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Results of the 2011 Financial Statement Audits

*Board of Governors
Meeting*

Folsom, CA

May 16-17, 2012



Agenda

Results of audit

Description of financial statements

Key audit areas

Independence

Required communications

Closing



Results of audit

- Audits are complete
 - Audit reports issued
 - Two sets of financial statements
 - General purpose – GAAP
 - Statutory – FERC
 - ISO Management prepared the financial statements
 - PwC audited the financial statements
- The ISO's audit opinions are unqualified
- Audits were completed on an accelerated time frame – FERC report issued in April
- Form and content of the financial statements are similar to prior years

Corporate financial statements

- General purpose use
 - Annual report
 - Financial users
- Basis of accounting – State and Local Government (GASB)
 - Required based on state government board appointment process
 - Differs from private accounting principles – some investments; benefit plans
- Audit comments
 - These are primary; prepared first
 - Audit is focused on these – over 90% of audit effort



California Independent System Operator Corporation

Financial Statements

For the years ended December 31, 2011 and 2010

FERC Form #1 Financial Statements

- Statutory
 - Filed with FERC
 - Available to public through FERC
- Basis of Accounting – FERC Chart of accounts
 - Basic accounting follows normal private accounting principles (FASB)
 - Statutory forms
- Audit comments
 - These are less reader friendly
 - Focus on statutory reporting requirements/ leverage primary audit
 - Net difference - \$1.3 million impact to income/loss in 2011



**FERC FINANCIAL REPORT
FERC FORM No. 1: Annual Report of
Major Electric Utilities, Licensees
and Others and Supplemental
Form 3-Q: Quarterly Financial Report**

FERC vs. GASB reporting

- Differences in net income/ loss from corporate (general purpose) financial statements
 - Investments - all at fair value under FERC, most under fair value for corporate (MTM gain of \$1.2 million for FERC)
 - Post employment medical plan - different actuarial valuation under FERC (\$0.1 million lower expense for FERC)
 - Net loss - \$1.3 million lower loss for FERC than corporate
- Significant differences between corporate and FERC financial statement footnotes
 - Generally reduced disclosures, no requirement for MD&A
 - Additional fair value disclosures
 - Additional schedules required by FERC (unaudited)

Key audit areas

Contingencies:

- Exposure to ISO comes from three sources
 - Market based adjustments; disputed charges
 - GMC could be contingent
 - Non market issues - corporate exposure as employer
- Key Assertion
 - Management believes any settlements would likely be resettled against the ISO's markets (not from the ISO)
 - Therefore, no recorded liabilities regarding these market matters
- Disclosures include
 - Refund case stemming from energy crisis
 - Market disputes

Key audit areas

Old headquarters facilities:

- Accounting for estimated future exit costs - \$6.4 million
- Loss recorded in 2011 (the substantial cease-use date)

New headquarters building:

- Total capitalized for the new building through 2011 – \$130.4 million
- 2011 was the first full year of depreciation on the building
- Building components being depreciated over 20-30 years

Other:

- Determination of fair value for hard to value investments (\$1.2 million gain recorded for FERC only)
- Risk of management override of controls – presumed risk (not ISO specific)

Independence

- Key element of audit relationship
- Numerous core processes in place to monitor compliance with PwC independence rules
 - Annual compliance
 - Annual training
 - Firm monitoring
- Individual audit independence and objectivity is manifested in numerous ways
 - Partner rotation requirements;
 - Rotation for ISO is more strict (5 years) than required
 - Mark Niehaus began partner role this year in accordance with rotation plan
 - Quality review partner role
 - Risk management oversight procedures
 - Each individual verified independence on each engagement

Required communications

There were no:

- Disagreements with Management
- Significant issues discussed prior to retention
- Significant difficulties encountered during the audit
- Material fraud or illegal acts
- Related party transactions, except as disclosed in the notes to the financial statements

Audit adjustments:

- There were no posted audit adjustments
- There were no uncorrected errors

Required communications

Internal controls:

- Scope of audit does not include an opinion on internal controls
- This differs from SSAE 16 audit that we perform over market systems
- During audit we are required to report to the Board of Governors any
 - Material weaknesses
 - Significant deficiencies
- No material weaknesses or significant deficiencies are reported
- Level of audit adjustments is an indicator of potential control issues; there were none
- We have shared controls related observations and recommendations with management in context of continuous improvement

Closing

- **We are independent of the ISO and have no relationships with the ISO that would impair our independence**
- **High level of commitment and cooperation of accounting and other staff greatly appreciated**
- **PwC encourages communication and feedback from the Board of Governors**
- **Questions**

