

Memorandum

To: Audit Committee of the ISO Board of Governors
From: Eric Schmitt, Vice President, Operations
Date: December 6, 2012
Re: **Acceptance of 2012 Operations Audit**

This memorandum requires Committee action.

EXECUTIVE SUMMARY

PricewaterhouseCoopers, LLC completed the California Independent System Operator Corporation Compliance Assessment relating to Specified Control Room Operational Processes and issued its report dated November 30, 2012. The compliance assessment evaluated the day ahead operational process and was completed with one exception noted. Management recommends that the Audit Committee accept the compliance assessment as submitted and proposes the following motion:

Moved, that the Audit Committee of the ISO Board of Governors accepts the compliance assessment issued on November 30, 2012 by PricewaterhouseCoopers LLC for the testing of specified control room operational processes for 2012, as attached to the memorandum dated December 6, 2012.

BACKGROUND

In accordance with tariff section 22.1.2.2, Management engaged PricewaterhouseCoopers to perform the annual independent review of the ISO's compliance with its operations policies and procedures. In the past, Management has requested that the independent entity provide an assessment, consistent with the tariff requirements. However, as discussed at the May 2012 Board meeting, for this year's assessment Management requested that the independent auditor conduct an audit in accordance with generally accepted auditing standards and issue an opinion that the ISO's operational processes are in compliance with select operations procedures representing generally accepted good utility practice. For 2012, Management has selected the day ahead operational process for the scope of the audit because of its importance to market participants and its impact on both operations and the market.

Although the day ahead market is a necessary feature of ISO market operation, its' set up and execution must be properly managed, consistent with the needs of the grid.

Management created and refined several operating procedures to ensure the greatest degree of accuracy possible with the resulting market solution. These procedures and activities are executed and reviewed on a daily basis by internal staff. However, selecting the day ahead market process as the examination scope affords an independent assessment of whether the processes are being followed, providing valuable feedback and identifying areas for additional improvement.

This year the audit period broken is into two periods, both managed from the Folsom facility. The auditors made their initial observations on August 6–15, 2012, and their second assessment on September 19–28, 2012.

PricewaterhouseCoopers performed the audit based on an attestation examination that results in an audit opinion. The examination included:

- The actual operations activities associated with the day ahead market operational functions; and
- The validation of the information provided from day ahead operator logs.

RESULTS

The audit focused on of the ISO's operating procedures selected on the basis that they were integral to their day ahead market function and could be objectively compared against actual operating practice. The audit scope covered the day ahead market procedural elements, criteria by which these procedural elements were assessed, and the ISO's self-assessment of compliance, whereby exception conditions, if present, were reported. Such exception conditions were identified when actual practice was not consistent with the procedural element's criteria. Several aspects of the day ahead market function were included in this audit's scope.

During the twenty day audit period at the Folsom control center there were a total of 480 hours reviewed from 13 operational testing perspectives. From these 13 criteria, across nearly 500 hours of observation, one issue was identified. This issue included generation resources identified by the ISO to be blocked from offering ancillary services to the day ahead market during the assessment period. During this time the ISO was not compliant with one of the criteria for procedural guidelines set forth in Attachment I for one generating unit over a six hour period. The ISO was in compliance with the remaining criteria set forth in the audit report for all other times within the assessment period. There is no financial or reliability impact of this blocking error, as the unit was not selected for dispatch because of an outage submission.

Management has reviewed the process to determine areas for improvement and has re-enforced the critical nature of the manual set up associated with the blocking process. An automated solution has been queued up for future design and an interim process has been created that includes a secondary review to ensure proper set up of

the blocking function. Follow up training was also performed based on this observation, ensuring all day ahead operators are familiar with the process enhancements.

CONCLUSION

Management recommends that the Audit Committee of the ISO Board of Governors accept the audit report issued by PriceWaterhouseCoopers on November 30, 2012.