



Office of the Auditor General of Ontario
Bureau de la vérificatrice générale de l'Ontario

April 11, 2018

To the Standing Committee on Public Accounts

Re: Report on the Special Audit of the Financial Statements of the Independent Electricity System Operator (IESO) for the Year Ended December 31, 2017

Dear Committee Members:

Further to my submission to the Committee dated March 20, 2018, I would like to provide new information on the following two matters:

1. On March 27, 2018, the IESO Board of Directors approved a *revised* set of financial statements for the IESO (having already approved a different set of financial statements). As a result, we have had to update our Independent Auditor's Report to reflect these changes (see details below).
2. We wish to clarify the roles of KPMG LLP, Deloitte LLP and Ernst & Young LLP with respect to the Fair Hydro Plan (see details below).

IESO's Revised Financial Statements

Subsequent to March 20, 2018, the IESO adjusted its financial statements (already approved by the Board of Directors on March 8, 2018) to include a note disclosing that in December 2017, the IESO pledged the current and future receivables from local distribution companies (LDCs) as collateral for debt investors of the Fair Hydro Trust. This means that if the IESO defaults on its payments of carrying costs to the Fair Hydro Trust, the money received from ratepayers (through LDCs) must be used to pay the Trust before power generators can be paid. This material disclosure stems from our recommendation to this effect.

The IESO and its external auditor, KPMG, had previously declined to support this recommendation. However, on March 28, 2018, we received the revised financial statements for the IESO that were approved by way of an IESO Board Resolution dated March 27, 2018. As well, KPMG's Auditor's Report was re-issued to us to reflect the new date of issuance of March 27, 2018, replacing the opinion previously provided to us March 8, 2018. The IESO has published its 2017 Annual Report containing its financial statements and KPMG's audit opinion dated March 27, 2018, on its website.

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Please find attached our final Independent Auditor's Report on our special financial statement audit of the IESO for the year ended March 31, 2017 (**Attachment 1**). Please note that our report contains references to the IESO's financial statements and can be read in conjunction with those financial statements. The purpose of our report is to highlight the potential error impact as at December 31, 2017, on the consolidated financial statements for the Province of Ontario. This potential error will be larger for the year ended March 31, 2018, if the planned accounting in the consolidated financial statements is not corrected.

Also attached for your information are the following documents:

- a copy of the IESO's 2017 Annual Report containing financial statements with KPMG's audit opinion (**Attachment 2**); and
- a copy of our updated management letter reflecting the IESO's updated responses to our recommendations (**Attachment 3**).

The Actual Roles Played by Large Accounting Firms with Respect to the Fair Hydro Plan

We would like to clarify the roles of KPMG, Deloitte and Ernst & Young with respect to the Fair Hydro Plan and what opinions they have provided to the government regarding the accounting treatment in the IESO's financial statements and the accounting treatment for the Province's consolidated financial statements.

As at March 19, 2018:

- **Deloitte LLP and Ernst & Young LLP have confirmed to us that they provided no formal opinions approving the accounting for the Fair Hydro Plan that the government planned to use for its consolidated financial statements.**
- **KPMG told us that it has not provided an opinion on the accounting for the Fair Hydro Plan in the government's consolidated financial statements.** Rather, KPMG supports just the accounting used by the IESO by signing an unqualified audit opinion on the IESO's financial statements for the years ended December 31, 2016 and 2017.
- Deloitte has not performed any direct work for the Office of the Provincial Controller Division on the accounting for the Fair Hydro Plan or for the IESO directly. Although Deloitte provided a theoretical analysis in July 2017 to KPMG for a related purpose, the scope of its work did not extend into any

assessment of specific regulatory assets or liabilities recognized by the IESO or the accounting for the Fair Hydro Plan.

- Although Ernst & Young has worked on the accounting for Ontario Power Generation and to help the Office of the Provincial Controller Division prepare its accounting position papers, this work does not constitute providing a formal opinion on the accounting to be used by the government in preparing the Province's consolidated financial statements based on the facts of the Fair Hydro Plan.

The sum of all of this work does not equate to approval of the accounting in the consolidated financial statements of the Province of Ontario. The Office of the Auditor General is the only independent party opining on the accounting from this consolidated perspective.

Conclusion

This information is provided for your consideration as you deliberate on the content of the report to be written and issued by the Standing Committee on Public Accounts regarding the Committee's hearing on Chapter 2 of the *2017 Annual Report of the Office of the Auditor General of Ontario* held on Wednesday, February 28, 2018.

We will continue to request that the government correct the impact of the IESO's accounting on the Province's consolidated financial statements for the year ending March 31, 2018.

This information and an updated status will be provided in Chapter 2 of Volume 1 of our 2018 Annual Report.

Sincerely,



Bonnie Lysyk
Auditor General

Attachment 1 – Independent Auditor's Report on the Special Financial Statement Audit of the IESO

Attachment 2 – IESO's Audited Financial Statements for the year ended December 31, 2017

Attachment 3 – IESO's Updated Management Letter Prepared by the Office of the Auditor General of Ontario