Costs	87.6	89.4	1.8
OM&A Pension Expense	16.8	13.8	(3.0)
Amortization	28.7	32.9	4.2
Net Interest	3.9	3.9	–
Total Costs	**137.0**	**140.0**	**3.0**

In 2007, projected total costs are approximately $137.0 million, an amount that is $3.0 million, or 2.1%, below the approved budget of $140.0 million.

OM&A Program Costs

The following table outlines the projected 2007 OM&A program costs relative to budget.

($ millions)	2007 Projected	2007 Budget	Projected Variance
Staff Costs	59.7	61.5	1.8
Computer Support, Maintenance & Equipment	9.5	10.3	0.8
Contract Services & Consultants	8.3	7.6	(0.7)
Administration	6.9	6.7	(0.2)
Telecommunications	3.2	3.3	0.1
Total OM&A Program Costs	**87.6**	**89.4**	**1.8**

Staff costs

Staff costs represent all operating costs associated with staffing, excluding pension expense. For 2007, staff costs are projected to be $59.7 million, or $1.8 million below the approved budget of $61.5 million. This spending variance largely reflects cost savings achieved through the effective management of hiring regular and temporary staff, as well as realized labour savings through minor organizational realignments.

Computer support, maintenance and equipment costs

Projected computer support, maintenance and equipment costs are $9.5 million in 2007, or $0.8 million below the approved budget. This variance is a result of lower than usual spending in services and software in areas, such as system change requests, lower priority problems and support of applications in areas such as records management, finance and metering. In 2007, the delivery of critical IT infrastructure and other capital projects were successfully prioritized. As a result, ongoing operating demands were met with less than expected costs.

Contract services and consultants

Projected contract services and consultants are $8.3 million, or about $0.7 million above the 2007 budget of $7.6 million. This variance is a result of numerous minor differences from the plan, including: increased intervenor and legal costs relating to 3x ramp rate, contract services working on OPA recoverable work, network management review, procurement process review and a recruitment audit.

Administration costs

Membership fees and facility costs including rent, utilities, building services and property tax make up the majority of the administration costs. The projected administration costs are $6.9 million, or $0.2 million higher than the approved 2007 budget. The majority of this variance is due to increased membership fees paid to NERC/NPCC, with slight offsets in building services costs.

Telecommunication costs

Projected telecommunication costs are $3.2 million, essentially in line with the $3.3 million budget.

OM&A Pension Expense

The projected OM&A pension expense for 2007 is $16.8 million or approximately $3.0 million higher than budget. This reflects a continued decline in the discount rate (determined by reference to high quality long-term corporate bonds). As a result, the actual discount rate utilized for the 2007 pension expense was 5.0%, below the 5.6% assumed in the 2007-2009 Business Plan.

Amortization

The projected amortization costs for 2007 are $28.7 million, or approximately $4.2 million lower than budget. This variance results from lower than planned capital spending in the year, combined with a revision to the service lives of several major market assets. The changes in service lives reflect the current capital plan to upgrade the existing tools in future years. The details of the IESO's capital program are included later in this section.

Net Interest

Net interest expense is projected to be on budget at $3.9 million.

Accumulated Operating Surplus

The accumulated operating surplus at the end of 2007 is projected to be approximately $5.4 million, resulting from:

- A projected operating surplus of $0.4 million in the year
- The opening balance of $5.0 million

As outlined earlier in this Plan, a closing balance of $5.4 million would result in a rebate of $0.4 million to market participants in 2008.

2007 PROJECTED BALANCE SHEET

The following chart shows a summarized projected balance sheet as at December 31, 2007, compared to the 2007 budget.

($ millions)	2007 Projected	2007 Budget	Projected Variance
Cash, Cash Equivalents and Temporary Investments	7.8	9.1	(1.3)
Accounts Receivable and Short-term Prepaid Expenses	21.9	20.4	1.5
Current Assets	**29.7**	**29.5**	**0.2**
Property and Equipment	101.0	105.0	(4.0)
Long-term Investments	16.6	15.3	1.3
Prepaid Pension Expense	3.7	6.8	(3.1)
Total Assets	**151.0**	**156.6**	**(5.6)**
Accounts Payable, Accrued Liabilities and Accrued Interest	20.0	20.0	–
Debt	81.2	88.2	(7.0)
Rebates to Market Participants	0.4	–	0.4
Accrual for Employee Future Benefits other than Pension	42.1	41.5	0.6
Total Liabilities	**143.7**	**149.7**	**(6.0)**
Accumulated Operating Surplus	5.0	5.0	0.0
Accumulated Market-related Penalties and Fines	2.3	1.9	0.4
Total Liabilities and Surplus	**151.0**	**156.6**	**(5.6)**

Material projected balance sheet variances relative to budget

- The projected total property and equipment balance at the end of 2007 is $101.0 million, an expected $4.0 million below the budgeted level. This variance is due to 2007 capital spending which is projected to be $8.2 million below budget, offset by lower than budget amortization of $4.2 million. The projected capital project expenditures are outlined in the next section of this document.
- Projected total debt at the end of 2007 is $81.2 million, an amount that would be $7.0 million below budget. This debt reduction continues to reflect the successful execution of the IESO's financing strategy to minimize cash balances and repay long-term debt whenever possible, even earlier than budgeted when appropriate.
- Projected prepaid pension asset at the end of 2007 is $3.7 million, or $3.1 million below budget, due to the higher than expected pension expense in the year.

2007 CAPITAL PROJECT EXPENDITURES

In 2007, the IESO projects that capital initiatives will total $11.8 million, an amount that is approximately $8.2 million below the approved budget, as outlined in the following table.

($ millions)	2007 Projected	2007 Budget	Projected Variance
Day-Ahead Market	–	8.0	(8.0)
Energy Management System/Market Information System Upgrade	3.2	3.2	–
Windows Refresh Program Stage 4&5	1.8	2.5	(0.7)
UNIX Server Infrastructure Refresh	1.8	1.5	0.3
Backup Operating Centre Relocation	1.0	1.3	(0.3)
Application Changes/Vendor Change Requests	1.0	1.0	–
Facility Outage Management System	0.4	0.3	0.1
On-Line Limit Derivation	0.2	–	0.2
Other Capital Initiatives	2.4	2.2	0.2
Total Capital	**11.8**	**20.0**	**(8.2)**

As in prior years, given the ongoing need for changes and reprioritization, the IESO does not use the business planning process as a mechanism for capital project approval. Rather, through business planning, an appropriate capital envelope is established for future years. The following section outlines the variances among the business plan capital project assumptions. As well, it also outlines project deliverables, achievements and challenges for the larger projects undertaken in 2007.

2007 Capital Initiatives

Day-Ahead Market

In 2007 the IESO is undertaking design and stakeholdering activities in respect of a day-ahead market (DAM). This work is expected to lead to a decision by the IESO Board of Directors in late 2007 or early 2008. No capital expenditures are expected in 2007.

Windows Refresh Program (Stage 4 & 5)

The Windows Refresh Program is a program that includes multiple stages and is expected to see capital expenditures from 2005 to 2008. The program will see the replacement of the aging Windows server infrastructure (hardware and software), much of which no longer has vendor support, in order to reduce associated business risk and operational costs. Stage 4 will migrate the critical business applications to the new MS Window Server 2003 infrastructure and Stage 5 will migrate the remaining business applications.

Overall the projected $0.7 million variance in 2007 is a result of $0.4 million of Stage 4 activities being undertaken in 2006, earlier than planned, and Stage 4 projected to be completed on time at a cost of $2.4 million, or $0.3 million below budget. Stage 5 has a projected spend of $0.9 million in 2007 and will be completed in 2008 for a total cost of $1.8 million.

UNIX Server Infrastructure Refresh

UNIX Server Infrastructure Refresh is a program that includes three phases. The program is expected to see capital expenditures from 2005 to 2008. Overall, this program will see the replacement and upgrade of the existing UNIX server environment, an environment that hosts most of the market applications and is comprised of aging hardware. The total program has been submitted with an estimated total cost of $4.2 million, consistent with the 2007-2009 Business Plan. The cost estimate included in the 2007-2009 Business Plan for Phase 2 related to the replacement of the Oracle database servers, the replacement of the Domain Name Servers and the creation of Portal Remote Archetypes. In 2007, total projected costs are $1.8 million, $0.3 million higher than the business plan forecast as a result of some Phase 3 costs being moved forward into 2007.

As part of Phase 2, the Energy Management System (EMS) servers, the MVSTAR settlements servers and a number of smaller applications and web servers were replaced. This is the continued replacement of aging hardware and a move to a modern Operating System that will be supported until at least 2012.

In 2007 as part of Phase 3 there is the planned replacement of the System Data Repository (SDR) servers and Operational Data Store (ODS) servers, the Funds Administration servers and Market Operating System/Market Information Management (MOSMIM) systems. There are a number of smaller applications and web servers that will also be replaced in Phase 3. This Phase shares the same benefits as noted above of replacing aging hardware and the move to a modern Operating System.

Energy Management System/Market Information System (EMS/MIS) Upgrade

This project serves to upgrade the EMS/MIS applications. These applications largely represent the toolset the IESO is currently using to meet its role in maintaining the reliability of the IESO Controlled Grid (ICG) and the operation of the IESO Administered Markets (IAM). Having been in-service since 2001, these systems are nearing the end of their technological life. The current applications are either at or near their computational capacity limits and configured software boundaries. The EMS/MIS upgrade will provide capacity for growth to incorporate future functional improvements. Accordingly, to ensure the applications continue to reside on reliable infrastructure, the underlying hardware for the EMS/MIS applications is being upgraded as part of the UNIX Server Infrastructure Refresh program.

The result of this project will be an EMS/MIS that allows hosting on current infrastructure technology, applications that include required functionality enhancements, and an increased assurance as to the reliable operation of the EMS/MIS. Accordingly, the upgrade will extend the life of the current system assets from 2008 to 2011.

The Board-approved business case for EMS/MIS was $6.7 million. Due to timing changes, actual 2006 spending levels were lower than planned, shifting resources to 2007 and 2008. The project continues to forecast costs that are consistent with the approved business case.

Backup Operating Centre Relocation

The Backup Operating Centre Relocation was initiated in 2006, after a thorough investigation of suitable locations. The project was delivered in 2007 as planned, for a total cost of $2.4 million. The 2007 variance of $0.3 million was a result of some project activities being undertaken in 2006, earlier than anticipated.

Facility Outage Management System

The Facility Outage Management System (FOMS) project is proposed to replace the existing outage management applications which have reached the end of their service lives and address two high level requirements. The first requirement is to provide market participants with an automated means to provide the outage information that they are required to submit to the IESO. It will also provide them with additional information regarding the status of their planned outages. The second requirement is to reduce the cost of the outage management process for market participants and the IESO, by improving the efficiency of the process. In a first time endeavour, the IESO and ISO-New England (ISO-NE) agreed to jointly develop a significant portion of the FOMS.

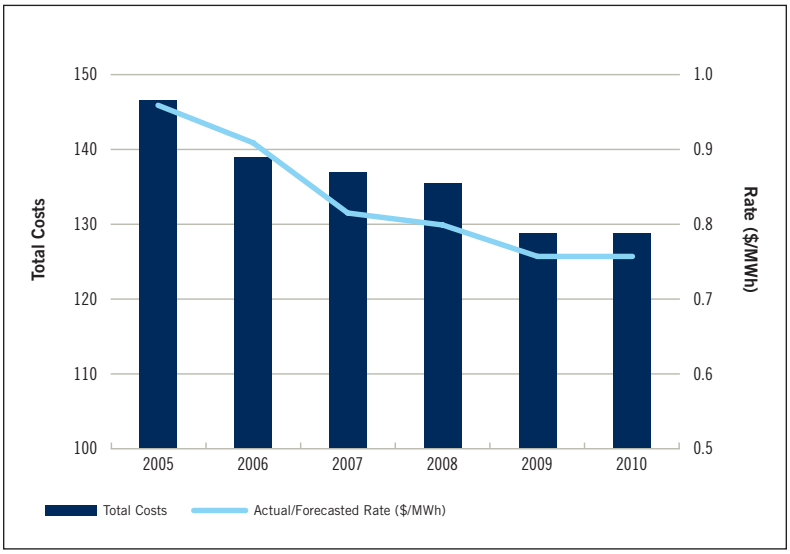
In 2007 the vendor advised ISO-NE and the IESO that the design work was revealing further potential for increasing both costs and schedule and that they were not confident that further discovery would not occur downstream, resulting in further adverse impacts. The parties agreed that this was not a suitable basis for continuing and stopped the work at that point.

The joint user requirements between the IESO and ISO-NE were completed as part of the design work and will provide a comprehensive basis for the selection of another vendor to complete this project.

FINANCIAL OUTLOOK 2008-2010

The financial outlook for the planning period 2008-2010 reflects strong cost management, successfully reflected in the IESO's proposed usage fee reduction of approximately 2%, or a projected usage fee of $0.799/MWh in 2008. This compares to a forecasted fee of $0.79/MWh for 2008 included in the 2007-2009 Business Plan. The IESO has been able to propose this fee reduction through:

- the continued successful management of business costs, including OM&A, amortization and interest, which resulted in these costs having an estimated total of $135.5 million in 2008, or some $1.7 million lower than was estimated for 2008 in last year's plan; and
- a slight increase in long-term interest rates, providing a modest reprieve from the constant increases in pension expense seen over the last number of years.



Key Assumptions over the Planning Period

Prior to reviewing the details over the period, it is important to ground these budgets and outlooks with the related assumptions. They are:

- Load forecasts used in calculating the usage fees over the plan horizon are based on the most recent 18-month outlook[3].
- The floating interest rate paid on the long-term debt, excluding the fixed rate debt with the Ontario Electricity Financial Corporation, will be 5.1% over the planning period.
- Pension expense for 2008 based on actual pension plan returns to the end of May 2007 with the 2009 and 2010 pension expense based on plan returns of 7.0%. This latter rate of return is consistent with the assumed expected long-term return on plan assets.
- Pension expense over the planning period based on a discount rate of 5.5%.

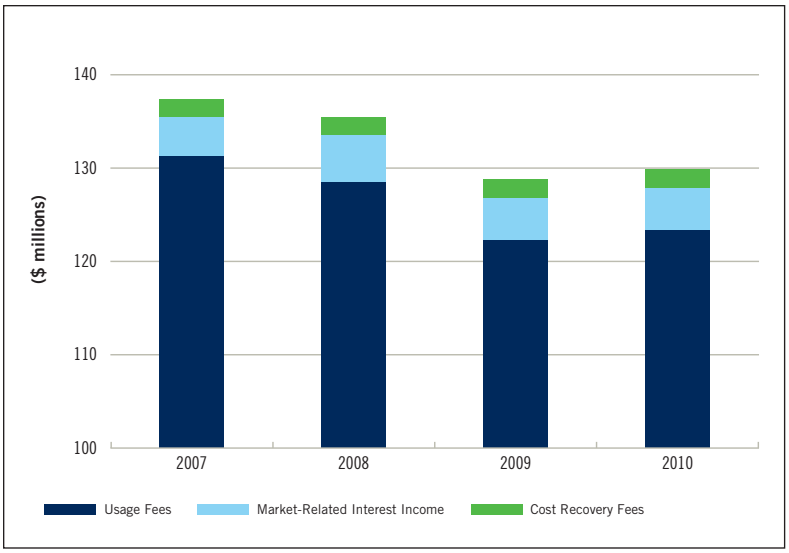
3 The forecasted energy demand levels that underpin the revenue forecast included in the plan are 160.8 TWh for 2008, 161.5 TWh for 2009 and 162.9 TWh for 2010.

The table below outlines the planned operating results over the planning period:

($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Usage Fees	156.9	144.7	131.2	128.5	122.2	123.3
Market-related Interest Income	3.5	4.9	4.2	5.0	4.6	4.6
Cost Recovery for Services	0.9	2.1	2.0	2.0	2.0	2.0
Total Revenues	**161.3**	**151.7**	**137.4**	**135.5**	**128.8**	**129.9**
OM&A Program Costs	83.3	83.1	87.6	89.9	93.9	95.1
OM&A Pension Expense	8.3	17.3	16.8	11.3	9.0	7.3
Amortization	47.4	32.4	28.7	29.3	23.1	24.5
Net Interest	7.6	6.2	3.9	5.0	2.8	1.9
Total Costs	**146.6**	**139.0**	**137.0**	**135.5**	**128.8**	**128.8**
Operating Surplus/(Deficit)	**14.7**	**12.7**	**0.4**	**–**	**–**	**1.1**
Transfer to the OPA	(15.0)	–	–	–	–	–
Refund to Market Participants	(13.6)	(12.7)	(0.4)	–	–	(1.1)
Accumulated Operating Surplus	**5.0**	**5.0**	**5.0**	**5.0**	**5.0**	**5.0**

As shown above the accumulated surplus is projected to remain flat at $5.0 million throughout the business planning period.

TOTAL REVENUES: 2007-2009



($ millions)	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Usage Fees	131.2	128.5	122.2	123.3
Market-Related Interest Income	4.2	5.0	4.6	4.6
Cost Recovery Fees	2.0	2.0	2.0	2.0
Total	**137.4**	**135.5**	**128.8**	**129.9**

Projected total revenues are expected to decrease by approximately $1.9 million in 2008 from levels expected in 2007, due primarily to planned reductions to the usage fee.

Usage fee revenue

The forecasted usage fee revenues are expected to decrease by $2.7 million in 2008 from the current year projection, with further decreases of $6.3 million in 2009, and a slight increase of $1.1 million in 2010. The forecast reduction in 2008 reflects the proposed usage fee reduction from $0.815/MWh to $0.799/MWh. A slight decrease of 0.2 TWh from 2007 to 2008 is also assumed. The above revenue levels reflect the following energy forecasts:

- 160.8 TWh in 2008
- 161.5 TWh in 2009
- 162.9 TWh in 2010

As stated previously, these forecast energy levels are based on the most recent 18-month outlook.

($ millions)	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Outlook Demand Forecast	154.4	154.5	154.9	156.5
Less: Transmission Line Losses[4]	(4.6)	(4.6)	(4.6)	(4.7)
Exports[5]	11.2	10.9	11.2	11.1
Total	**161.0**	**160.8**	**161.5**	**162.9**

Market-related interest income revenues

The market-related interest income revenues, which represent investment income earned on market funds as they flow through the settlement cycle, are expected to increase slightly to $5.0 million in 2008 and then remain flat at $4.6 million in 2009 and 2010. This is a result of anticipated invoice volumes in each of the years and the expected interest rate.

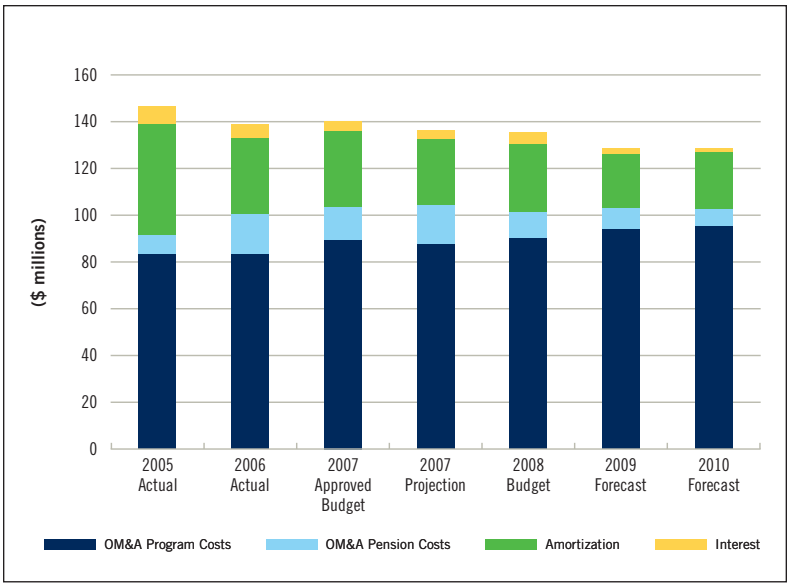
Cost recovery revenues

Cost recovery revenues (from connection assessments, support to the OPA and participant training) are expected to remain flat at $2.0 million per year over the planning period.

Since these revenues represent services that are provided at cost, there are corresponding costs within the OM&A program for these services. Accordingly, there is no net impact on the IESO for these services, and no impact on the market participant's usage fee.

4 Line losses are assumed to be 3%.
5 Exports assumptions are based on a three-year rolling average.

TOTAL COSTS: 2008-2010



($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
OM&A Program Costs	83.3	83.1	87.6	89.9	93.9	95.1
OM&A Pension Costs	8.3	17.3	16.8	11.3	9.0	7.3
Amortization	47.4	32.4	28.7	29.3	23.1	24.5
Net Interest	7.6	6.2	3.9	5.0	2.8	1.9
Total Costs	**146.6**	**139.0**	**137.0**	**135.5**	**128.8**	**128.8**

Over the planning period, it is expected that total costs will decrease in each year relative to the projected 2007 level.

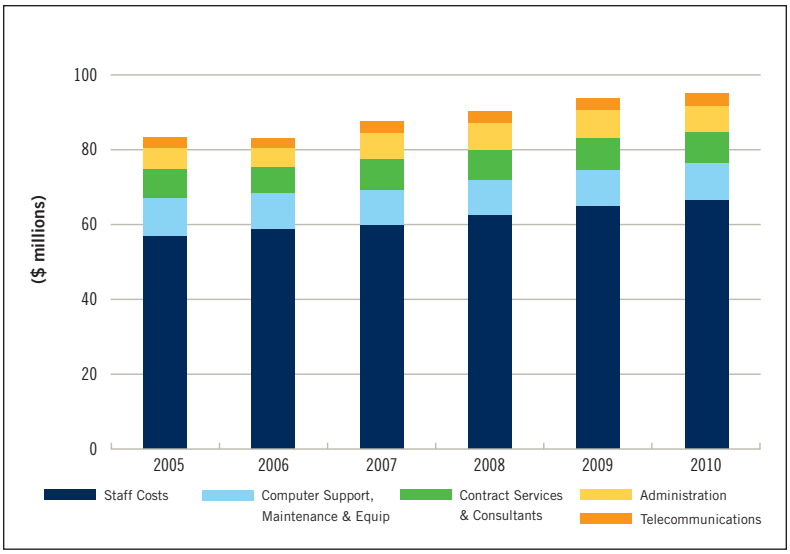
- In 2008, projected total costs of the business will decrease by $1.5 million, from $137.0 million to $135.5 million.
- In 2009, the forecasted total costs are projected to decrease further by $6.7 million, reflecting decreases in pension expense and amortization, and then to remain flat in 2010.

The net changes over the planning period reflect:

- Continued aggressive repayment of debt, thereby minimizing interest expenses;
- Prudent capital expenditure levels that will continue to drive a longer term reduction in amortization charges;
- Decreases in pension expense, resulting largely from increasing long-term interest rates and smoothed recognition of strong investment returns;
- Continued management of OM&A program costs to a level largely consistent with inflation, in an environment of ongoing challenges to meet the increasing demands of the business.

The following sections provide the detail and rationale for the changes in each area of cost.

OM&A Program Costs



The following table outlines the OM&A program costs over the planning period.

($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Staff Costs	56.7	58.7	59.7	62.4	64.8	66.5
Computer Support, Maintenance & Equipment	10.4	9.7	9.5	9.5	9.7	9.8
Contract Services & Consultants	7.7	6.9	8.3	8.0	8.7	8.3
Administration	5.7	5.1	6.9	6.7	7.3	7.1
Telecommunications	2.8	2.7	3.2	3.3	3.4	3.4
OM&A Program Costs	**83.3**	**83.1**	**87.6**	**89.9**	**93.9**	**95.1**

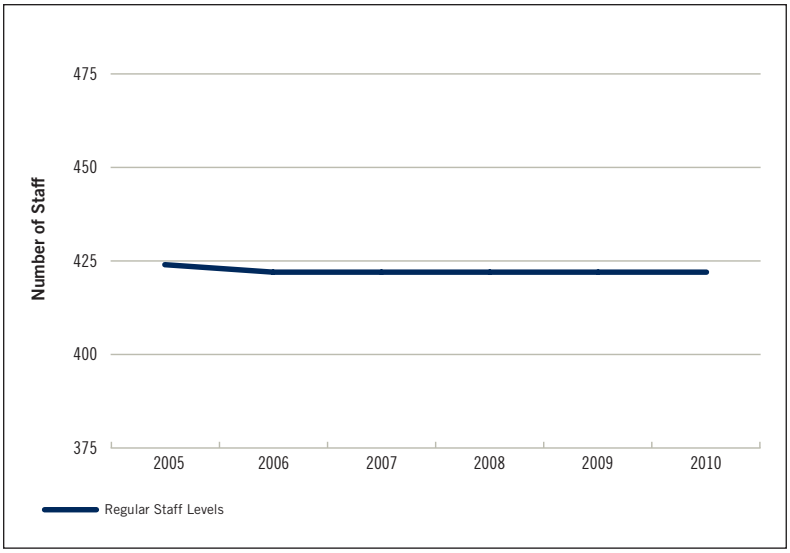
In 2008, OM&A program costs are budgeted to increase by $2.3 million, or by approximately 3% over the 2007 projection. As shown above, the primary reason for this increase relates to increases in staff costs ($2.7 million), offset somewhat by lower contract services & consultants ($0.3 million).

Staff Costs

The IESO continues to be a staff-intensive business. Over the planning period, staff costs represent almost 50% of the total costs and over 69% of the total OM&A program costs. This excludes OM&A pension expense, which although categorized separately nonetheless relates to regular staff. Factoring in the pension expense, staff-related costs account for over 54% of total costs in each year of the planning period.

The biggest challenge in the management of staff costs is the ever increasing demands on the IESO and its staff. Numerous developments within the sector continue to drive increased work in a number of areas. Examples of this include: an unprecedented amount of new electricity system infrastructure resulting from OPA procurements, proponent projects and the IPSP; high levels of investment in replacement and refurbishment of generation, transmission and load supply; increasing regulatory activity within Ontario and in the electricity sector across Canada and the U.S.; and overall governance demands related to the power system, the corporation and the IESO's pension plan.

In 2008, the first year of the plan, staff costs are budgeted to increase by about $2.7 million, or about 5%. This planned cost increase reflects compensation increases, primarily the result of current collective agreements, offset by continuous improvement and reprioritization of work and efficiency gains in the day-to-day activities that has allowed the increasing business demands to be met at a staffing level that remains the same as in 2007. In addition, there is a continued focus on the management of hiring lags and other workforce challenges. There are a number of ongoing initiatives and programs aimed to support the resourcing of staff including; on-campus recruiting, co-op programs, and internet-based resume management system.



The following table outlines the regular staff levels over the planning period:

($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Total Regular Staff Levels	424	422	422	422	422	422

Computer Support, Maintenance & Equipment

Computer support, maintenance and equipment costs are projected to remain flat in 2008 and to increase slightly over the planning period. These costs include annual support and maintenance fees for the market and operating systems, annual license renewals, as well as computer leases and consumables.

Contract Services & Consultants

Contract services and consultants are projected to fluctuate slightly in each of the planning years due mainly to different audits and reviews planned over the period. The majority of these costs are recurring annual expenses such as insurance, remuneration to Board, Panel and Committee members, audit and accounting fees, legal services, human resources services, communication products & services, as well as government relations functions and an allowance for an additional fee from the OEB beginning in 2008.

Administration[6]

Administrative costs are budgeted to decrease slightly in 2008 to $6.7 million and then rise again in 2009. The reduction in 2008 is largely due to the successful management of issues relating to NERC's compliance activities that are duplicative to the IESO's. As a result, the IESO realized a significant savings on NERC's assessments starting in 2008. Modest increases in NERC's assessments are expected over the remaining of the planning period.

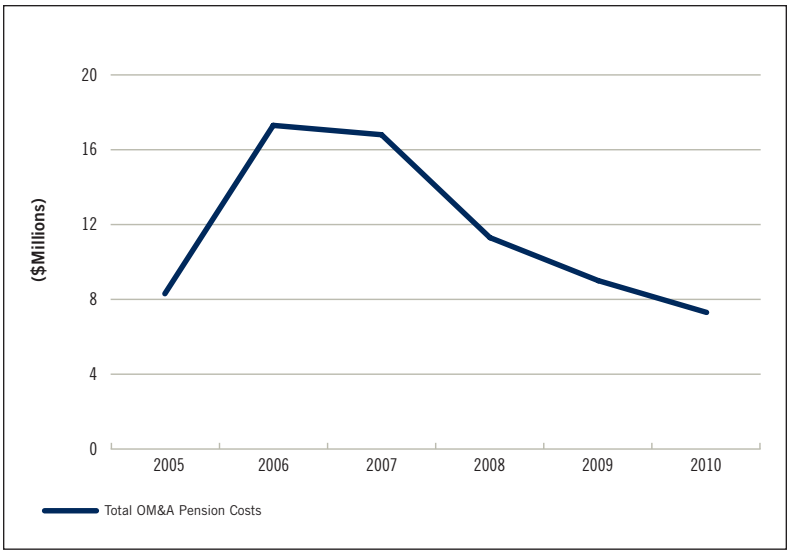
All other administration costs are expected to increase with cost-of-living changes with the exception of building services, which are expected to increase in both 2008 and 2009 due to required non-routine facility maintenance in those years.

Telecommunications

Telecommunication costs are budgeted to increase slightly over the planning period to reflect anticipated inflationary increases and further remote terminal unit (RTU) expansion.

6 Administrative expenses include memberships, rent, utilities, materials and supplies, rental facilities, building services, and property taxes.

OM&A Pension Expense



($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Pension Costs	8.4	17.8	17.3	11.9	9.6	7.8
Less: Capitalized Pension	(0.1)	(0.5)	(0.5)	(0.6)	(0.6)	(0.5)
Pension Expense	**8.3**	**17.3**	**16.8**	**11.3**	**9.0**	**7.3**

Pension expense represents the actuarially estimated cost of providing pension benefits to IESO employees, using cost calculation methods that are prescribed by the Canadian Institute of Chartered Accountants (CICA) and assumptions that reflect current long-term bond yields and management's best estimates for the future. This expense reflects the proper charge for pension in the financial statements, in accordance with Canadian Generally Accepted Accounting Principles (GAAP). Three factors that have a large influence on this expense are:

- the institutional arrangements in place;
- pension plan investment performance; and
- the critical assumptions used.

Institutional arrangements

In terms of institutional arrangements, the IESO has its own pension plan. Therefore, the pension expense charged through the usage fee is directly impacted by many variables, including fund performance and interest rate assumptions. Some organizations are part of a larger pension plan and their pension expense represents their required contributions to that plan. Those contribution levels are impacted by plan performance and changes to assumptions; however, the rate of change in annual pension expense is likely to be lower than that of an individual plan sponsor, like the IESO.

Pension plan investment performance

On pension plan investment performance, over the period 2002 through 2006, the plan earned an average annual return of 8.3%. These actual returns have exceeded both the benchmark (7.9%) and management's current annual long term assumed rate of return of 7.0%.

In recognition of the long-term nature of the obligations and the desire for a 'smoother' pension expense such that large fluctuations in the usage fee are mitigated, the IESO uses a smoothed value of assets in calculating the pension expense. As a result, the large positive equity investment returns of recent years have not yet been fully recognized in the smoothed asset values. Therefore, there are currently lower plan assets assumed to be available for investment, and this results in an assumption of lower investment earnings, resulting initially in larger pension expense reported. As the recent large positive equity returns are recognized in the smoothed value of assets over time, all else being equal, this will reduce the reported pension expense in future years.

Critical assumptions

The assumed long-term rate of return on plan assets remains at 7.0% per annum.

Pension liability – on the opposite side of the pension plan balance sheet is the pension liability. That liability represents the actuarially estimated, present value liability of the pension promises accrued to date for IESO employees and retirees. This estimate is impacted by factors including:

- Pension plan benefit provisions
- Long-term interest rates
- Plan membership
- Mortality assumptions
- Other demographic and economic assumptions and experience

The pension plan provisions have not increased. In fact, certain changes have been made to reduce employer-paid pension benefits. In 2007, the employee contribution rates were increased for The Society of Energy Professionals employees and Management Group employees. For Management Group employees who are hired on and after January 1, 2007, pensions are based on best five-year average earnings (instead of best three-year average earnings), employees are entitled to an unreduced early retirement pension once the sum of their age and service exceeds 90 years (instead of 84 years), and retiree pensions are indexed at 75% of the Ontario CPI (instead of 100%).

Long-term obligation – since this is a long-term obligation, there is an assumption made as to what interest rate to use to present-value the obligation. That interest rate is referred to as the discount rate and, according to Canadian GAAP, that rate should reflect the yields on high quality corporate long bonds in effect at the time of measurement.

Measurement date – the measurement date is September 30. For planning purposes, the discount rate in effect at the beginning of the planning process is used, and is then, subject to materiality considerations, revised on the measurement date. Over the last few years, long-term discount rates have dropped significantly, however, as of June 30, 2007 they have recovered somewhat. The effect of this change is a budgeted decrease of some $3.4 million to the pension expense in 2008.

Legislative requirement – there is a legislative requirement of all pension plan sponsors to undertake a complete actuarial valuation of the plan at least every three years. This valuation helps ensure appropriate funding of the pension promise. In 2005, the IESO undertook an actuarial valuation, which presented an opportunity for a true-up of the plan's demographic status to that assumed by the actuaries between valuations. There will be no further true-ups until the next valuation date which is scheduled for 2008.

The following table summarizes the details of the change in projected pension expense in 2008 from 2007.

($ millions)	Current Service Costs	Interest on Benefit Obligation	Expected Return on Assets	Amortization of Experience & Plan Improvements	Total
Projected 2007 Pension Costs	9.5	19.8	(19.6)	7.6	17.3
Expected Developments	0.3	1.2	(1.6)	(0.9)	(1.0)
Fund Performance	–	–	(0.4)	(0.6)	(1.0)
Change in Discount Rate	(1.4)	0.4	–	(2.4)	(3.4)
Budgeted 2008 Pension Costs	**8.4**	**21.4**	**(21.6)**	**3.7**	**11.9**

Looking at 2009 and 2010, based on an assumption of no change in long-term discount rates and investment returns of 7% per annum, the pension expense is expected to decrease modestly each year, as there are fewer prior year experience losses, due to discount rate decreases, that need to be recognized and the large positive equity investment returns of recent years that are recognized in the smoothed asset values.

CAPITAL SPENDING

Over the planning period, the IESO intends to make business and tool improvements estimated to total:

- $20.0 million in 2008
- $20.0 million in 2009
- $20.0 million in 2010

This total three-year spending level of $60.0 million includes an anticipated spending level for the DAM in the order of $16.0 million. Excluding DAM, this budgeted or forecast spending level ($44.0 million) is consistent with the actual and projected spending level of $40.2 million for the three-year period ending in 2007.

Given the ongoing need for changes and reprioritization, the business planning process is not used as the mechanism for capital project approval. Rather, through business planning, an appropriate capital envelope is established for future years. This practice is consistent with prior years. As well, the IESO recognizes the need for robust disclosure and information about the projects for which this capital funding will be utilized.

In recognition of this inherent conflict, the IESO has employed an approach to capital budgeting for the planning period that includes two distinct groupings of capital projects – key capital initiatives and other capital initiatives. Key capital initiatives represent the most critical capital projects over the planning period that the IESO believes must be completed within the timeframe identified in the following table. The other capital initiatives are also necessary projects, however, they are projects that either afford themselves to more flexibility in planning or delivery so timing is not as critical, or they are lower priority than some key initiatives. Stakeholders should expect that the IESO will deliver the key capital initiatives as scheduled and, over the life of the plan, will deliver the other capital initiatives.

As an example, the DAM has been assumed to be built and implemented in 2008/2009. If the project timing, deliverables or costs were different than the $16.0 million assumption that is evenly split between 2008 and 2009, then some of the resourcing for other capital initiatives might move ahead or be deferred.

Ultimately, the IESO believes this is a prudent and realistic manner in which to budget capital.

The following table provides more information on the capital plan.

($ millions)	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Key Capital Initiatives				
Day-Ahead Market	–	8.0	8.0	–
Energy Management System/ Market Information System Upgrade	3.2	1.1	–	–
Windows Refresh Program Stage 4&5	1.8	0.9	–	–
UNIX Server Infrastructure Refresh	1.8	0.5	–	–
On-Line Limit Derivation	0.2	0.5	1.0	1.0
Backup Operating Centre Relocation	1.0	–	–	–
Facility Outage Management System	0.4	0.8	–	–
NERC – CIP Program	–	0.2	0.2	–
Network Zoning Project	–	0.8	–	–
Participant Life Cycle Replacement	–	1.0	0.5	–
Other Capital Initiatives	3.4	6.2	10.3	19.0
Total Capital Spending	**11.8**	**20.0**	**20.0**	**20.0**

The planned capital spending level of $20.0 million in 2008 represents an $8.2 million increase from the 2007 projected level of $11.8 million.

Key Capital Initiatives

A number of the key capital initiatives within the planning period were started in 2007 and hence their descriptions are found earlier in this document.

Day-Ahead Market

A decision by the IESO Board of Directors on a DAM design is expected in late 2007 or early 2008, following a review of possible DAM designs throughout this fall. A decision to proceed with DAM would result in capital work beginning in the first half of 2008 and DAM operational by late 2009. The total projected capital spend is estimated at $16.0 million and is currently allocated evenly between 2008 and 2009. The project scope is based on maximizing use of existing processes while providing day-ahead pricing options to participants. The project costs and the timing are subject to variability depending on the final design. The DAM is expected to deliver:

- Improved efficiency of unit commitment to reduce the overall cost of supplying market demand;
- Improved operational signals to generators, which, among other things, should result in improved coordination of gas and electricity markets;
- The availability of better price signals for both consumers and producers to plan their business; and
- The ability for participants to lock in a price for their electricity and not be subject to the risks inherent in real-time operations.

On-Line Limit Derivation

The On-Line Limit Derivation project will be undertaken in several stages over the business planning period for a total projected cost of $2.7 million. The project is a response to mitigate identified risks in Market and System Operations, and essentially replaces much of the manual development of system operating limits with automated tools. The manual effort is very staff intensive and relies on staff expertise and judgment. The automated tools can operate on data provided in any time frame, from advance plans to real-time control room operation. Benefits of the project include; ability to manage substantial planned system infrastructure changes, increased ability to respond to unplanned system events, reduced constraints on generation dispatch and outage planning and increased security of operation.

NERC – Critical Infrastructure Protection (CIP) Program

NERC Standards CIP-002 through CIP-009 provide a cyber security framework for the identification and protection of Critical Cyber Assets to support reliable operation of the Bulk Electric System. These standards include a requirement to segregate the critical systems which support system operations and to protect these systems from cyber threats. To comply with these standards, the IESO projects to spend $0.4 million over the business planning period in developing the processes and procedures to manage and control these Critical Cyber Assets.

Network Zoning Project

The Networking Zoning project is a specific requirement under the NERC-CIP program. NERC CIP standards now require that the IESO's critical cyber assets all reside within its own Electronic Security Perimeter to provide an enhanced level of security, auditability, logging and access control. This project is being undertaken to implement defined network zones to provide a higher level of network isolation between these network segments. This zoning will be implemented by the use of network firewall devices separating these defined zones, with only the required data being allowed between zones.

This project will create infrastructure zones and the processes to manage the zones going forward, and the IESO projects to spend $0.8 million over the business planning period.

Participant Life Cycle Replacement

The Participant Life Cycle (PLC) system is the primary repository of market participant registration data at the IESO. The system is used to provide market participant data to critical market systems. The existing PLC has reached the end of its service life and needs to be replaced. The project will include a business process review to determine the required processes and procedures from several existing IESO registration processes to allow the IESO to ultimately leverage these into one new market participant registration information system. The PLC Replacement Project will then acquire and/or develop the information systems to facilitate the storage of data which is currently held in the existing PLC database as well as additional data from other IESO registration databases. The IESO projects to spend $1.5 million over the business planning period.

Other Capital Initiatives

Please refer to Appendix 2 for a complete listing of all Other Capital Initiatives and their expected costs during the planning period.

Throughout the planning period, based on shifting priorities, opportunities, and challenges, the actual plan may differ from that outlined in this plan. Within the IESO, all capital projects require Business Unit Leader, President and CEO, or Board of Directors approval as appropriate.[7]

Asset Service Lives

As part of the business planning process, the service lives used in the amortization of capital assets are reviewed. The IESO reviews existing assets against the proposed capital plan, and also reviews service life changes that are needed during the year. This is done to see if there is a need to reduce existing service lives because of early replacement or to see if there is a need to increase or extend asset lives, due to prudent asset management.

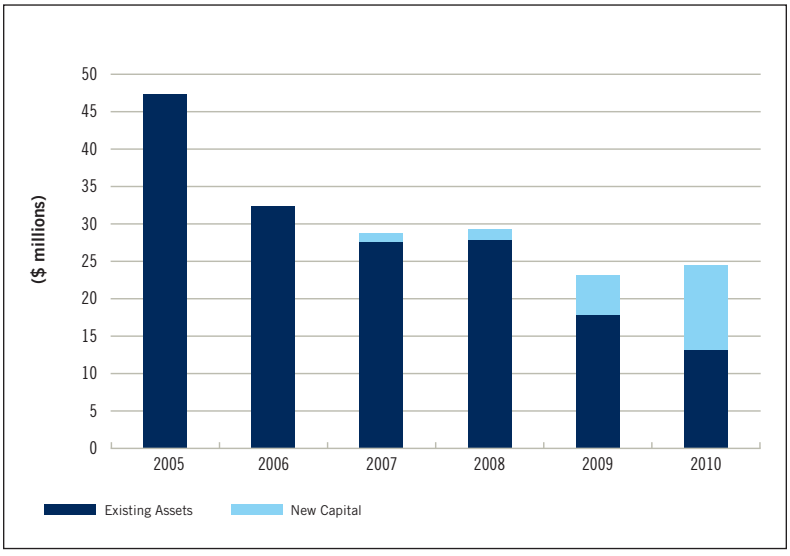
The proposed capital plan within this business plan includes the replacement or upgrade of several major market systems. These assets had previously been assumed to be completely amortized in 2007 and 2008; however based on this current projection their service lives will be extended to match their planned replacement dates.

Amortization Expense over the Planning Period

Over the planning period, the expected annual amortization expense will fluctuate slightly from the projected 2007 level. This fluctuation reflects the IESO's success in using some information system infrastructure longer than originally planned and lower costs for replacement infrastructure.

For those applications that are being upgraded or replaced over the planning period, this work is expected to cost less than the original implementation due to the increased knowledge of the IESO. In addition, the initial implementation was done in parallel to the market rules development, resulting in additional initial costs.

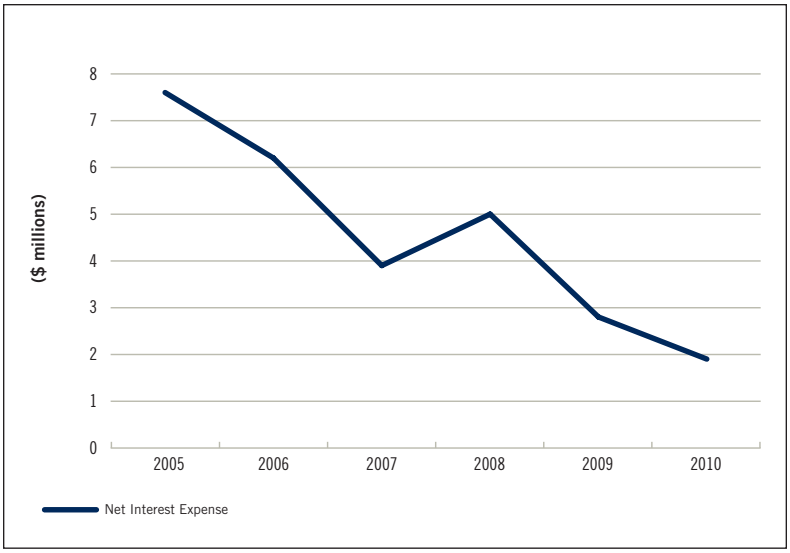
The following table outlines the amortization expense over the planning period:



7 Business Unit Leaders can approve capital projects up to $500 thousand, President & CEO can approve capital projects up to $4.0 million, and the Board of Directors approves all capital projects in excess of $4.0 million.

($ millions)	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Existing Assets In-Service	27.6	27.8	17.8	13.2
New Capital	1.1	1.5	5.3	11.3
Total Amortization	**28.7**	**29.3**	**23.1**	**24.5**

Net Interest Expense



($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Interest Expense	**7.6**	**6.2**	**3.9**	**5.0**	**2.8**	**1.9**

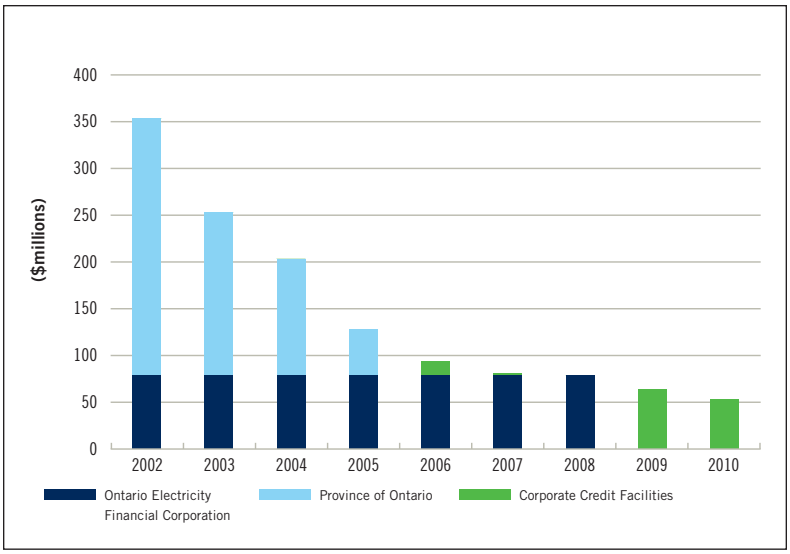
The interest expense over the planning period is largely based on the following financing strategy.

Financing Strategy

The long-term note payable to Ontario Electricity Financial Corporation ("OEFC") in the amount of $78.2 million is unsecured and is repayable on May 1, 2009, bearing a fixed interest rate of 7.9%. As the debt with OEFC includes a 'hold harmless' clause within its legal structure, it is likely to remain in effect until maturity and will result in $6.2 million of interest annually and an increased cash balance at the end of 2008.

In 2006, the IESO refinanced the Province of Ontario debt due March 31, 2007 with a credit facility provided by a Canadian chartered bank. The cost to borrow under the credit facility is lower and the agreement gives the IESO flexibility to adjust borrowings to cash flow and changes in interest rates. Specifically, the IESO may borrow at the prime rate of the bank or under the Bankers Acceptance facility plus a stamping fee of 30 basis points; the standby fee is ten basis points. The assumed interest rate on this debt for each year over the planning period is 5.1%.

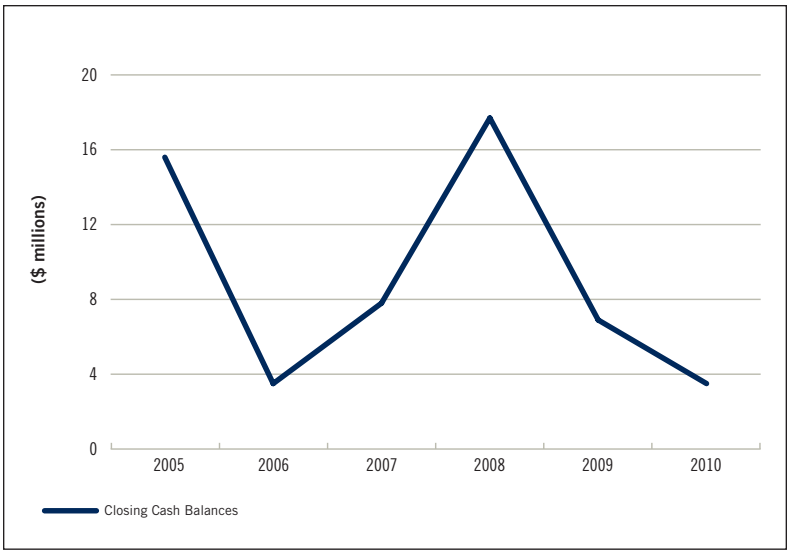
Based on budgeted cash flows, the IESO anticipates paying off the existing credit facility in 2008 – with $12.0 million being repaid in 2007 and the balance of $3.0 million in 2008. Also, the IESO expects to refinance the debt to the OEFC in 2009. Likely, this debt would be refinanced through a corporate credit facility. Based on current cash flow projections, $15.0 million of the original OEFC debt would be retired in 2009, with a further $10.0 million in 2010, resulting in a total debt level of $53.2 million at the end of 2010 – that would reflect repayment of 85% of the IESO's debt since 2002.



The financing strategy above outlines the plan to continue to reduce debt over the planning period. The resulting interest costs, which reduce over the planning period, are estimated as follows:

- $6.2 million in 2008
- $4.2 million in 2009
- $3.2 million in 2010

Over the planning period, the IESO intends to maintain adequate cash balances, while still repaying debt as outlined above. The following chart shows the planned closing cash balances from 2005 through 2010.



Investing this cash will result in investment income that will partially offset interest expense. The assumed average rates of return on investments are 4.75% over the planning period. These rates are in comparison to a forecast rate of return on 2007 investments of 4.46%.

In addition to cash and temporary investments, the IESO also holds long-term investments. These investments represent corporate assets that have been notionally put in place to discharge the liabilities associated with the Supplemental Employee Retirement Plan (SERP). The SERP represents the IESO's pension obligation that exceeds the component of individuals benefits in excess of the limits outlined in the Income Tax Act. As the long-term investments relate to a long-term obligation, these assets are invested in a balanced portfolio of pooled funds. Consistent with changes to Canadian GAAP in 2007, capital appreciation in the investment is now recognized on all gains/losses as they occur. This change impacted investment income starting in 2007 as the IESO included an assumed return on these assets in each year going forward. In addition, a one-time gain of $1.8 million was reflected in 2007 for previously unrecognized life-to-date appreciation on the market value of assets. On an ongoing basis, the Plan will assume a return of 7.0% on these assets – a rate of return consistent with management's assumed long-term rate of return of the registered pension plan assets. The ongoing forecasted income is $1.2 million in 2008, $1.3 million in 2009, and $1.5 million in 2010.

The IESO maintains two separate lines of credit: $60.0 million of corporate credit facility (use of which is described above) and $100.0 million for market settlement needs. The cost of these lines of credits, aside from any interest on drawn amounts, includes stamping fees and a standby charge. In total, the annual cost is approximately $0.3 million in each of the planning years.

For large and enduring projects, interest is capitalized on funds expended before the project is placed in-service. In 2007 this includes the EMS/MIS upgrade and over the planning period includes the DAM.

The resulting capitalized interest is:
- $0.3 million in 2008
- $0.3 million in 2009

The following table outlines net interest expense over the planning period:

($ millions)	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
Interest Expense on Debt	9.1	7.7	6.8	6.2	4.2	3.2
Investment Income	(1.1)	(0.5)	(0.1)	–	(0.1)	(0.1)
Returns on Long-term Investments	(0.6)	(1.2)	(2.8)	(1.2)	(1.3)	(1.5)
Financing Charges	0.2	0.2	0.3	0.3	0.3	0.3
Capitalized Interest	–	–	(0.3)	(0.3)	(0.3)	–
Net Interest Expense	**7.6**	**6.2**	**3.9**	**5.0**	**2.8**	**1.9**

YEAR 2008 REGULATORY APPROVALS – IESO USAGE FEE

This section details the calculation of the IESO usage fees for the year 2008 for which approvals from the OEB are requested. Revenue sources, detailed rationale, derivation and amounts are listed.

Revenue Sources

There are several sources of revenue for 2008:

- Cost recovery for services
- Interest earned on market settlement funds
- Revenue from IESO fees

Cost Recovery for Services

The IESO will continue in its plan to recover the cost of services that are directly attributed to a participant, such as training, assessments, and services to the Ontario Power Authority on a cost recovery basis. The estimated total revenues from cost recovery in 2008 are $2.0 million.

Interest Earned on Market Settlement Funds

According to the market rules, at the end of each year, monies which have been earned from interest on market settlement funds are applied to offset the IESO administration charge in the following year. The projected market-related interest income is $5.0 million for 2008.

Revenue from IESO Fees

The OEB approved the fee methodology in 2000. The fee structure, which has been in effect since market opening, includes an application fee of $1,000 per application, plus a $/MWh usage fee. The revenue from application fees is expected to be negligible in 2008.

Usage Fee

This section derives the fee for the year 2008 for approval by the OEB, and provides a projection for 2009 and 2010.

The first step is to calculate the revenues required.

Revenue Requirement Calculation for IESO Usage Fee			
($ millions)	**2008**	**2009**	**2010**
Revenue Requirements	135.5	128.8	129.9
Less: Other Revenues			
• Cost recovery for services	2.0	2.0	2.0
• Interest earned on market funds	5.0	4.6	4.6
Revenue Requirement to be recovered by IESO Usage Fee	128.5	122.2	123.3

The second step is to estimate the charge determinant for the usage fee. The charge determinant is the total AQEW (Allocated Quantity of Energy Withdrawn) for the year, including exports out of Ontario:

Year	18-Month Outlook Demand Forecast (TWh)	–	Transmission Line Losses (TWh)	+	Exports (TWh)	=	Market Demand (TWh)
2008	154.5	–	4.6	+	10.9	=	160.8
2009	154.9	–	4.6	+	11.2	=	161.5
2010	156.5	–	4.7	+	11.1	=	162.9

The third step is the rate calculation:

Year	Revenue Requirement To Be Recovered ($ million)	÷	Market Demand (TWh)	=	Usage Fee ($/MWh)
2008	128.5	÷	160.8	=	0.799
2009	122.2	÷	161.5	=	0.757
2010	123.3	÷	162.9	=	0.757

Implementation of 2008 usage fee

Pending approval by the OEB for the 2008 usage fee, the 2007 usage fee will continue to be charged to market participants. Once the OEB approves the fee, rebates to market participants will be made for the difference between the old and new usage fee based on the allocated quantity of energy withdrawn for the period January 1, 2008 and the end of the month in which the OEB approves the fee. The rebate will be redirected to market participants in the next billing cycle following the month in which the OEB approves the fee.

Disposition of Deferral Account Balance Surplus

Based on the settlement agreement accepted by the OEB on March 21, 2007, any surplus held at the end of a year in excess of $5.0 million is returned to the market participants in the form of a rebate in the following year. The rebate is based on the market participant allocated quantity of energy withdrawn during the prior year.

Overall, the 2007 projected operating results would result in an accumulated operating surplus of $5.4 million by year-end. This is determined by adding last year's actual accumulated surplus of $5.0 million to this year's projected surplus of $0.4 million. The result is an estimated rebate of approximately $0.4 million.

The final amount to be rebated will be based on the audited financial statements for the fiscal year 2007 and the refund will be rebated to market participants in the next billing cycle following the month in which the IESO Board of Directors approves the 2007 financial statements.

SECTION B:
FINANCIAL OUTLOOK RELATING TO THE SMART METERING ENTITY

In 2006, a regulation under the Electricity Act was issued expanding the IESO's objects to include responsibilities under the provincial government's Smart Metering Initiative (SMI). These responsibilities cover overall co-ordination of the Smart Metering System Implementation Program and project management of the development and delivery of the Meter Data Management and Repository (MDM/R).

A recent regulation under the Electricity Act further designated the IESO as the Smart Metering Entity. As such, in addition to its current role, the IESO will be responsible for the administration and operation of the MDM/R and the enrollment into the MDM/R of all the Local Distribution Companies in the province.

It is intended that the IESO's internal and contracted expenses will be recovered through a regulatory mechanism, which will be independent of the IESO's current fee structure and of the revenues derived from the wholesale market.

Until the regulatory mechanism is in place, the IESO has included preliminary estimates of high-level revenues and costs for its Smart Meter activities in the consolidated financial statements provided in Appendix 1.

All direct and incremental costs associated with the MDM/R will be collected and charged separately from all other IESO costs that form part of the revenue requirements for the IESO usage fee. For 2008, incremental corporate overhead costs are expected to be minimal, and are therefore not currently planned to be separately charged to the smart meter accounts.

The IESO will be developing a fee proposal later this fall in respect of its role as Smart Meter Entity, at which time smart meter revenues and costs will be confirmed and the current consolidated financial projections updated. The preliminary estimates incorporated into the consolidated financial statements, and the associated assumptions, are set out below.

SMART METERING ENTITY OUTLOOK 2008-2010

($ millions)	2007 Projected	2008 Budget	2009 Plan	2010 Plan
SME Fees	–	4.8	12.4	18.7
Total Revenues	**–**	**4.8**	**12.4**	**18.7**
SME Program Costs	4.8	11.6	12.7	10.7
Amortization	1.2	3.6	3.6	3.6
Net Interest	0.5	1.9	2.2	2.1
Total Costs	**6.5**	**17.1**	**18.5**	**16.4**
Operating Surplus/(Deficit)	**(6.5)**	**(12.3)**	**(6.1)**	**2.3**
Accumulated (Deficit)	**(6.5)**	**(18.8)**	**(24.9)**	**(22.6)**

The above calculations include numerous assumptions including:

- A regular staff complement of 4 will be required by the SME. The function of these staff will be in the IT and customer service areas of the business.
- An additional two full-time equivalents will be required for the other support areas of the business, such as market entry, finance and settlements, however, it is not intended to hire regular staff complement. It is intended that this support work will be resourced through overtime, temporary resources or other means – the responsibility for managing this provision of service will reside within the respective functional areas of the business.
- The development costs for the Meter Data Management and Repository are projected to be recovered over a six-year service life.
- Revenues were based on a projection of active service delivery points/month for smart meters installed across the province.
- Required debt financing will be obtained through the IESO's corporate credit facility.

Appendix 1: Consolidated Financial Statements

Actual and Pro Forma Statement of Operations and Accumulated Surplus

For the Year Ended December 31
(in Millions of Canadian Dollars)

	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
REVENUES						
Usage fees	156.9	144.7	131.2	128.5	122.2	123.3
SME fees	–	–	–	4.8	12.4	18.7
Market-related interest income	3.5	4.9	4.2	5.0	4.6	4.6
Cost recovery for services	0.9	2.1	2.0	2.0	2.0	2.0
Total Revenues	**161.3**	**151.7**	**137.4**	**140.3**	**141.2**	**148.6**
EXPENSES						
OM&A program costs	83.3	83.1	92.4	101.4	106.5	105.8
OM&A pension expense	8.3	17.3	16.8	11.4	9.1	7.4
Amortization	47.4	32.4	29.9	32.9	26.7	28.1
Net Interest	7.6	6.2	4.4	6.9	5.0	4.0
Total Expenses	**146.6**	**139.0**	**143.5**	**152.6**	**147.3**	**145.3**
Operating Surplus/(Deficit)	**14.7**	**12.7**	**(6.1)**	**(12.3)**	**(6.1)**	**3.3**
Transfer to Ontario Power Authority	(15.0)	–	–	–	–	–
Rebates to Market Participants	(13.6)	(12.7)	(0.4)	–	–	(1.1)
Accumulated Surplus – Usage fees	**5.0**	**5.0**	**5.0**	**5.0**	**5.0**	**5.0**
Accumulated Deficit – SME fees	**–**	**–**	**(6.5)**	**(18.8)**	**(24.9)**	**(22.7)**
Market-related Penalties & Fines	0.5	0.7	–	–	–	–
Customer Education Fund Expenditures	(0.4)	(0.2)	(0.7)	(1.1)	(1.2)	–
Accumulated Fines and Penalties – End of Year	**2.5**	**3.0**	**2.3**	**1.2**	**–**	**–**

Actual and Pro Forma Statements of Financial Position

As at December 31
(in Millions of Canadian Dollars)

	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
ASSETS						
Current Assets						
Cash & cash equivalents	9.6	3.5	7.8	7.7	6.9	3.5
Temporary investments	6.0	–	–	–	–	–
Accounts receivable	19.9	20.9	18.2	18.6	17.5	17.5
Short-term prepaid expenses	2.7	3.8	3.7	3.7	4.3	4.1
	38.2	**28.2**	**29.7**	**30.0**	**28.7**	**25.1**
Property & Equipment						
Property & equipment in service	335.3	352.2	386.3	397.2	423.4	443.4
Less: accumulated amortization	(207.4)	(239.1)	(269.0)	(301.9)	(328.6)	(356.7)
Net Book Value	127.9	113.1	117.3	95.3	94.8	86.7
Construction-in-progress	4.0	4.7	4.3	13.4	7.2	7.2
	131.9	**117.8**	**121.6**	**108.7**	**102.0**	**93.9**
Other Assets						
Long-term investments	9.9	12.6	16.6	19.0	21.5	24.2
Prepaid pension expense	21.9	12.5	3.7	0.6	0.1	1.5
Deferred Charges – Smart Meters	–	1.6	1.6	1.5	1.3	1.0
	31.8	**26.7**	**21.9**	**21.1**	**22.9**	**26.7**
TOTAL ASSETS	**201.9**	**172.7**	**173.2**	**159.8**	**153.6**	**145.7**
LIABILITIES						
Current Liabilities						
Accounts payable & accrued liabilities	19.9	21.0	19.0	19.0	19.0	19.0
Accrued interest	1.0	1.0	1.0	1.0	–	–
Current portion of long-term debt	–	15.0	31.7	27.3	102.8	86.6
Rebates to market participants	13.6	12.7	0.4	–	–	1.1
	34.5	**49.7**	**52.1**	**47.3**	**121.8**	**106.7**
Long-term debt	128.2	78.2	78.2	78.2	–	–
Accrual for employee future benefits other than pension	31.7	36.8	42.1	46.9	51.7	56.6
TOTAL LIABILITIES	**194.4**	**164.7**	**172.4**	**172.4**	**173.5**	**163.3**
Accumulated Surplus – Usage Fees	5.0	5.0	5.0	5.0	5.0	5.0
Accumulated Deficit – SME Fees	–	–	(6.5)	(18.8)	(24.9)	(22.6)
Accumulated Fines and Penalties	2.5	3.0	2.3	1.2	–	–
TOTAL LIABILITIES & ACCUMULATED SURPLUS	**201.9**	**172.7**	**173.2**	**159.8**	**153.6**	**145.7**

Actual and Pro Forma Statement of Cash Flows

For the Year Ended December 31
(in Millions of Canadian Dollars)

	2005 Actual	2006 Actual	2007 Projected	2008 Budget	2009 Plan	2010 Plan
OPERATING ACTIVITIES						
Operating surplus/(deficit) after Rebates	1.0	–	(6.5)	(12.3)	(6.1)	2.3
Change in Rebates to Market Participants	13.6	(0.9)	(12.3)	(0.4)	–	1.1
Market Penalties and Fines	0.5	0.7	–	–	–	–
Customer Education Fund Expenditures	(0.4)	(0.2)	(0.7)	(1.1)	(1.2)	–
Amortization	47.4	32.4	29.9	32.9	26.7	28.1
Change in FV long-term investment	–	–	(2.7)	(1.2)	(1.3)	(1.5)
Decrease in Prepaid Pension Expense	8.4	17.7	17.3	11.9	9.6	7.8
Increase in accrual for employee future benefits	4.5	6.4	6.6	6.2	6.3	6.5
Pension plan contributions	(8.2)	(8.4)	(8.5)	(8.8)	(9.1)	(9.2)
Payment of employee future benefits	(1.3)	(1.4)	(1.3)	(1.4)	(1.5)	(1.6)
Changes in Other Non-cash items related to Operations	(2.1)	(1.3)	0.6	(0.4)	(0.5)	0.2
Cash Provided from Operations	**63.4**	**45.0**	**22.4**	**25.4**	**22.9**	**33.7**
INVESTING ACTIVITIES						
Net Sale/(Purchase) of Temporary Investments	39.9	6.0	–	–	–	–
Purchase of Long-Term Investments	(1.9)	(2.7)	(1.2)	(1.2)	(1.2)	(1.2)
Investment in Property & Equipment	(9.1)	(17.8)	(33.6)	(20.0)	(20.0)	(20.0)
Investment in Deferred Charges – SMP	–	(1.6)	–	0.1	0.2	0.3
Cash Used in Investing Activities	**28.9**	**(16.1)**	**(34.8)**	**(21.1)**	**(21.0)**	**(20.9)**
FINANCING ACTIVITIES						
Issue/(Retirement) of debt	(75.0)	(35.0)	16.7	(4.4)	(2.7)	(16.2)
Draw on contribution to the OPA	(15.0)	–	–	–	–	–
Cash Provided from Financing Activities	**(90.0)**	**(35.0)**	**16.7**	**(4.4)**	**(2.7)**	**(16.2)**
Net Change in Cash Flow	**2.3**	**(6.1)**	**4.3**	**(0.1)**	**(0.8)**	**(3.4)**
Cash and Cash Equivalents – Beginning of Year	7.3	9.6	3.5	7.8	7.7	6.9
Cash and Cash Equivalents – End of Year	**9.6**	**3.5**	**7.8**	**7.7**	**6.9**	**3.5**

Appendix 2: Capital Projects

Key Corporate Capital Projects ($ millions)

Key Corporate Capital Projects	Project Description	2007 Projected Spending	2008 Plan	2009 Plan	2010 Plan	2008-2010 Plan Total
Day-Ahead Market	As described in the Business Plan	**0.0**	**8.0**	**8.0**		**16.0**
On-Line Limit Derivation (New for 2008-2010)	Currently much of the limit derivation in the IESO is performed manually both on and off shift. This project would acquire or develop the tools to facilitate on-line limit derivation in both the on-shift and back office environments. The new systems would be fully integrated into the existing suite of tools.	**0.2**	**0.5**	**1.0**	**1.0**	**2.5**
PLC Replacement (New for 2008-2010)	The Participant Lifecycle (PLC) System is the primary repository of market participant data at the IESO and is used to provide this data to critical market systems. Improvements will address handling of other forms of information currently stored in other IESO registration databases.	**0.0**	**1.0**	**0.5**		**1.5**
Energy Management System/Market Information System Upgrade	Upgrade the EMS/MIS which monitors and facilitates the reliability of the IESO controlled grid, and supports market operations. The upgrade will extend the life of the current systems from 2008 to 2011, maintain system performance, improve functionality of tools, better integrate EMS/MIS user interfaces with other IESO interfaces, and reduce costs related to IESO user workstation and server maintenance and support, that would otherwise increase beyond economic levels.	**3.2**	**1.1**			**1.1**
Windows Refresh Program (Stages 4 & 5)	Stage 4: Migrate those Business Applications deemed critical from a reliability, capacity or performance perspective to the new MS Windows Server 2003 infrastructure. Stage 5: Complete the replacement of aging IESO Windows server infrastructure (Hardware & Software), by migrating remaining Business Applications to the new core MS Windows Server 2003 infrastructure.	**1.8**	**0.9**			**0.9**
Network Zoning Project (New for 2008-2010)	This project is essential for supporting the NERC CIP Program. NERC has identified that addition cyber security is required for all critical systems which support grid operations. This project will create the infrastructure and the process required to manage it going forward.	**0.0**	**0.8**			**0.8**
Facility Outage Management System	Provide an automated and integrated real-time tool to deliver significantly improved outage management services. Currently two separate applications: Integrated Outage Management System (IOMS) and Outage Scheduler (OS), provide outage management services for submitting, modifying and viewing outage information. A single automated and integrated application will improve data validation, on-line viewing of outage information, improve planning capability, and reduced process inefficiencies. It will also provide IESO staff with additional capability to perform performance tracking, and will reduce internal process inefficiencies. The project would result in IESO being able to determine security limits with greater accuracy, thereby positively impacting on the efficiency and security of the IESO-controlled grid.	**0.4**	**0.8**			**0.8**
UNIX Server Infrastructure Refresh	Replace aging UNIX server infrastructure, which no longer has vendor support, on an on-going basis, in order to reduce support and maintenance costs, reduce hardware purchase costs, and provide better availability and on-going reliability. Examples of benefits include: reduced support calls due to hardware failures; increased reliability with newer more stable systems; reduced licensing costs; server consolidation and reduced server count.	**1.8**	**0.5**			**0.5**
NERC – CIP Program (New for 2008-2010)	Capital expenditures directly related to complying with NERC's Critical Infrastructure Protection Program.	**0.0**	**0.2**	**0.2**		**0.4**
Back-up Operating Centre Relocation and Configuration	Re-locate the IESO's backup control centre to a more secure location, to address current and assessed future security environment status. Project to be completed in 2007	**1.0**				**0.0**
TOTAL – KEY CORPORATE PROJECTS		**8.4**	**13.8**	**9.7**	**1.0**	**24.5**
TOTAL – OTHER PROJECTS	As described in detailed listing	**3.4**	**6.2**	**10.3**	**19.0**	**35.5**
TOTAL IESO CAPITAL PROJECTS		**11.8**	**20.0**	**20.0**	**20.0**	**60.0**

Other IESO Capital Projects ($ millions)

Other Projects	Project Description	2007 Projected Spending	2008-2010 Plan Total
APPLICATIONS			
Configuration Management System	This project will introduce a Configuration Management system and respective processes.		**2.2**
Application Changes / Vendor Change Requests	A funding envelope, to facilitate minor changes to IESO applications. Allocation of these funds is managed by a cross-functional IESO team, the IT User Committee, comprised of representatives of all business units.	**1.0**	**2.1**
Records Management Replacement	Replace the IESO's existing Foremost Records Management system, which has a technological life cycle end date of 2007, in order to maintain the existing records management system capabilities, incorporate needed improvements, and increase storage scalability.	**0.1**	**1.6**
Meter Data Repository	Acquire and implement an application that will replace current MVStar.		**1.0**
Real-Time Commercial Reconciliation System Upgrade	This project is being undertaken to upgrade the Commercial Reconciliation System and its' Graphical User Interface (GUI) from the current version used in support of the real time electricity market. It will put the settlement process on an up-to-date technology platform that is supported by the vendors and will meet the needs of the settlement process while resulting in reduced support costs and ensuring continued compatibility of this system with infrastructure, operating system, and database technology.The project will include improvements to the approach currently used to do post-final settlement calculations.		**1.0**
PKI Refresh	Replacement or upgrading of Public Key Infrastructure assets to mitigate end of life risks and obsolescence.		**1.0**
BITS Replacement	Replacement or upgrading of BITS asset to mitigate end of life risks and obsolescence.		**1.0**
Meter Trouble Report and Notice of Disagreement Upgrade	Place the Meter Service Provider/Market Participant facing Meter Trouble Reporting and Notice of Disagreement workflow systems on a current platform and technology with applications supported by the vendor of choice. This is a lifecycle driven upgrade, which includes functionality driven upgrades and improvements.		**0.8**
System Data Repository Constellation	Reconfigure the data warehouse (constellation style) database design, enabling improvements in handling the large and increasing data volumes, which are utilized in supporting market analysis and satisfying reporting obligations. Current capabilities of the System Data Repository of market activity data requires modifications and upgrades to handle increasing data volumes, and facilitate faster and more effective data retrieval and analysis in support of surveillance and compliance activities.		**0.8**
Appropos System Upgrade/ Replacement	This project will extend or replace the Apropos customer support solutions, as they will have been in service for 5 years and are in need of improvements.		**0.8**
Lawson & Essbase Upgrade	This project will upgrade the Lawson and Essbase corporate financial system components to be on a current platform and technology supported by the vendor.		**0.5**
Publishing Tool Replacement	Deliver an assessment tool which enables the IESO to perform both daily and forward looking security and adequacy assessments and makes these results available to the standard production reporting system. The objective is to reduce manual effort and simplify tasks.		**0.5**
Market Portal Upgrade	Upgrade the underlying market portal technology, including software.		**0.5**
Oracle Financials	Purchase of Oracle Financial Applications		**0.5**
Other Minor IT Applications Projects	Total of projects which individually do not exceed $500,000 each	**0.4**	**5.4**
TOTAL APPLICATIONS		**1.5**	**19.7**

Other Projects	Project Description	2007 Projected Spending	2008-2010 Plan Total
IT – INFRASTRUCTURE			
Tier 1 Storage Addition.	Add 2 new Tier 1 Storage arrays for additional capacity and scalability		**2.0**
Network Equipment Replacement	Replace the existing CISCO Network Gear which has a technological life cycle end of life in 2008. This equipment serves as the technical infrastructure that facilitates the connection between corporate business applications.		**1.8**
Pre-Production Environment	Improvement to and consolidation of the quality assurance/pre-production environment that will enable better mimicking of the IESO's production environment. This will enable improved quality and reliability assurances from implementation testing, which occurs prior to introducing systems into a full production environment.		**1.5**
Microsoft Licenses 2008	Procure sufficient Microsoft Licenses to ensure legal compliance. Determine the most cost effective approach to procure Microsoft Licenses as required for 2008 and beyond. This includes all MS Office products and MS Operating System Licenses.		**1.1**
Rebuild Computer Room	Rebuild IESO computer room and associated elements that have become obsolete, unsupported, or unreliable		**1.0**
Telemetry Improvements	Combination of reliability modifications for Control Rooom and Replacement of Cybetec Boxes		**1.0**
Control Room Wallboard Replacement	Replace the IESO control room's wallboard display		**0.8**
Increased Disk Storage	An annual program to address planned and needed increases in storage capacity requirements.	**0.4**	**0.6**
Systems Management Rationalization	This project will rationalize all the systems management tools into a common infrastructure		**0.5**
Other Minor IT Infrastructure Projects	Total of projects which individually do not exceed $500,000 each	**0.8**	**1.7**
TOTAL IT-INFRASTRUCTURE		**1.2**	**12.0**
FACILITIES IMPROVEMENTS			
Security Upgrades	Replacement and enhancement of obsolete access control system and surveillance systems.		**0.5**
Uninterruptible Power Supply Replacement	Replace current UPS in order to ensure on-going reliability, based on increased risk of age related unreliability of existing UPS		**0.5**
Other Minor Facilities Improvements	Total of projects which individually do not exceed $500,000 each	**0.7**	**0.3**
TOTAL FACILITIES IMPROVEMENTS		**0.7**	**1.3**
OTHER UNPLANNED PROJECTS AND CONTINGENCY			**2.4**
TOTAL – OTHER IESO CAPITAL PROJECTS		**3.4**	**35.3**

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