California Independent System Operator Corporation

Financial Statements
December 31, 2009 and 2008

California Independent System Operator Corporation
Table of Contents
December 31, 2009 and 2008

PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the Members of the Board of Governors
California Independent System Operator Corporation

In our opinion, the accompanying balance sheets and the related statements of revenues, expenses and changes in net assets and of cash flows present fairly, in all material respects, the financial position of the California Independent System Operator Corporation (the "Company") at December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The Management's Discussion and Analysis on pages 2 through 11 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

PricewaterhouseCoopers LLP

Sacramento, California
April 5, 2010

The following discussion and analysis of the California Independent System Operator Corporation (the Company) provides an overview of the Company's financial activities for the years ended December 31, 2009 and 2008. This discussion and analysis should be read in conjunction with the Company's financial statements and accompanying notes, which follow this section.

BACKGROUND

The Company is a nonprofit public benefit corporation incorporated in May 1997, and is responsible for the operation of the long-distance, high-voltage power lines that deliver electricity throughout most of California (the California grid) and to neighboring control areas and states, as well as with Canada and Mexico.

The Company's principal objective is to ensure the reliability of the California Grid, while fostering a competitive wholesale marketplace for electrical generation and related services in California. The Company operates pursuant to tariffs filed with the Federal Energy Regulatory Commission (FERC).

The Company operates a day-ahead market for transmission congestion, ancillary services and balancing energy, as well as real-time markets for ancillary services and balancing energy and administers reliability-must-run (RMR) contracts. RMR contracts allow the Company access to power at contractually agreed-upon prices from generation units which, due to their location and other factors, must be operated at certain times to ensure the local transmission reliability. The Company also performs a settlement and clearing function by collecting payments from users of these services and making pass-through payments to providers of such services.

The Company is governed by a Board of Governors (Board) composed of five members appointed by the California Governor and confirmed by the California State Senate.

Financial Reporting
The Company's accounting records are maintained in accordance with generally accepted accounting principles for proprietary funds as prescribed by the Governmental Accounting Standards Board (GASB) and, where not in conflict with GASB pronouncements, accounting principles prescribed by the Financial Accounting Standards Board (FASB).

Cash held by the Company on behalf of market participants is recorded in a restricted asset account with a corresponding liability due to market participants on the balance sheet. Market transactions are maintained in financial records separate from the Company and accordingly the financial results of these market transactions are not included in the financial statements of the Company.

Revenue and Rates
The Company charges a Grid Management Charge (GMC) to market participants to recover the Company's operating costs, capital expenditures and debt service costs, and to provide for an operating reserve.

The 2009 and 2008 unbundled GMC rates were comprised of the following six service categories: core reliability services; energy transmission services; forward scheduling; congestion management; market usage; and settlements, metering and client relations. The congestion management category was eliminated with the implementation of the new market on April 1, 2009.

The following table summarizes the pro forma bundled GMC rate based on the budgeted revenue requirement divided by the estimated control area transmission volume. As reflected in the table, the pro forma GMC rate has been stable during the past three years.

	2009	2008	2007
Revenue requirement in millions	$ 193.0	$ 191.6	$ 189.9
Pro forma GMC rate per MWh	0.776	0.755	0.760
Estimated volume in millions of MWh	248.6	253.7	250.0

Liquidity
The Company's rate structure provides for operating reserves which for 2009 and 2008 were fully funded for each service category. In July 2009, the Company issued $200.0 million of fixed rate revenue bonds for the construction of the Company's new headquarters and operations facility in Folsom, California.

In June 2008, the Company issued $197.0 million of fixed rate revenue bonds, (the 2008 Series Bonds). The proceeds of the 2008 bonds were used to refund all variable rate demand bonds outstanding at the time of issuance, fund debt service reserves related to the issued debt, and pay certain debt issuance costs. The remaining proceeds are being used to fund computer hardware and software systems, other facilities and equipment, and other planned capital projects. In connection with the issuance of the 2008 Series Bonds, the Company retired the interest rate swaps and bond insurance associated with the debt instruments that were refunded.

In order to mitigate the risk that an issuer of an investment will not fulfill its repayment obligation, the Company limits investments to those rated by a nationally recognized rating agency at the time of purchase with a short term rating of at least A-1 (or equivalent) for commercial paper and a long term rating of at least A- (or equivalent) for medium-term notes. The Company typically holds investments to maturity.

The Company recorded a mark-to-market gain of $2.4 million on the Company's investment portfolio for the year ended December 31, 2009 versus a loss of $4.1 million for the year ended December 31, 2008. The gain in 2009 was the result of the recovery of investment values of corporate bonds in 2009 from their values in 2008.

The New Market
The Company's new market became operational April 1, 2009. The new market was a significant initiative to improve the reliability, market operations and information systems of the California grid. The new market is comprised of major system components including:

- Day-Ahead Market - An integrated software process to account for hourly self-schedules and bids, reliability needs and market power mitigation in the 24-hour period before electricity flows in real time.
- Congestion Revenue Rights - Financial instruments that allow market participants to obtain risk protection from congestion charges in the day-ahead market.
- Scheduling Infrastructure Business Rules - A system that validates and publishes bids for information and use in other applications.
- Real-Time Market - A system that simultaneously optimizes energy and ancillary services based on locational marginal pricing (LMP), so that congestion is managed efficiently and reliably.
- Settlements and Market Clearing - An integrated set of systems that process settlement statements, billing, invoicing, cash clearing and credit business functions for the markets.
- State Estimator with a Full Network Model - A computer software program that provides a near real-time assessment of system conditions within the California grid.

The main benefits associated with the new market are:

- Enhanced Reliability – The new market provides transparent rules for buyers and sellers in California's wholesale electricity markets where prices reflect actual costs based on the physical flow of electricity on transmission lines. By creating a day-ahead market and scheduling process, the power flows over the next 24 hours are modeled according to the actual physical constraints so that risks of shortages and congestion on transmission lines are assessed and minimized.
- Improved Information - By providing transparent nodal marginal prices that reflect the true cost of energy and transmission, the new market reveals areas with congested transmission lines so that qualified entities can build new lines or generation resources, with the Company's coordination, to improve efficiency and reliability.
- Improved Cost Management - The alignment of costs with market activity provides for increased confidence in the Company-managed markets. The operating signals from LMP and the more efficient mix of resources identified by the day-ahead market are important cost management improvements.
- New Robust Technology - Replacing the dated computer infrastructure with new hardware, architecture and systems has provided the Company with greater functionality and flexibility. A new suite of systems provides more effective and reliable support for grid and market operations.

Payment Acceleration

The Company implemented payment acceleration beginning November 1, 2009, approximately 6 months after the new market went into service. Payment acceleration has reduced the time period between settlement trade dates and market clearing from approximately 90 days to less than 30 days. The shorter time period between trade date and the market clearing allows cash to be settled sooner thereby improving cash flow for timely recovery of GMC charges. Payment acceleration also reduces the risk to market participants in the event of a default or bankruptcy within the market.

New Headquarters Facility

The Company began construction of a new headquarters and operations facility on land the Company owns in Folsom, California, with a targeted completion date of 2011. To fund the development of this facility, the Company issued $200.0 million of fixed rate revenue bonds in July 2009. The building will be approximately 278,000 square feet composed of three wings and will include office space, conference rooms, training rooms, a cafeteria, shipping/receiving area, a control center, data center and a mechanical/equipment room. It has been designed to meet one of the higher standards of energy efficiency with reduced environmental impact.

Commitments and Contingencies

As part of the tariffs and applicable contracts, the Company has dispute resolution processes for market participants, transmission owners and RMR owners to register disagreements about information in the settlement statements or billing amounts for market and RMR activity. Once good faith efforts, known as good faith negotiations (GFN), have been made to negotiate and resolve disputes, written claims may be submitted either to mediation or arbitration. Several disputes and other claims, some of which are material in amount, have been filed with the Company and are in the process of being resolved. To date, all prior settlements, market adjustments and matters in GFN have been resettled against the market and the Company believes that any settlements or market adjustments relating to current disputes and the matters in GFN would be resettled against the market, as permitted by the tariff.

FINANCIAL HIGHLIGHTS

Balance Sheets, Statements of Revenues, Expenses and Changes in Net Assets

The financial statements provide both short-term and long-term information about the Company's financial status. The balance sheets include all of the Company's assets and liabilities, using the accrual method of accounting, and identify any assets which are restricted as a result of bond covenants or external commitments. The balance sheets provide information about the nature and amount of resources and obligations at specific points in time. The statements of revenues, expenses and changes in net assets report all of the Company's revenues and expenses during the year. The statements of cash flows report the cash provided and used during the year by operating activities, as well as other cash sources such as investment income and debt financing, and other cash uses such as payments for bond principal and capital additions.

Condensed Balance Sheets (in millions):

	2009	2008	2007
Assets			
Current assets	$ 553.7	$ 378.5	$ 331.7
Fixed assets, net	289.8	257.3	212.9
Other noncurrent assets	152.5	70.7	77.3
Total	$ 996.0	$ 706.5	$ 621.9
Liabilities and Net Assets			
Current liabilities	$ 401.6	$ 279.8	$ 276.2
Long-term debt	333.6	173.4	125.1
Other Noncurrent liabilities	14.2	12.5	13.1
Net assets	246.6	240.8	207.5
Total	$ 996.0	$ 706.5	$ 621.9

Assets

Current Assets (in millions):

	2009	2008	2007
Cash and cash equivalents	$ 443.0	$ 298.3	$ 220.8
Investments	62.4	21.5	58.5
Accounts receivable and other assets	48.3	58.7	52.4
Total	$ 553.7	$ 378.5	$ 331.7

2009 Compared to 2008 - Current assets amounted to $553.7 million at December 31, 2009, an increase of $175.2 million during the year. The increase in cash, cash equivalents, and investments of $144.7 million is primarily related to an increase of $106.3 million in amounts restricted for market participants, an increase of $8.1 million in bond proceeds restricted for debt service, and cash provided by operations of $35.7 million. The increases were partially offset by decreases in cash, cash equivalents and investments primarily related to a decrease in capital service funds of $5.5 million due to movement of funds to longer term investments. Accounts receivable and other assets decreased by $10.4 million due primarily to lower GMC receivables at the end of 2009 as compared to 2008 because of shorter GMC collection periods resulting from payment acceleration.

2008 Compared to 2007 - Current assets amounted to $378.5 million at December 31, 2008, an increase of $48.8 million during the year. The increase in cash, cash equivalents, and investments of $40.5 primarily related to an increase of $24.0 million of bond proceeds restricted for capital expenditures, an increase of $32.9 million in amounts restricted for market participants and cash provided by operations of $81.1 million. The increases were partially offset by decreases in cash, cash equivalents and investments primarily related to decrease in debt service funds of $45.9 million arising from the refinancing of the bonds and $52.8 million used for fixed assets. Accounts receivable and other assets increased by $7.3 million due primarily to higher GMC receivables at the end of 2008 as compared to 2007 and increases in other current assets from prepaid amounts.

Fixed Assets, net (in millions):

	2009	2008	2007
Net assets in service	$ 205.7	$ 34.1	$ 33.1
Work-in-progress	84.1	223.2	179.8
Total	$ 289.8	$ 257.3	$ 212.9

2009 Compared to 2008 - The Company has invested $289.8 million in fixed assets and work-in-progress, net of accumulated depreciation, at December 31, 2009. During 2009, the assets comprising the Company's new market systems were placed in service and moved from work-in-progress. The Company also capitalized $79.6 million of additions to work-in–progress in 2009, primarily for the costs associated with the new headquarters facility and other projects.

In 2009, the Company also wrote off assets with a net book value of $6.4 million. The assets were related to software and hardware that were used to run the markets, along with assets related to the new headquarters building. As the new market was being implemented in 2009, the Company determined that certain software and hardware components were not performing as expected and made the decision to abandon the assets and replace them. Additionally, design studies done in 2000 related to the new headquarters building were abandoned as these were not consistent with the Company's security and space needs and current environmental strategy.

2008 Compared to 2007 - The Company has invested $257.3 million in fixed assets and work-in-progress, net of accumulated depreciation, at December 31, 2008. During 2008, the Company capitalized $56.7 million of additions to fixed assets, including additions to work-in–progress that relate to the Company's new market systems. The internally developed software related to the new market was substantially complete and capitalization ceased on December 1, 2008.

Other Noncurrent Assets (in millions):

	2009	2008	2007
Investments	$ 145.2	$ 65.7	$ 70.4
Other assets	7.3	5.0	6.9
Total	$ 152.5	$ 70.7	$ 77.3

2009 Compared to 2008 -Other noncurrent assets amounted to $152.5 million at December 31, 2009, an increase of $81.8 million during the year, principally related to funds from the 2009 bond offering that were invested long-term.

2008 Compared to 2007 - Other noncurrent assets amounted to $70.7 million at December 31, 2008, a decrease of $6.6 million during the year, principally related to a decrease in the value of corporate notes.

Liabilities

Current Liabilities (in millions):

	2009	2008	2007
Accounts payable and accrued expenses	$ 28.8	$ 14.0	$ 16.8
Accrued salaries and compensated absences	25.7	22.3	19.9
Current portion of long-term debt	39.1	31.0	64.6
Due to market participants	262.1	155.8	122.9
Generator non-compliance fines refund obligation	45.9	56.7	52.0
Total	$ 401.6	$ 279.8	$ 276.2

2009 Compared to 2008 -Current liabilities amounted to $401.6 million at December 31, 2009, an increase of $121.8 million during the year. Accounts payable and accrued expenses increased by $14.8 million primarily due to accrued costs for the headquarters facility project. Amounts due to market participants increased by $106.3 million primarily due to an increase in collateral deposits of $103.8 million, as a result of the collateral requirements for participants of the 2010 annual congestion revenue rights auction. In addition, generator interconnection study deposits increased by $2.7 million. Generator noncompliance fines refund obligation decreased $10.8 million due to the FERC ruling that reduced the estimated liability (recorded as an interest expense recovery) and additional interest expense related to the 2009 year of $2.0 million on the remaining refund amounts.

2008 Compared to 2007 - Current liabilities amounted to $279.8 million at December 31, 2008, an increase of $3.6 million during the year. Amounts due to market participants increased by $32.9 million primarily related to increases in generator interconnection study deposits of $45.0 million offset by decreases in other restricted market participant funds of $12.1 million. Generator noncompliance fines refund obligation increased $4.7 million due to additional accrued interest on the related refund.

Long-Term Debt (in millions):

Summarized activity of long-term debt for the year ended December 31, 2009, is as follows (in thousands):

	Beginning of Year	Issuance/ (Payments)	End of Year
CIEDB Revenue Bonds, Series 2008	$ 197.0	$ (31.0)	$ 166.0
CIEDB Revenue Bonds, Series 2009	-	200.0	200.0
Total long-term debt	$ 197.0	$ 169.0	$ 366.0

Summarized activity of long-term debt for the year ended December 31, 2008, is as follows (in thousands):

	Beginning of Year	Issuance/ (Payments)	End of Year
CIEDB Revenue Bonds, Series 2008	$ -	$ 197.0	$ 197.0
CIEDB VRDBs			
Series 2007	60.0	(60.0)	-
Series 2004	84.4	(84.4)	-
Series 2000	45.3	(45.3)	-
Total long-term debt	$ 189.7	$ 7.3	$ 197.0

Debt service requirements below reflect scheduled maturities of long-term debt at December 31, 2009. Interest is calculated using the stated fixed rate of the bonds. As of December 31, 2009, the Company had an underlying rating of A from S&P, A2 by Moody's and AA- by Fitch.

	Principal	Interest	Total
Debt Service Requirements			
2010	$ 39.1	$ 17.7	$ 56.8
2011	42.3	15.6	57.9
2012	28.6	14.3	42.9
2013	39.6	12.4	52.0
2014	27.1	11.0	38.1
2015-2039	189.3	170.0	359.3
Total	$ 366.0	$ 241.0	$ 607.0

2009 Compared to 2008 - At December 31, 2009, the Company had $366.0 million of outstanding bonds issued through the California Infrastructure and Economic Development Bank (CIEDB). The increase in long-term debt was primarily attributable to the issuance of new bonds which included additional debt to finance the construction of a new headquarters facility, and which was partially offset by the scheduled payments on the 2008 bonds.

2008 Compared to 2007 - At December 31, 2008, the Company had $197.0 million of outstanding bonds issued through the CIEDB. Included in the balance is an unamortized premium on the 2008 bonds of $7.4 million. The increase in long-term debt was primarily attributable to the issuance of new bonds which included additional debt to finance capital projects.

Other Noncurrent Liabilities (in millions):

	2009	2008	2007
Derivative liability	$ -	$ -	$ 1.4
Employee retirement plan obligations	14.2	12.5	11.7
Total	$ 14.2	$ 12.5	$ 13.1

2009 Compared to 2008 - Other noncurrent liabilities amounted to $14.2 million at December 31, 2009, an increase of $1.7 million during the year as a result of increases in employee retirement plan obligations, which was attributable to the excess of plan costs over current year funding.

2008 Compared to 2007 - Other noncurrent liabilities amounted to $12.5 million at December 31, 2008, a decrease of $0.6 million during the year. The overall decrease was the result of the termination of the interest rate swap (the derivative liability) of $1.4 million during 2008 in connection with the bond refunding, partially offset by an increase in employee retirement plan obligations of $0.8 million which was attributable to the excess of plan costs over current year funding.

Net Assets (in millions):

	2009	2008	2007
Invested in capital assets, net of related debt	$ 115.5	$ 136.2	$ 81.5
Restricted	-	1.6	43.5
Unrestricted	131.1	103.0	82.5
Total	$ 246.6	$ 240.8	$ 207.5

2009 Compared to 2008 - Net assets invested in capital assets, net of related debt, amounted to $115.5 million at December 31, 2009, a decrease of $20.7 million during the year. The decrease was attributable primarily to the increase in accounts payable and accrued expenses for capitalized costs. Unrestricted net assets amounted to $131.1 million at December 31, 2009, an increase of $28.1 million during the year, due primarily to the decrease in the generator fines liability of $12.8 million and net changes reflected in the other two categories.

2008 Compared to 2007 – Net assets invested in capital assets, net of related debt, amounted to $136.2 million at December 31, 2008, an increase of $54.7 million during the year. The increase was attributable primarily to the capitalized costs funded from unrestricted funds. Restricted net assets amounted to $1.6 million at December 31, 2008, a decrease of $41.9 million from the year prior, which was primarily attributable to lower bond sinking requirements of the 2008 revenue bonds as compared to the requirements for the bonds that were refunded. Unrestricted net assets amounted to $103.0 million at December 31, 2008, an increase of $20.5 million during the year, due primarily to a surplus of revenues over expenses in 2008, partially offset by the net changes reflected in the other two categories.

Changes in Net Assets

Condensed Statement of Revenues, Expenses and Changes in Net Assets (millions):

	2009	2008	2007
Operating revenues	$ 208.3	$ 200.7	$ 200.6
Operating expenses	213.1	161.8	153.8
Operating (loss) income	(4.8)	38.9	46.8
Other income (expenses)	10.5	(5.6)	(0.6)
Total	$ 5.7	$ 33.3	$ 46.2

Operating Revenues

2009 Compared to 2008 - Total operating revenues in 2009 increased by $7.6 million due primarily to higher than expected volumes in the new day-ahead market. This resulted in higher revenues in some GMC rate categories as compared to 2008.

2008 Compared to 2007 - Total operating revenues in 2008 were substantially the same as in 2007. In 2008, GMC from regular operations for the year was $194.8 million. GMC from regular operations in 2008 was higher than in 2007 due primarily to higher volumes of activity related to certain billing determinants. In 2007, GMC from regular operations was $187.7 million. The 2007 GMC revenue also included $7.1 million of GMC amounts from San Diego Gas and Electric Company (SDG&E), as a result of a settlement, which did not recur in 2008.

Operating Expenses and Percentages (dollars in millions):

	2009	2008	2007
Salaries and related benefits	$ 107.4	$ 91.6	$ 83.5
Communication and technology costs	20.9	23.9	21.5
Legal and consulting costs	18.3	15.7	16.6
Other: leases, facilities and administrative	17.3	17.8	17.2
Abandonment and loss on retirement of assets	6.4	-	-
Depreciation and amortization	42.8	12.8	15.0
Total	$ 213.1	$ 161.8	$ 153.8
Salaries and related benefits	50.4 %	56.5 %	54.3 %
Communication and technology costs	9.8	14.8	14.0
Legal and consulting costs	8.6	9.7	10.7
Other: leases, facilities and administrative	8.1	11.0	11.2
Abandonment and loss on retirement of assets	3.0	-	-
Depreciation and amortization	20.1	8.0	9.8
Total	100.0 %	100.0 %	100.0 %

2009 Compared to 2008 - Operating expenses were $213.1 million in 2009, $51.3 million higher than in 2008. The increase in 2009 as compared to 2008 is primarily attributable to higher depreciation expense of the new market assets placed in service and to the depreciation expense associated with the abandonment and retirement of assets. In addition, total salaries and related benefits increased due to higher number of employees in 2009 as compared to 2008 and higher overtime in connection with the implementation of the new market.

2008 Compared to 2007 - Operating expenses were $161.8 million in 2008, $8.0 million higher than in 2007. The increase in 2008 as compared to 2007 is primarily attributable to higher total salaries and related benefits resulting from an increase in the number of employees.

Other Income (Expense) (in millions):

	2009	2008	2007
Interest income	$ 7.3	$ 3.7	$ 13.1
Interest expense	(9.6)	(8.9)	(11.9)
Interest expense recovery	12.8	-	-
Change in derivative valuation	-	(0.4)	(1.8)
Total	$ 10.5	$ (5.6)	$ (0.6)

2009 Compared to 2008 - Interest income was $3.6 million higher in 2009 compared to 2008 due primarily to the partial recovery of the financial markets which resulted in the recognition of $2.4 million of gains on investments as compared to the $4.1 million loss in 2008. This was partially offset by lower interest income on restricted funds of $1.2 million due to lower interest rates. Interest expense increased by $0.7 million, primarily due to higher outstanding debt in 2009 which increased interest expense on bonds by $3.9 million, and which was partially offset by a reduction in other interest expenses. The interest expense recovery of $12.8 million recognized in 2009 was the result of a FERC ruling (as further described above under current liabilities). The Company did not own any derivative financial instruments in 2009.

2008 Compared to 2007 - Interest income was $9.4 million lower in 2008 compared to 2007 due primarily to lower interest earnings caused by lower interest rates of $3.4 million, a loss of $4.1 million from the mark-to-market of investments and $1.9 million of interest income recorded in 2007 related to the SDG&E settlement that did not recur in 2008. Interest expense was $3.0 million lower in 2008 versus 2007. The decreased expense was primarily due to 2008 bond premium amortization of $2.4 million which did not exist in 2007, $1.8 million decrease in interest on generator fines driven primarily from lower FERC interest rates and $1.2 million increase in capitalized interest on work in progress. The change in derivative valuation in 2008 is due to the lower mark-to-market on the swaps during the period they were outstanding in 2008 as compared to 2007.

California Independent System Operator Corporation
Balance Sheets
December 31, 2009 and 2008

($ in thousands)

	2009	2008
Assets		
Current assets:		
Cash and cash equivalents, including restricted amounts	$ 442,996	$ 298,312
Accounts receivable	39,155	51,582
Short-term investments, including restricted amounts	62,427	21,496
Other current assets	9,137	7,117
Total current assets	553,715	378,507
Noncurrent assets:		
Long-term investments, including restricted amounts	145,215	65,715
Fixed assets, net	289,772	257,253
Other assets	7,340	5,023
Total noncurrent assets	442,327	327,991
Total assets	$ 996,042	$ 706,498
Liabilities and Net Assets		
Current liabilities:		
Accounts payable and accrued expenses	$ 28,766	$ 13,990
Accrued salaries and compensated absences	25,683	22,345
Current portion of long-term debt	39,100	31,000
Due to market participants	262,099	155,767
Generator noncompliance fines refund obligation	45,956	56,685
Total current liabilities	401,604	279,787
Noncurrent liabilities:		
Long-term debt, net of current portion	333,679	173,372
Employee retirement plan obligations	14,203	12,495
Total noncurrent liabilities	347,882	185,867
Total liabilities	749,486	465,654
Commitments and contingencies		
Net assets		
Invested in capital assets, net of related debt	115,449	136,189
Restricted	-	1,616
Unrestricted	131,107	103,039
Total net assets	246,556	240,844
Total liabilities and net assets	$ 996,042	$ 706,498

The accompanying notes are an integral part of these financial statements.

California Independent System Operator Corporation
Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2009 and 2008

($ in thousands)

	2009	2008
Operating revenues:		
GMC revenue	$ 202,353	$ 194,841
Other revenues	6,001	5,903
Total operating revenues	208,354	200,744
Operating expenses:		
Salaries and related benefits	107,439	91,638
Equipment leases and facility costs	8,681	9,615
Communications, technology and temporary staffing contracts	20,942	23,912
Legal and consulting services	18,312	15,678
Training, travel and professional dues	3,670	3,585
Insurance, administrative and other expenses	4,917	4,503
Abandonment and loss on retirement of assets	6,362	-
Depreciation and amortization	42,784	12,822
Total operating expenses	213,107	161,753
(Loss) income from operations	(4,753)	38,991
Other income (expense):		
Interest income	7,321	3,729
Interest expense	(9,699)	(9,359)
Interest expense recovery	12,843	-
Total other income (expense)	10,465	(5,630)
Change in net assets	5,712	33,361
Net assets, beginning of year	240,844	207,483
Net assets, end of year	$ 246,556	$ 240,844

The accompanying notes are an integral part of these financial statements.

California Independent System Operator Corporation
Statements of Cash Flows
Years Ended December 31, 2009 and 2008

($ in thousands)

	2009	2008
Cash flows from operating activities:		
Receipts from scheduling coordinators for GMC	$ 214,780	$ 192,586
Other receipts	6,001	5,903
Payments to employees and to others for related benefits	(104,037)	(88,589)
Payments to vendors/others	(57,635)	(63,576)
Receipts from market participants	505,626	168,496
Payments to market participants	(399,294)	(135,648)
Net cash provided by operating activities	165,441	79,172
Cash flows from noncapital financing activities:		
Repayment of bonds	(2,195)	(16,352)
Interest on debt	(16)	(142)
Net cash used in noncapital financing activities	(2,211)	(16,494)
Cash flows from capital and related financing activities:		
Purchases and development of fixed assets	(70,319)	(57,750)
Proceeds from issuance of bonds	199,940	202,722
Repayment of bonds	(28,805)	(173,348)
Interest on debt	(5,666)	(2,614)
Net cash provided by (used in) capital financing activities	95,150	(30,990)
Cash flows from investing activities:		
Purchases of investments	(160,420)	(209,648)
Sales and maturities of investments	39,989	251,349
Interest received	6,735	4,148
Net cash (used in) provided by investing activities	(113,696)	45,849
Net increase in cash and cash equivalents, restricted and unrestricted	144,684	77,537
Cash and cash equivalents, restricted and unrestricted, beginning of year	298,312	220,775
Cash and cash equivalents, restricted and unrestricted, end of year	$ 442,996	$ 298,312

The accompanying notes are an integral part of these financial statements.

California Independent System Operator Corporation
Statements of Cash Flows
Years Ended December 31, 2009 and 2008

($ in thousands)

(continued)	2009	2008
Supplemental information:		
Cash paid for interest	$ 8,919	$ 5,502
Reconciliation of income from operations to net cash provided by operating activities		
(Loss) income from operations	$ (4,753)	$ 38,991
Adjustments to reconcile (loss) income from operations to net cash provided by operating activities:		
Depreciation and amortization	42,784	12,822
Abandonment and loss on retirement of assets	6,362	-
Changes in operating assets and liabilities:		
Accounts receivable and other assets	12,427	(3,934)
Accounts payable and other accrued expenses	2,289	(1,555)
Due from market participants	106,332	32,848
Net cash provided by operating activities	$ 165,441	$ 79,172
Supplemental disclosure of noncash financing and investing activities		
Amortization of bond premium	$ 2,591	$ 1,786
Amortization of bond issuance costs and loss of refunding	(745)	(844)
Change in valuation of derivative financial instruments	-	(400)
Generator fines interest included in interest expense	(2,114)	(4,682)
Generator fines interest expense recovery	12,843	-
Change in purchases and development of fixed assets included in accounts payable and accrued expenses	10,281	(2,249)

The accompanying notes are an integral part of these financial statements.

1. Organization and Operations

The Company, a nonprofit public benefit corporation incorporated in May 1997, is responsible for the operation of the long-distance, high-voltage power lines that deliver electricity throughout the California grid and to neighboring control areas and states, as well as with Canada and Mexico. The Company charges a GMC to market participants to recover the Company's costs and to provide an operating reserve. The Company's principal objective is to ensure the reliability of the California grid, while fostering a low-cost wholesale marketplace for electrical generation and related services in California. The Company operates pursuant to tariffs filed with the FERC.

The Company operates a day-ahead market for transmission congestion, ancillary services and balancing energy as well as real-time markets for ancillary services and balancing energy, and administers RMR contracts. RMR contracts allow the Company access to power at contractually agreed-upon prices from generation units which, due to their location and other factors, must be operated at certain times to ensure the reliability of local transmission. The Company also performs a settlement and clearing function by collecting payments from users of these services and making pass-through payments to providers of such services. Cash held by the Company on behalf of market participants is recorded in a restricted asset account with a corresponding liability due market participants on the balance sheet. Except as noted above, market transactions are maintained in financial records separate from the Company, and accordingly, the financial results of these market transactions are not included in the financial statements of the Company. GMC revenues have a priority claim against any market-related receipts. Any market defaults are allocated to market participants.

The Board of the Company is composed of five members appointed by the California Governor and subject to and confirmed by the California State Senate.

2. Summary of Significant Accounting Policies

Method of accounting
The accompanying financial statements have been prepared on an accrual basis of accounting in accordance with accounting principles for proprietary funds as prescribed by the GASB, and where not in conflict with GASB pronouncements, accounting principles prescribed by the FASB. The Company uses the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Use of estimates
The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. In particular, the Company's results of operations and financial position are materially affected by the management estimates associated with generator noncompliance fines, as discussed in Note 6. Actual results could materially differ from these, and other, estimates.

Cash and cash equivalents
Cash and cash equivalents, restricted and unrestricted, include cash on hand, governmental securities, commercial paper, money market investments, mutual funds and certificates of deposit and other highly liquid investments with original maturities of three months or less. Cash and cash equivalents are unrestricted unless specifically restricted by bond indentures or tariff.

Accounts receivable and revenue recognition
The GMC is based on rates filed with FERC and is designed to recover the Company's operating costs, capital expenditures, debt service costs, and to provide for an operating reserve. The GMC and other market service billings are recognized as revenue, based on estimated meter data submitted by market participants and therefore, may be subject to adjustment after final invoices have been issued.

The 2009 and 2008 GMC rates were comprised of the following service categories: core reliability services; energy transmission services; forward scheduling; congestion management; market usage; and settlements, metering and client relations. The congestion management category was eliminated with the implementation of the new market on April 1, 2009.

The operating reserve is calculated separately for each GMC service category and accumulates until the reserve becomes fully funded (at 15 percent of budgeted annual operating costs for each rate service category). At December 31, 2009, the operating reserve for each service category was fully funded. In accordance with the tariff, any surplus operating reserve balance is applied as a reduction in revenue requirements in the following year. The tariff requires GMC rates to be adjusted not more than once per quarter in the event that billing determinant volumes differ by more than five percent from those projections used to set rates. During 2009 and 2008, adjustments were made to certain GMC rates pursuant to these provisions.

Generator interconnection studies
The Company is responsible for conducting generator interconnection studies. The project sponsors are the owners of generating plants planning to become connected to the California grid. The project sponsors request the Company to conduct these studies and they are required to make a deposit before any studies are performed. At any time, the project sponsors may withdraw from the studies and have the right to some or all of the remaining unapplied deposits.

In accordance with the tariff, the Company charges the project sponsors the actual costs of the studies. Related study costs include both internal costs and external costs and are recorded, when incurred, as operating expenses. As costs are incurred, the Company recognizes revenue for the same amount, which is recorded as a component of other revenues. The Company applies the deposits against the related receivable once the studies are completed.

Generator noncompliance fines
From December 8, 2000 through June 30, 2001, the Company assessed noncompliance fines on participating generators that failed to fully comply with dispatch instructions when the Company was seeking to prevent an imminent or threatened system emergency. In accordance with the tariff, these fines are retained by the Company. The Company recorded the net realizable amount of such fines as revenue when the underlying noncompliance event occurred, and adjusts such amounts in recognition of evolving factors affecting the ultimate recognition of the fines charged.

Investments
Investments include government and federal agency securities, corporate bonds, guaranteed investment contracts, (GICs) and forward delivery agreements with maturities of more than three months. Investments are carried at fair value except for the GIC and a forward delivery agreement. The GIC and the forward delivery agreement are nonparticipating investment contracts that cannot be negotiated or transferred and their redemption terms do not consider market rates. As a result, these investments are carried at cost. Income on investments and the gain or loss from the mark-to-market on investments is recorded as a component of interest income.

Fixed assets
Fixed assets are recorded at cost. Depreciation is computed using the straight-line method over the assets' estimated useful lives. Most of the Company's investment in fixed assets consists of information systems which are being depreciated over useful lives of three to five years. The cost of improvements to or replacement of fixed assets is capitalized. Interest incurred during development is capitalized. When assets are retired or otherwise disposed of, the cost and related depreciation are removed from the accounts and any resulting gain or loss is reflected in the Company's statement of changes in revenues, expenses and changes in net assets for the period. Repairs and maintenance costs are expensed when incurred. The Company capitalizes direct costs of salaries and certain indirect costs incurred to develop or obtain software for internal use. Costs incurred related to software development during the preliminary stage of a project and training and maintenance costs are expensed as incurred. Costs related to abandoned projects are expensed when the decision to abandon is made.

Other assets
Other assets consist primarily of debt issuance costs that are amortized over the life of the bonds using the bonds outstanding method (which approximates the effective interest method). Other assets also include a loan to an officer (see Note 5) and certain employee retirement plan trust accounts.

Compensated absences
The Company accrues vacation leave when the employee becomes eligible to the benefit. The Company does not record sick leave or other leave as a liability since there are no cash payments for sick leave or other leave made when employees terminate or retire. At December 31, 2009 and 2008, the total accrued liability for vacation was $6.7 million and $5.9 million, respectively.

Income taxes
The Company is exempt from federal income tax under Section 501(c) (3) of the U.S. Internal Revenue Service (IRS) Code and is exempt from California State franchise income taxes.

Net assets
The Company classifies its net assets into three components:

- **Invested in capital assets, net of related debt** – This component of net assets consists of capital assets, net of accumulated depreciation reduced by the outstanding debt balances, net of unamortized debt expenses.
- **Restricted** – This component consists of net assets with constraints placed on their use. Constraints include those imposed by debt covenants (excluding amounts considered in net capital, above) and by the Company's tariff and agreements with external parties.
- **Unrestricted** – This component of net assets consists of net assets that do not meet the definition of "invested in capital, net of related debt" or "restricted".

Concentration of credit risk
Financial instruments that subject the Company to credit risk consist primarily of accounts receivable relating to GMC billings due from market participants and cash and cash equivalents and investments.

All of the Company's receivables are due from entities in the energy industry, including utilities, generation owners and other electricity market participants. For the years ended December 31, 2009 and 2008, approximately 62 percent and 54 percent, respectively, of GMC revenues were from two market participants.

GMC revenues have a priority claim against any market-related receipts, which means that even if an entity defaults on an invoice containing a GMC charge, the Company receives the full GMC so long as sufficient funds were received on other market invoices.

The Company's concentration of credit risk related to cash and cash equivalents, and investments is described in Note 3.

Presentation
Certain reclassifications have been made to the 2008 presentation to conform to the 2009 presentation.

Subsequent events
The Company evaluates events or transactions that occur after the balance sheet date but before financial statements are issued for potential recognition or disclosure in the financial statements. The Company has evaluated all subsequent events through April 5, 2010, the date the financial statements were issued, and no items were noted that need to be disclosed.

3. Cash and Cash Equivalents and Investments

Cash and cash equivalents and investments
The Company's investment policy restricts investments to obligations that are unconditionally guaranteed by the United States (U.S.) government or its agencies or instrumentalities, municipal and state obligations or tax-exempt obligations, bankers' acceptances, certificates of deposit, repurchase agreements, general obligation bonds of corporations, commercial paper, GICs and forward delivery agreements. Additionally, bond sinking and reserve fund portfolios are invested in accordance with the trust agreements pursuant to the bond indenture. The Company's investment policy includes restrictions for investments relating to maximum amounts invested as a percentage of the total portfolio and maximum maturities and minimum credit ratings.

Credit risk
To mitigate the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment, the Company limits purchases of investments to those rated at the time of purchase by a nationally recognized rating agency of at least A-1 (or equivalent) for commercial paper and at least A- (or equivalent) for medium-term notes.

Interest rate risk
It is the policy of the Company to diversify its overall investment portfolio. Investments are diversified in order to avoid losses that may result from an over concentration of assets by type, issuer or maturity. Of the Company's total portfolio at December 31, 2009 and 2008, all of the Company's cash and cash equivalents have maturities of 90 days or less. The investments have a maximum maturity of five years with the exception of bond reserve funds which are invested in accordance with the terms of the related bond indenture.

Concentration of credit risk

This is the risk of loss associated with the percentage of an entity's investment in a single issuer. The Company's investment policy limits investments by asset class. In 2009 and 2008, investments with issuers comprising more than five percent of the Company's total investment portfolio are noted below:

	2009	**2008**
Federal National Mortgage Association (FNMA)	13%	9%
Morgan Stanley	9%	23%
Federal Home Loan Mortgage Corporation (FHLMC)	8%	16%
Federal Home Loan Bank (FHLB)	7%	-
Citbank	7%	-

Custodial credit risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Company will not be able to recover the value of its deposits, investments or collateral securities that are in the possession of an outside party.

Individual securities purchased by the Company are currently held in a custodial account by a third party custodian. All cash and investments related to the 2008 and 2009 bond series are held by a trustee. All investments are registered in the Company’s name.

The Company had uninsured and uncollateralized bank deposits in amounts of $1.6 million and $1.9 million at December 31, 2009 and 2008, respectively.

Summary of Balances

At December 31, 2009, the Company's cash, cash equivalents and investments consist of the following (in thousands):

Description	Credit Rating*	Remaining Maturities (in Years) Less than 1	1 - 5	More than 5	Total Fair Value
Cash and cash equivalents					
Unrestricted					
Bank overdrafts		$ (402)	$ -	$ -	$ (402)
Money market funds	*AAAm*	115,575	-	-	115,575
		115,173	-	-	115,173
Restricted					
Deposits		267	-	-	267
Money market funds	*AAAm*	327,556	-	-	327,556
		327,823	-	-	327,823
Total cash and cash equivalents		442,996	-	-	442,996
Investments					
Short-term investments - restricted					
FNMA	*AAA*	21,916	-	-	21,916
FHLB	*AAA*	9,705	-	-	9,705
FFCB	*AAA*	8,522	-	-	8,522
US Treasury	*AAA*	22,284	-	-	22,284
Total short-term investments		62,427	-	-	62,427
Long-term investments					
Unrestricted					
Preferred and common stock	*N/A*	-	-	37	37
FNMA	*AAA*	-	4,697	-	4,697
FHLMC	*AAA*	-	15,805	-	15,805
FHLB	*AAA*	-	4,706	-	4,706
US Treasury	*AAA*	-	29,438	-	29,438
Corporate Notes					
	AA-	-	17,079	-	17,079
	A+	-	11,235	-	11,235
	A	-	9,883	-	9,883
	AA	-	5,524	-	5,524
	A-	-	5,466	-	5,466
	BBB+	-	3,053	-	3,053
	AAA	-	2,626	-	2,626
	AA+	-	1,026	-	1,026
		-	110,538	37	110,575
Restricted					
GIC	*Not Rated*	-	19,697	-	19,697
Forward delivery agreement	*Not Rated*	-	-	14,943	14,943
		-	19,697	14,943	34,640
Total long-term investments		-	130,235	14,980	145,215
Total investments		62,427	130,235	14,980	207,642
Total cash, cash equivalents and investments		$ 505,423	$ 130,235	$ 14,980	$ 650,638

** S&P Rating, if available, or Fitch*

At December 31, 2008, the Company's cash, cash equivalents and investments consist of the following (in thousands):

Description	Credit Rating*	Remaining Maturities (in Years) Less than 1	1 - 5	More than 5	Total Fair Value
Cash and cash equivalents					
Unrestricted					
Bank overdrafts		$ (1,162)	$ -	$ -	$ (1,162)
Money market funds	*Unrated*	-	-	-	-
Money market funds					
	AAA	18,703	-	-	18,703
	AAAm	61,923	-	-	61,923
		79,464	-	-	79,464
Restricted					
Deposits		300	-	-	300
Money market funds	*AAAm*	218,548	-	-	218,548
		218,848	-	-	218,848
Total cash and cash equivalents		298,312	-	-	298,312
Investments					
Short-term investments					
Unrestricted					
FHLMC	*AAA*	14,042	-	-	14,042
Restricted					
Forward delivery agreements	*AAA/Aaa*	-	-	-	-
FNMA	*AAA*	7,454	-	-	7,454
Total short-term investments		21,496	-	-	21,496
Long-term investments					
Unrestricted					
Preferred and common stock	*N/A*	-	-	37	37
FFCB	*AAA*	-	3,064	-	3,064
FNMA	*AAA /Aaa*	-	-	-	-
FHLMC	*AAA /Aaa*	-	-	-	-
FHLB	*AAA /Aaa*	-	-	-	-
Corporate notes					
	AA	-	12,362	-	12,362
	A+	-	11,506	-	11,506
	AA-	-	7,662	-	7,662
	A	-	4,269	-	4,269
	AAA	-	3,372	-	3,372
	BBB+	-	2,529	-	2,529
	BBB	-	1,217	-	1,217
		-	45,981	37	46,018
Restricted					
GIC	*Not Rated*	-	19,697	-	19,697
Total long-term investments		-	65,678	37	65,715
Total investments		21,496	65,678	37	87,211
Total cash, cash equivalents and investments		$ 319,808	$ 65,678	$ 37	$ 385,523

** S&P Rating, if available, or Fitch*

The Company's cash, cash equivalents and investments at December 31 consist of unrestricted and restricted funds as follows (in thousands):

	2009	2008
Unrestricted funds, operating account	$ 171,103	$ 139,525
Restricted funds:		
Market participants	262,099	155,767
Debt service	58,629	29,778
Capital expenditures	158,807	60,453
Total	$ 650,638	$ 385,523

Cash and cash equivalents restricted for market participants consist of the following at December 31 (in thousands):

	2009	2008
Security deposits	$ 124,743	$ 46,931
Market funds pending settlement	69,079	27,239
Pass-through fees due to others	10,195	26,058
Generator interconnection study deposits	58,082	55,539
Total amounts restricted for market participants	$ 262,099	$ 155,767

Cash and cash equivalents restricted for market participants consist of amounts held by the Company to be remitted to market participants or others on their behalf. Security deposits are amounts received from market participants who are required to post collateral for their transactions in the Company's markets. Market funds pending settlement consist of amounts collected during the settlement and clearing function that will pass through to market participants in subsequent periods. A portion of the market funds pending settlement ($18.2 million at December 31, 2009 and 2008) is being held pending resolution of the FERC Refund Case (Note 12). Pass-through fees due to others consist of amounts collected from market participants that will be paid to market participants for summer reliability, startup costs and emission costs. Generator interconnection study deposits are amounts collected for future studies.

4. Fixed Assets

Changes in the Company's fixed assets for the year ended December 31, 2009, are as follows (in thousands):

	2008	Additions and Transfers In	Deletions and Transfers Out	2009
Nondepreciable fixed assets:				
Land	$ 7,617	$ -	$ -	$ 7,617
Work-in-progress	215,564	79,628	(218,754)	76,438
	223,181	79,628	(218,754)	84,055
Depreciable fixed assets:				
Grid, market and settlement software	175,669	204,627	(79,884)	300,412
Enterprise and support software	30,381	4,533	(2,775)	32,139
Computer hardware and other equipment	29,505	8,759	(6,697)	31,567
Leasehold improvements	16,937	551	-	17,488
Furniture, fixtures and other	10,426	284	(53)	10,657
	262,918	218,754	(89,409)	392,263
Less: accumulated depreciation	(228,846)	(42,784)	85,084	(186,546)
	34,072	175,970	(4,325)	205,717
Total fixed assets, net	$ 257,253	$ 255,598	$ (223,079)	$ 289,772

Changes in the Company's fixed assets for the year ended December 31, 2008, are as follows (in thousands):

	2007	Additions and Transfers In	Deletions and Transfers Out	2008
Nondepreciable fixed assets:				
Land	$ 7,617	$ -	$ -	$ 7,617
Work-in-progress	172,250	57,296	(13,982)	215,564
	179,867	57,296	(13,982)	223,181
Depreciable fixed assets:				
Grid, market and settlement software	172,097	3,936	(364)	175,669
Enterprise and support software	37,165	1,363	(8,147)	30,381
Computer hardware and other equipment	26,382	6,610	(3,487)	29,505
Leasehold improvements	15,271	1,666	-	16,937
Furniture, fixtures and other	10,714	407	(695)	10,426
	261,629	13,982	(12,693)	262,918
Less: accumulated depreciation	(228,569)	(12,822)	12,545	(228,846)
	33,060	1,160	(148)	34,072
Total fixed assets, net	$ 212,927	$ 58,456	$ (14,130)	$ 257,253

The Company capitalized interest related to the development of fixed assets of $4.4 million and $4.5 million for the years ending December 31, 2009 and 2008, respectively. The 2009 amount includes a reduction of $1.1 million for income earned on unspent debt proceeds. There were no such amounts in 2008. The new market system was placed into operation on April 1, 2009 and as a result, $198.6 million of assets were moved from work-in-progress and placed in service.

For the year ended December 31, 2009, the Company recorded $6.4 million in abandonment and loss on retirement expenses. The assets that were abandoned in 2009 were software and hardware that were used in running the markets and certain assets related to the new headquarters building. As the new market was being implemented in 2009, the Company determined that certain software and hardware components were not performing as expected and made the decision to abandon the assets and replace them. Additionally, the costs associated with earlier design studies for the new headquarters building were abandoned as these designs were not aligned with the Company's current environmental strategy.

5. Employee Note Receivable

The Company has provided $500,000 in financing to an officer of the Company in connection with the purchase of his primary residence. The loan is collateralized by a subordinated deed of trust on the property, accrues interest at 6.5 percent per annum, compounded annually, and requires annual payments of $68,000. Portions of the note may be forgiven by the Company based on the officer's continuing employment as set forth in the employment agreement. The balance due at December 31, 2009 and 2008 of approximately $434,000 and $474,000, respectively, including accrued interest, is included in other assets in the accompanying balance sheets.

6. Generator Noncompliance Fines

In 2000 and 2001, the Company billed generator noncompliance fines to market participants totaling $122.1 million. Through December 31, 2009, collection of these fines totaled $60.7 million. Generally, these fines were assessed at twice the highest price paid in the Company's markets for energy and were applied against the amount of energy the participating generator failed to supply as directed by the Company during specific emergency conditions as defined in the tariff. These fines will be retroactively adjusted as a result of the FERC Refund Case, as described in Note 12, in which the prices used to calculate the fines are subject to adjustment, with any surplus collections being refunded with interest to market participants.

Based on estimates of the mitigated energy prices in the FERC Refund Case, the Company recorded fine revenues totaling $29.5 million, which results in a refund liability of $31.2 million. The ultimate settlement of fines is expected after the conclusion of the proceedings in the FERC Refund Case and the ultimate financial settlement of the California Power Exchange (Cal PX). While there are significant uncertainties associated with this process, management believes it is unlikely that there will be any future reduction in generator fines that will ultimately reduce the amount of fine revenues realized by the Company.

In accordance with FERC rulings, the Company accrues interest on the portion of fines collected in excess of the estimated realizable amount, which are to be refunded to market participants when the amounts are settled. Such interest expense amounted to $2.1 million and $4.7 million in 2009 and 2008, respectively. At December 31, 2009 and 2008, accrued interest payable related to these fines totaled $14.8 million and $25.5 million, respectively.

Through December 31, 2008, the Company excluded the calculation of interest on the preparatory rerun corrections, based on the position that interest would only accrue upon the preparatory rerun being invoiced. The Company, however, believed that preparatory rerun corrections should be eligible for interest from the due date of the original trade month being corrected in the same manner as interest on corrections for mitigated market-clearing prices in the refund rerun and requested a FERC ruling on this issue. On May 27, 2009, FERC ruled that preparatory rerun corrections in the FERC Refund Case are eligible for interest in the same manner as interest on corrections for mitigated market-clearing prices in the refund rerun. Such interest amounted to $12.7 million at the date of FERC's ruling, of which $12.2 million relates to amounts that accumulated through December 31, 2008. Accordingly, in May 2009, the Company recognized $12.8 million as a reduction of interest expense with a corresponding adjustment to the estimated generator noncompliance fines refund liability.

At December 31, 2009 and 2008, the estimated net realizable amount of fines is $29.5 million. Included in current liabilities at December 31, 2009 and 2008, is an estimated refund liability to market participants of $31.2 million representing the difference between the $60.7 million in collections and the estimated fines to be retained, plus accrued interest.

7. Long-term Debt and Related Agreements

Long-term debt consists of the following at December 31, (in thousands):

	2009	2008
CIEDB Revenue Bonds, Series 2009		
Fixed interest rates of 3.00% - 6.25% with maturities from 2012 through 2039	$ 200,000	$ -
CIEDB Revenue Bonds, Series 2008		
Fixed interest rates of 4.00% - 5.00% with maturities through 2014	165,970	196,970
Unamortized net premium:		
Series 2009 bonds	1,955	-
Series 2008 bonds	4,854	7,402
Total long-term debt	372,779	204,372
Less: current portion	(39,100)	(31,000)
Total long-term debt, less current portion	$ 333,679	$ 173,372

Summarized activity of long-term debt for the year ended December 31, 2009, is as follows (in thousands):

	Beginning of Year	Issuance/ (Payments)	End of Year
CIEDB Revenue Bonds, Series 2008	$ 196,970	$ (31,000)	$ 165,970
CIEDB Revenue Bonds, Series 2009	-	200,000	200,000
Total long-term debt	$ 196,970	$ 169,000	$ 365,970

Summarized activity of long-term debt for the year ended December 31, 2008, is as follows (in thousands):

	Beginning of Year	Issuance/ (Payments)	End of Year
CIEDB Revenue Bonds, Series 2008	$ -	$ 196,970	$ 196,970
CIEDB VRDBs			
Series 2007	60,000	(60,000)	-
Series 2004	84,400	(84,400)	-
Series 2000	45,300	(45,300)	-
Total long-term debt	$ 189,700	$ 7,270	$ 196,970

Scheduled future debt service payments for the 2008 and 2009 Series A Bonds as of December 31, 2009, are as follows (in thousands):

	Principal	Interest	Total
2010	$ 39,100	$ 17,735	$ 56,835
2011	42,250	15,651	57,901
2012	28,585	14,300	42,885
2013	39,580	12,375	51,955
2014	27,145	10,957	38,102
2015 - 2039	189,310	169,971	359,281
	$ 365,970	$ 240,989	$ 606,959

Long-term debt and related agreements
In July 2009, the Company issued $200.0 million of fixed rate revenue bonds (the 2009 Bonds) through the CIEDB, at a premium of $2.0 million. The proceeds of the issuance were used to provide funds for the design and construction of a new headquarters building, the acquisition or development of computer hardware and software systems, and the acquisition of office equipment.

In June 2008, the Company issued $197.0 million of fixed rate revenue bonds (the 2008 Bonds) through the CIEDB, at a premium of $9.2 million. The proceeds of the issuance were used to refund all variable rate demand bonds outstanding at the time of issuance, fund debt service reserves related to the issued debt, and pay certain debt issuance costs. The remaining proceeds will be used to fund computer hardware and software systems, other facilities and equipment, and other planned capital projects.

The 2009 and 2008 Bonds are supported by a pledge of the Company’s revenues and operating reserves. In addition, the 2009 Bonds are supported by a deed of trust on the new headquarters building and land. The premiums on the bonds are being amortized over the life of the bonds.

All of the Company's variable rate debenture bonds were refunded during 2008 with a portion of the proceeds from the 2008 Bonds. In connection with this refunding, the related standby bond purchase agreement and bond insurance were terminated. The Company recognized a loss on refunding related to these bonds of $1.0 million. The loss is being amortized over the remaining life of the original bonds, which were scheduled to mature at various dates through 2013.

Interest expense
Interest expense recorded by the Company related to long-term debt includes interest paid on the bonds, bond remarketing costs, bond insurance and liquidity costs and amortization of the bond issuance costs, the bond premium and loss on refunding.

8. Fair Value of Financial Instruments

The following valuation methods and assumptions were used as a basis for the fair value of each class of financial instrument :

Investments
The fair values of investments, including cash equivalents, except as noted below, are based upon quoted market prices. Fair values for the GIC and forward delivery agreement are based on counterparty quotes and discounted cash flows.

Long-term debt
The fair value of fixed rate long-term debt, which includes the short-term portion, is based on current market rates.

The fair values of the Company's financial instruments as of December 31, 2009, are presented below (in thousands):

	Recorded Value	Fair Value
Investments, including cash and cash equivalents	$ 650,638	$ 650,856
Long-term debt	(372,779)	(382,356)

The fair values of the Company's financial instruments as of December 31, 2008, are presented below (in thousands):

	Recorded Value	Fair Value
Investments, including cash and cash equivalents	$ 385,523	$ 386,424
Long-term debt	(204,372)	(207,554)

The carrying values reported on the balance sheet for current assets and liabilities, excluding the short term portion of long-term debt, approximate fair value.

9. Employee Benefit Plans

The Company maintains a number of employee benefit plans. The description of the plans and their key provisions is included below. Obligations included in the Company's balance sheets related to these plans consist of the following at December 31 (in thousands):

	2009	2008
Executive pension restoration plan	$ 866	$ 666
Post-employment medical benefit plan	12,650	10,970
Supplemental executive retirement plan	320	509
Executive savings plan	367	350
Total employee retirement plan obligations	$ 14,203	$ 12,495

Retirement savings benefits plan
The Company sponsors a defined contribution retirement plan, the California ISO Retirement Savings Benefits Plan (the Retirement Plan) that is subject to the provisions of the Employee Retirement Income Security Act of 1974 and substantially covers all employees. The Retirement Plan is administered by the Company with the assistance of a third party. The assets of the plan are held separately from Company assets and are not combined with the assets on the balance sheet.

Employees may elect to contribute up to fifty percent of their eligible compensation to the Retirement Plan, subject to statutory limitations. The Company matches contributions up to six percent of an employees' eligible compensation and an additional contribution equal to five percent of eligible compensation for employees with less than five years of service, or seven percent for employees who have at least five years but not more than ten years of service. An additional contribution of one percent of eligible compensation is also made by the Company for each five year increment of service after an employees' ten year anniversary.

Employees' contributions to the Retirement Plan for 2009 and 2008 were $6.7 million and $6.3 million, respectively. The Company's contributions to the Retirement Plan for 2009 and 2008 were $7.8 million and $7.1 million, respectively.

Executive pension restoration plan
The Company sponsors the Executive Pension Restoration Plan, a non-qualified defined contribution plan, which allows certain officers of the Company to make contributions and receive Company contributions in excess of the 401(k) contribution limits set forth by IRS regulations as described in the retirement savings benefits plan above.

The contributions and earnings thereon are held in a trust and the balances as of December 31, 2009 and 2008, were $866,000 and $666,000, respectively and are included in Other Assets with a corresponding liability in Employee Retirement Plan Obligations. The Company recognized expenses for contributions of $229,000 and $259,000 in 2009 and 2008, respectively.

Post-employment medical benefit plan

Plan description
The Company sponsors the California ISO Retiree Medical Plan, a defined benefit plan, to provide post-employment health care benefits to all employees who retire from the Company on or after attaining age 60 with at least five years of service and to their spouses, domestic partners and eligible dependents, as provided for under the terms of the plan. Depending on the retirement age and coverage elections made by the beneficiaries, the Company pays a portion (ranging from 60 to 100 percent) of the premiums. There are 26 employees and 14 retirees eligible to receive benefits pursuant to the plan as of December 31, 2009.

Funding and investment policy
The Company has established a trust for the purposes of funding the plan. The trust was established as a tax-exempt voluntary employees' beneficiary association. All assets of the trust are to be used for the exclusive benefit of the participants and beneficiaries of the plan. Although the Company has fiscal accountability for these assets and holds them in a fiduciary capacity, the assets are not considered assets of the Company and are therefore not included on the balance sheets of the Company. As of December 31, 2009 and 2008, the trust assets were $4.2 million and $1.8 million, respectively. Trust assets were primarily invested in corporate bonds. The investment of the trust assets generally follows the Company's investment policy.

The Company's current funding policy is to annually contribute an amount such that the total amount in the trust approximates the actuarially determined liability attributable to retirees and their spouses and to active participants who are fully eligible to retire.

Annual Other Post-employment Benefits (OPEB) Cost and Net OPEB Obligation
The Company's annual OPEB cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45 "*Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions".* The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 15 years (using the level dollar open method). The ARC is adjusted for the amortized amount of the discounted present value (ordinary annuity) of the balance of the net OPEB at the beginning of the year.

The Company's annual OPEB cost at December 31 is as follows (in thousands):

	2009	**2008**
Annual required contribution	$ 4,274	$ 3,099
Interest on net OPEB obligation	521	536
Adjustment to annual required contribution	(1,039)	(1,000)
Annual OPEB cost	3,756	2,635
Contributions made	(2,076)	(1,871)
Increase in net OPEB obligation	1,680	764
Net OPEB obligation, beginning of year	10,970	10,206
Net OPEB obligation, end of year	$ 12,650	$ 10,970

The Company's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and net OPEB obligation for the year ended December 31 (in thousands):

Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2007	$ 2,128	2%	$ 10,206
2008	2,635	71%	10,970
2009	3,756	55%	12,650

Actuarial methods and assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

The following significant actuarial methods and assumptions were used in the calculation of annual OPEB cost for the year ending December 31, 2009.

Valuation date	January 1, 2009
Actuarial cost method	Projected unit credit
Amortization method	Level dollar, open
Remaining amortization period	15 years
Asset valuation method	Market
Investment rate of return	4.75%
Healthcare cost trend rate	9% initial, 5% ultimate

Funding status and funding progress

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule below reflects multiyear trend information to show the status of funding based on the actuarial value of plan assets relative to the actuarial accrued liabilities. This information is required supplemental information.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Projected Unit Credit (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)
January 1, 2008	$ -	$ 12,225	$ 12,225	0%
January 1, 2009	1,813	17,171	15,358	11%
January 1, 2010	4,137	18,009	13,872	23%

The actuarial valuation as of January 1, 2010, was based on actuarial methods and assumptions that were generally consistent with those used in the calculation of the annual pension cost for the year ending December 31, 2009, except for the discount rate (which changed from 4.75 percent to 5.00 percent), health care cost trend rate (which changed from 9% to 8.43%) and HMO pre-65 morbidity adjustment (which changed from 60% to 52%, as a result of lower than expected number of retirees). The changes in these assumptions decreased the AAL by approximately $1.1 million.

The actuarial valuation as of January 1, 2009, was based on actuarial methods and assumptions that were generally consistent with those used in the calculation of the annual pension cost for the year ending December 31, 2008, except for the discount rate (which changed from 5.25 percent to 4.75 percent) and the health care cost year of ultimate trend (which changed from 2012 to 2016). The changes in these assumptions increased the AAL by approximately $3.1 million.

Supplemental executive retirement plan
The Company sponsors the California ISO Supplemental Executive Retirement Plan (SERP Plan), a non-qualified defined benefit plan intended to provide selected executives of the Company with target retirement benefits based upon an executive's average earnings and total number of years of service with the Company, as defined in the plan. The target benefit is to be offset by other retirement benefits, including those provided by the Company, and by any distributions from this plan made to pay the beneficiary's share of federal, state and local taxes. The plan is unfunded.

The activity and related obligations associated with the plan during 2009 and 2008 is as follows (in thousands):

	2009	**2008**
Obligation, beginning of year	$ 509	$ 369
Current period actuarially determined cost	205	140
Benefits distributed during the year	(394)	-
Obligation, end of year	$ 320	$ 509

The Company recognized expenses of $205,000 and $140,000 in 2009 and 2008, respectively in connection with this plan.

Executive savings plan
The Company sponsors the Executive Savings Plan, a non-qualified defined contribution plan under section 457(b) of the IRS Code. The Company contributes a percentage of each officer's annual base compensation to the plan. Officers may elect to make voluntary contributions, subject to statutory limitations. The contributions and earnings thereon are held in a trust and the balance as of December 31, 2009 and 2008 was $367,000 and $350,000, respectively and is included in Other Assets, with a corresponding liability in Employee Retirement Plan Obligations. The Company recognized expenses of $92,000 in both 2009 and 2008, in connection with this plan.

10. Insurance Programs and Claims

The Company is exposed to various risks of loss related to torts; theft, damage to, and destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. The Company maintains various commercial and mutual insurance plans that provide coverage for most claims in excess of specific dollar thresholds, which range from $500 to $1.0 million per claim. Primary insurance policies have coverage limits set based on the Company's assessment of reasonable exposure within that risk category, with consideration of insurance types and coverage limits for comparable entities. Additionally, the Company maintains excess liability coverage that provides umbrella coverage for certain exposures to a limit of $135.0 million. Miscellaneous losses below insurance deductibles are expensed as incurred. In 2009 and 2008, the Company did not incur any claims in excess of the coverage described above.

The Company is a participant in a group captive insurance company for workers compensation insurance coverage. The Company's annual net insurance costs for such coverage vary based on claims incurred at the Company, and to a lesser extent, claims activity of other members of the captive insurance company. The Company's annual insurance expense is limited through reinsurance and risk sharing arrangements of the captive to an additional percentage of the initial base premium paid.

11. Lease and Contract Commitments

The Company has long-term operating leases and service contracts that expire at various times through 2017 including telecommunication equipment and services, information system equipment and services and systems infrastructure and office facilities.

The following are the future minimum payments under these agreements as of December 31, 2009 (in thousands):

2010	$	12,560
2011		12,300
2012		11,174
2013		3,124
2014		596
	$	39,754

Lease and service contract costs of approximately $12.2 million and $12.8 million were charged to operating expense in 2009 and 2008, respectively.

12. Contingencies and Settlements

The FERC Refund Case

In 2000 and 2001, the California energy markets, including those managed by the Company, experienced high prices, shortages of energy and reserves, rolling blackouts and liquidity problems for many market participants. Several of them, including the California Power Exchange (Cal PX), filed for bankruptcy.

Purchasers of energy during this period sought refunds at FERC. FERC has issued a series of orders related to mitigating the market clearing prices in markets administered by the Company and Cal PX for the period from October 2, 2000 through June 20, 2001 (the FERC Refund Case). Several of the Company's market participants have settled their liability arising from the FERC Refund Case and related proceedings. Management believes the ultimate outcome of the FERC Refund case (except as it relates to generator noncompliance fines, as described in Note 6) will have no financial impact on the Company as these refund amounts are funded and will ultimately be resettled among market participants.

Market billing disputes in good faith negotiations

As part of the tariff and applicable contracts, the Company has dispute resolution processes for market participants, transmission owners and RMR owners to register disagreements regarding information reflected in the settlement statements or billing amounts for market and RMR activity. After good faith efforts, known as good faith negotiations (GFN), have been made to negotiate and resolve disputes, written claims may be submitted either to mediation or arbitration.

One material unresolved market related dispute remains outstanding in GFN at December 31, 2009. This dispute is described below and is specifically related to disagreements with the Company's financial settlement of market transactions and related tariff interpretations.

The Company has an obligation to procure ancillary services necessary to maintain the reliability of the California grid consistent with applicable reliability criteria and to fulfill its responsibilities as a balancing authority. Following GFN, Pacific Gas and Electric Company (PG&E) filed a claim against the Company concerning charges for ancillary services procured by the Company in connection with transactions scheduled on the California Oregon Transmission Project during the period from April 1998 to April 1999. In December 2001, an arbitrator issued a ruling in favor of PG&E for $14.3 million, plus interest and, after motions for rehearing and clarifications, FERC affirmed this decision. This award will be allocated to market participants and invoiced in conjunction with the FERC Refund Case as defined above. In addition, as part of a compliance filing in the Refund Case, the Company plans to ask FERC to preclude any future disputes related to this matter.

Other disputes, some of which are material in amount, have been filed with the Company. Management believes that any settlements or market adjustments relating to these disputes and the matters in GFN would be resettled against the market with no liability to the Company.

Indemnifications

The Company's bylaws require its annual financial statements to include disclosures about certain payments made by the Company related to indemnifications to or on behalf of officers and Board members. There were no such payments in 2009 and 2008.

Other matters

The Company, during the ordinary course of its operations, has been involved in various lawsuits and claims, several of which are still pending. Management and legal counsel are of the opinion that there are no other material loss contingencies that would have a material adverse impact on the financial position of the Company, except as disclosed within the notes to these financial statements.