

Memorandum

To: ISO Board of Governors
From: Nancy Saracino, Chief Compliance Officer
Date: May 13, 2008
Re: **Compliance Committee Update**

This memorandum does not require Board action.

The CAISO Five-Year Strategic Plan (2008-2012) identifies compliance as a significant element, particularly with respect to the recently adopted NERC and WECC Mandatory Standards. Consistent with this focus, the Compliance Committee intends to provide regular reports to the ADR/Audit with respect to compliance implementation and training, and this is the Compliance Committee's first report in 2008.

Mandatory Reliability Standards Compliance

Effective as of November 19, 2007, a new department of Mandatory Standards Compliance, under the direction of the Chief Compliance Officer, is leading all CAISO activities related to compliance, documentation, verification, monitoring and reporting of compliance with the mandatory standards. The following is an update of FERC, NERC and WECC activities and an outline of the department's implementation efforts.

The Mandatory Standards Compliance department has undertaken many critical tasks toward ensuring compliance with the mandatory reliability standards and developing business processes and procedures to monitor and report on mandatory standards compliance. Primarily, the Mandatory Standards Compliance department has been focused on identification of business unit ownership for each of the 831 mandatory reliability standards requirements that are applicable to the ISO and the process of identifying business unit documentation for these requirements. As a part of this effort, Internal Audit has been reviewing compliance documentation and producing observations to improve the documentation. Mandatory Standards Compliance is using these reviews and working with the business units to improve our documentation overall to ensure any future compliance audits by WECC or NERC will be successful.

Consistent with this effort, the ISO has contracted with industry experts to assist in compliance documentation review, gap analysis and improvement. Grid Operations documentation is currently undergoing review, which likely will yield many opportunities for improvement with respect to the expectations in this area. An additional consultant is in the beginning stages of work with Planning and Infrastructure Development and each department with responsibility for compliance with the Critical Infrastructure Protection standards.

Awareness training is a critical part of a good internal compliance program. As an initial step, Mandatory Standards Compliance is using an hour each week of the Summer Workshops to inform operators and engineers of our

compliance responsibilities and the resources that are available to them. As part of this presentation, the Chief Compliance Officer is underscoring the importance of compliance with the mandatory reliability standards and emphasizing the ISO's commitment to compliance.

Keeping abreast of the many changes taking place in the NERC and WECC standards and providing the ISO's input into their development ensures that compliance with the Reliability Standards will remain possible and that future Reliability Standards are written in such a way that compliance in a market environment remains possible. The Mandatory Standards Compliance Group coordinates the ISO's participation in appropriate Standards Drafting Teams and coordinates input from the ISO to the drafting teams as they modify the standards.

Training

The Compliance Committee is planning company-wide awareness campaigns to ensure that all employees, regardless of their direct involvement with the mandatory standards, are informed of them and the significant role they play in the ISO's strategic business plan. Due to the wide applicability of the Critical Infrastructure Protection (CIP) standards and their early effective date, the CIP standards were the first set of standards selected for inclusion in such a campaign. The CIP awareness campaign is currently under development and is expected to be rolled out sometime early this summer.

This year, the ISO intends to provide approximately four hours of mandatory training for all employees. Normally this training is held in the late summer and early fall; however, this year the Compliance Committee supports the decision to hold this training during the summer so as to minimize potential conflicts with MRTU implementation. The mandatory training for all employees is expected to focus on the following subjects: (i) the Employees Code of Conduct and Ethical Principles; (ii) Substance Abuse Awareness and Prevention, (iii) Controls, Reporting Requirements, and Audits; (iv) Mandatory Standards Compliance; and (v) Tariff Compliance.

Coordination and Next Steps

The Compliance Committee continues to coordinate with all compliance-related functions within the organization to fill gaps, avoid duplication, and maximize the value of our efforts to continuously improve compliance monitoring and reporting with the resources we have available. As a result, the Compliance Committee has added two additional members, the Chief Financial Officer and the Director of Organizational Effectiveness. In addition, we are in the process of identifying all compliance related Board reporting activities within the organization, whether reported to the Board independently or through the Compliance Committee,¹ in an effort assure that all key areas are properly reported.

¹ For example, Internal Audit, Finance, and Operations each provide one or more separate reports to the ADR/Audit Committee and/or the Board, some of which are prepared by third parties.