

Minutes of the Market Participant Audit Advisory Subcommittee Meeting (MPAAS)**March 24, 2005****NYISO Washington Ave, Albany, NY**

Attendees' Names**Representing****MPAAS Members**

Arthur Brennan	NYPA
Robert Farrell (Chair)	LIPA
John Ventura	Con Ed
Walter Werther (Vice-Chair)	KeySpan
Daniel Zeppetello	NIMO

MPAAS Guests

Curt Ashman	Energy East
Dave Clarke	Navigant
Rich deJong	Energy East
Paul Gioia	LeBoeuf Lamb Greene & MacRae LLP

NYISO Staff

Vincent Budd
Leigh Bullock
Brad Kranz
Marc Rubin
Belinda Thornton

Mr. Bob Farrell, of LIPA, called the meeting to order.

I. Approval of Minutes from August, 2004

The minutes from the August 2004 MPAAS meeting were approved and will be posted on the NYISO website.

II. Approval of Minutes from October 28, 2004 Meeting

The minutes from the October 28, 2004 MPAAS meeting were approved with revisions already made, and will be posted on the NYISO website.

III. TCC Briefing by Belinda Thornton, NYISO

Ms. Thornton reported on the TCC issue background and measures that were taken since the event to prevent a reoccurrence.

Mr. Gioia asked to make a few statements on behalf of the Transmission Owners (TOs), who were very concerned about the TCC auction issues. He stated that the TOs believed that there had been consistent problems with respect to the accuracy of the markets, and it was imperative that action be taken promptly to ensure that the NYISO has controls in place to improve the accuracy of the markets, as well as the confidence of Market Participants (MPs). He added that the NYISO Board shared this concern, and recommended that this be a joint effort between MPs and the NYISO. Mr. Gioia's specific points for consideration included:

- There were outstanding issues with respect to the planned Ernst & Young audit on TCC issues raised last year. The NYISO needs to resolve the outstanding issues and get this audit started.
- A similar audit for the 2000-2002 period should be planned and executed subsequent to the audit discussed above.
- It is important that MPs have a full understanding of the control measures being developed and have an opportunity to make decisions on whether these are sufficient. The MPs need to have a better understanding of the work done by Bearing Point.
- The MPAAS should decide whether similar controls should be adopted for other markets such as the Day-Ahead Energy Market and the Installed Capacity (ICAP) Market.
- The SAS 70 audit process needs a thorough review. Why hadn't this provided an adequate level of quality control? SAS 70 audit results have not provided MPs with a sufficient level of confidence. What is KPMG doing and what shouldn't they be doing?
- There needed to be consideration as to what extent third-party audits are appropriate in other areas of the NYISO. The NYISO Board did not have a problem as long as the audit is productive and makes sense.

In conclusion, Mr. Gioia stated [in his opinion] that the Board supports the concept of shared governance and is mindful of the NYISO's fiduciary responsibilities for MP property and funds. Mr. Gioia believes that the NYISO and its MPs will be able to jointly resolve these issues.

The group noted his statements.

Ms. Thornton continued with her report, first briefly providing MPAAS members with her background at the NYISO and then explaining how she became involved with the TCC issue. She also provided background information on the TCC issue and detailed the

numerous actions that were taken in the summer of 2004 to ensure the accuracy of future auctions. The actions taken included:

- Internal/third-party database validations
- Self-verification initiative
- Third-party review
- Development and implementation of a database validation tool

The group raised questions on the controls that were originally in place for the TCC auctions. Ms. Thornton explained that problems stemmed from the spreadsheets that were used to maintain the TCC auction data and that although controls were in place, there was a comparison control failure with the Grandfathered rights flag between the Billing and TCC spreadsheets. Mr. Ventura stated that because the transfer to the new database did not note that the flag did not transfer, he did not think that the proper controls were in place for the database conversion.

Mr. Ashman asked if the SAS 70 audit included checking instances where spreadsheets were being used, and if not, why not? He stated that controls need to be put in place for locking down spreadsheets and that spreadsheet control has to be included in the SAS 70 audit, as this is critical to the billing application. Ms. Thornton and Mr. Rubin noted his concern.

Internal/Third Party-Database Validations:

Ms. Thornton stated that the databases were validated prior to the August Reconfiguration Auction and that a database validation tool is run prior to every auction. In addition, Attachment L to the OATT was reviewed and audited and source documents were also reviewed to ensure accuracy. Auction templates were created and put into a separate place to ensure that the correct template would be chosen.

Self-verification:

Ongoing self-verification was begun during July. Attachment L is being updated and, at the request of TOs, has been put off until the May 2005 Management Committee Meeting. The NYISO is hoping to have this ready for the fall 2005 capability period. Ms. Thornton stated that data from all the TOs has not been received. Those who have not responded back will be notified. She emphasized the need for timely reporting.

Third Party Review:

Ms. Thornton noted that Bearing Point had been reviewing the TCC process, and had made recommendations for improvement, which were being implemented.

Database Validation Tool:

Ms. Thornton reported that a database validation tool was developed prior to the August Auction. All database auction errors found were corrected. The database tool was run prior to the Auction and a clean report was produced, indicating that the two databases were in synch. This database comparison tool looks at all data in BAS, compares it to

the TCC data, and drops out exceptions. Exceptions are then reviewed. Mr. Brennan asked if the validation tool was developed in-house. Ms. Thornton responded that the tool had been developed by Bearing Point.

Ms. Thornton further detailed measures that were taken to prevent TCC error reoccurrences, based on recommendations from Bearing Point, who had reviewed the entire TCC process and controls. These included:

- Management validation: the TCC auction is now run by four staff members and divided into different pieces. A review is performed by a manager after the auction to ensure that all procedures were followed. In addition, there has been significant organizational restructuring including: reassignment of the TCC functions to the Assistant Vice-President, realignment of TCC auction and marketing functions between Auxiliary Market Operations (formerly Resource Reliability) and Product Management, assignment of a new Manager for Auxiliary Operations, the addition of a TCC Product Manager, and establishment of a TCC quality assurance person.
- Pre-/post- discussion: included is who has responsibility for each area and documentation for any auction anomaly that may have occurred. A complete package will now be put together for each auction that included all pre- and post-discussion.
- Revenue allocation issues templates were developed. Two people pull data through the templates and provide results to the manager for review. In the templates are the formulas for how the data is carried through. A second check is performed by a separate area to make sure that the same results are produced.
- Development of the grandfathered rights database: this database, originally in hardcopy format, is now being moved to an electronic database and is 75% complete.
- Ongoing: baseline TCC Auction Dataflow was presented and sub-processes were defined. Validation points were reviewed, noted, and prioritized based on risks. High priority items have already been reviewed and should be in place by June 2005.

Mr. Brennan asked if these controls have been documented. Ms. Thornton replied that all changes have been documented, and that this is an ongoing process.

The group discussed the spreadsheet review and whether there was enough documentation for people reviewing the spreadsheets to discover errors. Mr. Clarke stated that, in his opinion, the documentation was insufficient.

Ms. Thornton discussed the TCC automation project. This project will fully automate the TCC auction and data validation. High-level functional requirements had been defined and the NYISO was reviewing three proposals to determine whether it was more

appropriate to “buy” or “build”. Mr. Ventura asked if some of the TCC controls that were put in place had been applied to the ICAP market. Ms. Thornton said that some had been applied.

Mr. Ashman asked if the Market Monitoring & Performance Unit (MMP) would have any oversight once this process change is over. Mr. Budd said that discussions with Dr. David Patton had been ongoing since the TCC issue surfaced and in an effort to get an outside perspective into the process. This is one of the MMP goals.

Mr. deJong asked if there were any errors found in the ICAP Market. Ms. Thornton answered that none had been discovered and stated that MMP will be looking at the ICAP market as well.

Regarding the KPMG Enron Audit, Mr. Ventura questioned why the TCC errors were not found on the billing issues list. This control was implemented after the discovery of the ENRON issue to assure that significant billing issues could be reviewed more openly. He stated that the Billing Issues List (the BIG List) was supposed to be maintained, modified, and reviewed with BIC, BAWG, and the NYISO Board. The fact that the TCC issues were not on the BIG List is indicative of infrastructure problems from a controls perspective, he mentioned. It was noted that the BIG list was not brought to the BAWG on a regular basis. Thus, the controls agreed to by the NYISO subsequent to the ERON audit were not sustained. The MPAAS asked who was responsible for getting the TCC issues on the BIG list.

The MPAAS asked when the Board was advised of the additional TCC errors and adjustments made for 2000 through 2002? Was the Board advised prior to the completed 2004 settlements that errors existed beyond the 912 MWs? In this case, some MPs were in the final stages of securing their internal control certification, as required by Sarbanes-Oxley, Section 404, when the NYISO announced the additional TCC errors, although the NYISO had known about the errors for months. The MPAAS stated clearly that the NYISO processes must be changed to prevent the NYISO from failing to disclose errors or embarrassments found timely to the discovery of the errors or embarrassments.

The MPAAS discussed the Group 1 and Group 2 errors, differentiating between revenue allocation issues and auction modeling issues, respectively. Ms. Thornton stated that there is a detailed description of these groups on the NYISO website. Mr. Ventura asked what the implication was of the 912 MWs and each group of items in Group 1 and Group 2. Mr. Rubin said they are not independent. The first set of changes would impact the second. Mr. Ventura commented that the impact of the error corrections of those errors unrelated to the 912 MW was effectively hidden in the total adjustment.

The group again expressed concern with the controls over the infrastructure. The issues identified appeared to be very basic controls that should have been caught by

the reviewers and independent auditors. Database reconciliation should have been a simple step, especially in a SAS 70 audit. Why wasn't this caught during the SAS 70 audit?

Mr. Brennan expressed concern that the errors that brought about the TCC problems represented very basic controls that the NYISO had not had in place and that this is the very thing that the SAS 70 is supposed to detect. He stated that if the MPs could not rely on the NYISO to implement the right controls and furthermore could not rely on the KPMG SAS 70 audit to detect and correct situations like this then their only alternative would be to conduct their own third party audits under Article 10 of the Tariff. He further expressed concern about the lack of utility experience on the part of the KPMG staff assigned to the SAS 70 audit and suggested NYISO consider rotating SAS 70 audit firms and try to have staff with more utility experience assigned.

Mr. Farrell said that it seemed as though the NYISO was going in the right direction and asked if Ms. Thornton could expand her expertise into other areas such as SMD2 (LBMP pricing). Mr. Budd stated that aggressive steps were being taken towards improving controls at the NYISO.

IV. TCC Audit Briefing

Mr. Ventura gave MPAAS members an update on the Ernst and Young Audit. He reported that the TCC holders had not gotten back to him until February 1st and that there were minor errors and some changes in directional flows. Additionally, the audit could not be performed under the confidentiality agreements disclaimer that the NYISO would not take responsibility for accuracy or completeness under the audit.

Mr. Budd reported that that the lawyers were close to an agreement. There was a two-phase plan to:

1. Review all processes
2. Perform procedures.

Mr. Gioia mentioned 2002 – 2004 data. The audit agreements should be separate since the 2000-2002 period only related to Transmission Owners. The TOs were prepared to do it and after performing the first audit, the second phase should be fairly simple. For the first audit, Ernst & Young agreed to accept the technical work of Mr. Mike Cadwalader to look at the equations to make sure they are proper. Had the equations been worked through to completion?

Mr. Ventura reported that Mr. Cadwalader is on vacation and, therefore, Mr. Ventura has not been able to get details. He will be back next week and they will talk and send out the draft agreement to the group. Mr. Ventura's hope is to begin the audit during the middle of April.

V. Article 10 process update.

Mr. Ventura briefed the group on Article 10. The adjustments were posted on the web. Mr. Rubin asked for comments, as to-date none had been received. An issue was raised with the confidentiality agreement (paragraph 13). Mr. Rubin suggested removing "or omissions" from the paragraph. He informed the group that whether or not the MPs make other changes, the NYISO will ensure that the phrase will be omitted from Article 10. Mr. Zeppetello brought up the list of his issues that were e-mailed to Mr. Rubin, who indicated that they had all been reviewed.

VI. 7. SAS 70 Type 2, comments on 2004 and 2005.

SAS 70 Type 2 comments on 2004 and 2005 reviews were discussed by MPAAS members. The MPAAS would like to be more involved in the current SAS 70 by reviewing/discussing KPMG's work plan. The MPAAS would like to see KPMG's program and verify their processes. The MPAAS recommended that the firm be rotated but, if that is not feasible, the KPMG partner and/or staff be rotated, bringing in people who are more experienced in the utility industry.

Mr. Rubin stated that a contract has been signed for 2005, but he will bring this concern back to the Audit & Compliance Committee. Mr. Ventura asked that SAS 70 include a test of TCC controls. Mr. Brennan agreed, saying that it makes sense to have a different set of eyes review this. Mr. Rubin will also bring this to the Audit & Compliance Committee.

VII. Audit briefing – 2005 plan

Mr. Rubin reported on the 2005 Internal Audit plan. The Audit & Compliance Committee asked for clarification on line number 65: billing/continuous monitoring. The group clarified that they were looking for a detailed explanation of the continuous line item monitoring that is done by Billing.

Action Item: Marc will report back to MPAAS with a detailed explanation on the continuous line item monitoring that is done by Billing.

VIII. Audit Plan Status

Mr. Rubin provided an update on the Audit Plan Status. The following audits were reviewed:

		<u>Issuance</u>	<u>COSO?</u>
4-21	Billing - KPMG Billing Issues	1/18/05	No
4-25	IT Systems Penetration - External Hacking	11/8/04	No
4-26	IT Systems Penetration - Internal Hacking	9/30/04	No
4-27	IT - Security - Remote	2/11/05	No
4-32	Cash Management	10/27/04	Yes
4-33	Reliability Cost Allocations	10/15/04	Yes
4-34	ICAP Commitment & Monitoring	10/27/04	Yes
4-35	Price Validation	12/2/04	No
4-36	Monthly Billing	3/3/05	No
4-38	Web-Based Reconciliation - Stress Testing	9/28/04	No
4-39	Risk Management - ERM Process	1/6/05	No
4-40	Code of Conduct	11/2/04	Yes
4-41	ICAP Market	2/10/05	Yes
4-42	IT - COSO Alignment	2/15/05	No
4-46	Customer Settlements Follow-Up	11/2/04	No
4-48	MMU Follow-Up	11/2/04	No
4-49	Manual Billing Adjustments	1/27/05	Yes
4-50	Power System Operations Training	2/10/05	No
4-53	2002 Customer Settlements - Follow-Up	2/10/05	No
4-54	Regulatory - Follow-Up	2/3/05	No
4-56	2000-2002 Resource Reliability - Follow-Up	3/7/05	No
4-57	Contractor Performance	3/7/05	No
5-03	Customer Technical Services - Follow-Up	2/10/05	No

IX. Other Business

Mr. Ventura expressed concern with some SMD2 implementation issues. He asked that Mr. Rubin look into pricing on March 20th (Capital area – hour beginning 2200 and 2300) RT LBMP. The pricing at 22 hours is \$54.00, hour 23 is -\$15.00.

Action item: Mr. Rubin will look into this and report back. This could be a reserved price.

Other issues were raised, including Attachment N verification. No one had seen this. There was a spreadsheet concern on UCAP. It was asked if anyone was doing anything to verify TCC surcharges. Were the actual dollars paid back and the interest calculated? Funds paid out were paid from working capital – as a surcharge on TCC and interest on working capital. These were being paid by the TCC owners. Was anyone checking that the amounts paid were correct and that the interest was correct? Was this a manual process done with spreadsheets?

The MPAAS asked that Mr. Rubin look into this. Because there were many MPAAS issues that were also related to BAWG, Mr. Brennan asked that a BAWG representative attend the MPAAS meetings, and in addition, if BAWG was to raise a significant issue, look into having a NYISO person report on the controls. The MPAAS will provide a list of concerns as they arise to Mr. Rubin.

Mr. Ventura asked about the new facility and the Alternate Control Center and the suggestion that was made to look into hiring a Construction Manager. He stated that the construction should be watched by someone who has construction auditing expertise, and a periodic review of payments to the contractor should be performed. Mr. Ventura asked if anything had been done about this request. Was the NYISO hiring a management/inspector to watch over the contractor and to review the phases of the contractor? Mr. Budd reported that a construction/engineer team has been assigned to the project that he thinks performs in the role of construction management as well. Mr. Budd did not think that auditing the payment schedule was in the plan.

X. Next Meeting.

The next two MPAAS meetings were scheduled to be held June 16, 2005 in White Plains and August 17, 2005 at the NYISO in Albany.

Action items:

Action Item: Mr. Rubin will report back to MPAAS with a detailed explanation on the continuous line item monitoring that is done by Billing.

Action item: Mr. Rubin will look into the noted SMD2 pricing issue and report back. This could be a reserved price.

Mr. Rubin will look into TCC surcharges. Were the actual dollars paid back and the interest calculated? Funds paid out were paid from working capital – and recovered as a surcharge on TCCs with interest on the working capital advanced for the pay out. These were being paid by the TCC owners. Was anyone checking that the amounts paid were correct and that the interest was correct? Was this a manual process done with spreadsheets?

Open Questions:

Mr. Ashman asked if the SAS 70 audit included checking instances where spreadsheets were being used, and if not, why not?

MPAAS asked who was responsible for getting the TCC issues on the BIG list?

The MPAAS asked when the Board was advised of the additional TCC errors and adjustments made for 2000 through 2002? Was the Board advised prior to the completed 2004 settlements that errors existed beyond the 912 MWs?

Why wasn't this [database controls] caught during the SAS 70 audit?

Mr. Rubin will bring the following issues to the Audit and Compliance Committee of the Board:

**SAS 70 Audit: Rotate the Firm in a future year (2005 contract signed)
Rotate the KPMG Partner and/or Staff on the audit
Include testing of TCC Controls**