CCA-AESO-001

Reference
Section 3.1.4

Issue/Sub-Issue
General and Administrative Costs

Preamble
The 2012 recorded general and administrative costs were $81.5 million, which is $2.7 million (or 3%) more than the 2012 approved forecast of $78.7 million. This variance resulted from increases and decreases in several general and administrative cost components, including variances that exceeded the threshold above which explanations are required (as discussed earlier in Section 3.1) in computer and telecommunications services and maintenance, interest, and amortization.

Request
(a) With reference to line 39 of Table 3-1 please provide an analysis showing the forecast and actual base salaries, benefits, incentive payments and overtime. Provide variance explanations between forecast and actuals with respect to each of the components of salaries and benefits. Explain the due diligence process that is in place internally to ensure, and to demonstrate to the AESO Board and to the AUC, that salaries exceeding budget in 2012, are prudent.

(b) By reference to line 40 of Table 3-1, please explain why the contract services and consultants costs exceeded the forecast in 2012. Explain the due diligence process that is in place internally to ensure, and to demonstrate to the AESO Board and to the AUC, that consultants' costs exceeding budget in 2012, are prudent.

Response
(a) Additional detail on salaries and benefits is provided below.

<table>
<thead>
<tr>
<th>Description</th>
<th>2012 Forecast</th>
<th>2012 Recorded</th>
<th>Variance over (Under)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base salaries</td>
<td>$27.9</td>
<td>$29.9</td>
<td>$1.9 6.8%</td>
</tr>
<tr>
<td>Benefits (including incentive and overtime pay)</td>
<td>11.3</td>
<td>12.4</td>
<td>1.0 8.8%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$39.3</strong></td>
<td><strong>$42.2</strong></td>
<td><strong>$2.9 7.4%</strong></td>
</tr>
</tbody>
</table>

2012 recorded staff and benefits costs were higher than forecast primarily due to vacancy rates being lower than forecast throughout the year as well as conversion of contractor resources to staff positions where appropriate. The 2012 forecast vacancy rate was 8%, consistent with forecast assumptions in previous years. The 2012 recorded vacancy rate was about 3% as a result of greater emphasis on recruitment. The AESO’s recruitment strategy was reviewed and...
endorsed by members of the AESO Board to support the ongoing advancement of the AESO’s business initiatives and to mitigate risks associated with tight labor markets during 2012 for both electric industry professionals and general staff.

The AESO considers that incentive pay forms part of a comprehensive and competitive compensation package and has included incentive pay with benefits in the table above. The variance of benefits above forecast is comparable to the variance of base salary above forecast.

The AESO incurred very limited overtime pay in 2012 due, in part, to the lower vacancy rate and through utilization of time off in lieu and other recognition mechanisms for extra time occasionally required to accomplish business initiatives.

(b) Please refer to information response AUC-AESO-001 for additional detail on the initiatives that comprised contract services and consultants costs in 2012.

As discussed in the application (section 2.4, page 22, paragraphs 89-91), throughout the year the AESO reviews and monitors the costs incurred to accomplish the established business priorities and plans of the AESO and to continue to meet the AESO’s legislated mandate. AESO management actively manages the organization’s financial affairs on a timely basis, including monthly reviews of the AESO’s financial results, the status of corporate goal achievement, and key human resource statistics. The monthly financial review includes a comparison of actual costs to budget and forecast amounts, with analysis of material variances for general and administrative costs as well as ancillary services costs, losses costs and capital.

When budgets and forecast costs do not fully accommodate the actual costs needed to accomplish the established business priorities and plans of the AESO, the AESO has controls and procedures in place to determine appropriate actions which may include approving additional expenditures to accomplish specific business priorities or meet its mandate, or managing the timing or reducing the scope of other business priorities to remain within budget.

The AESO’s budget review and approval process, developed in consultation with stakeholders, includes an agreed-upon practice when estimated costs are expected to exceed budgeted amounts. Variances up to 10% above budgeted general and administrative expenditures and up to 20% above budgeted general capital expenditures may be approved by the AESO Board and subsequently communicated to stakeholders. Variances above those thresholds are reviewed with stakeholders in advance of a request for AESO Board approval.

As well, the AESO budget controls and procedures include:

- a pay-for-performance salary administration process designed to align with and attain corporate goals based on business priorities, with the AESO Board providing oversight and approval of the annual corporate goals;
- regular updates to the AESO Board on the status of attaining corporate goals, with strategies developed or altered to better achieve goals at risk of not being met, including reprioritization of goals;
- risk prioritization and mitigation through development and implementation of financial and other policies;
- internal controls approved by the AESO Board and its Committees to provide reasonable assurance of achieving effective and efficient operations, reliable financial reporting, and compliance with laws and regulations; and
- evaluation of the AESO’s governance, risk management, and control processes through audits, reviews, and procedures performed throughout the year by the AESO’s Controls & Audit Services group and by third-party audit firms when required.
Of note during 2012, subsequent to the approval of the 2012 budget, the AESO changed a historical practice that transferred third-party consultant costs associated with planning major transmission system projects to transmission facility owners for capitalization as part of the overall project costs. After reviewing the practice, the AESO determined that such system development costs should more appropriately be recovered as part of AESO general and administrative costs to enhance accountability and cost management and for consistency with costs of AESO staff involved in planning transmission system projects. In 2012, these consultant costs that were no longer charged to transmission facility owners were $0.8 million, with no associated budget.

The AESO notes that the consultant costs associated with major transmission projects were offset by the conversion of contractor resources to staff positions mentioned in part (a) above as well as other variances above and below forecast, such that the net increase in contract services and consultants was $0.5 million (or 4%) above forecast.
CCA-AESO-002

Reference
Section 3.1.4

Issue/Sub-Issue
Amortization

Preamble
The 2012 recorded amortization cost was $13.3 million, which is $2.2 million (or 20%) more than the 2012 approved forecast of $11.1 million, primarily due to the higher-than-forecast allocation of amortization costs to the transmission function.

Request
Please provide a calculation of the forecast and actual amortization expense by asset account and identify the factors contributing to the increase in amortization expense in 2012 actual relative to 2012 forecast. Provide justification for the major increases.

Response
Please see amortization expense by asset class in the table below.

<table>
<thead>
<tr>
<th>Asset Account</th>
<th>Term</th>
<th>2012 Forecast</th>
<th>2012 Recorded</th>
<th>Variance Over (Under)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Computer hardware, furniture, and office equipment</td>
<td>3 years</td>
<td>$2.4</td>
<td>$4.0</td>
<td>$1.6</td>
</tr>
<tr>
<td>Computer software development</td>
<td>5-7 years</td>
<td>6.6</td>
<td>5.8</td>
<td>(0.8)</td>
</tr>
<tr>
<td>System coordination computer systems (EMS)</td>
<td>7 years</td>
<td>1.5</td>
<td>2.2</td>
<td>0.7</td>
</tr>
<tr>
<td>System Coordination Centre</td>
<td>20 years</td>
<td>0.7</td>
<td>0.8</td>
<td>0.1</td>
</tr>
<tr>
<td>Leasehold improvements</td>
<td>lease terms</td>
<td>0.0</td>
<td>0.5</td>
<td>0.1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>$11.1</strong></td>
<td><strong>$13.3</strong></td>
<td><strong>$2.1</strong></td>
</tr>
</tbody>
</table>

In preparing the 2012 forecast in mid-2011, estimates and assumptions for 2011 and 2012 capital costs by asset account, project commissioning dates, and allocation of capital costs to the AESO’s transmission function were required. Because of the nature of the estimates and assumptions made and the limitations on the information available when preparing the forecast, the AESO anticipated that variances from forecast would occur.

In the deferral account reconciliation application, the AESO referred to a higher-than-forecast allocation of amortization costs to the transmission function (section 3.1.4, pages 37-38, paragraph 193). This description applied to the allocation of amortization for capital asset additions during 2012, and reflected
corporate computing assets added in 2012 primarily to support the transmission function. However, the allocation of amortization for 2012 capital additions represented only a portion of the amortization variance from forecast. The most significant factor contributing to the 2012 amortization variance from forecast was the impact of the estimates, assumptions, and limitations on information affecting the amortization forecast for the transmission function.

The AESO notes that the amortization expense is the allocation of the costs of capital assets over their useful lives and does not represent the actual capital expenditures themselves. The AESO’s capital expenditures are managed through a portfolio management process that covers approval, development, and implementation. When an annual capital forecast is initially approved prior to a forecast year, a list of projects that are expected to occur in the forecast year is presented based on current knowledge and future business initiatives. The portfolio management process is then used throughout the year to manage the changes, additions, and deferrals of projects that may occur to reflect refinement and adjustment of business priorities and initiatives over time.