

# ISO rule 9.1.5 - Project Procurement Compliance Monitoring Audit Process

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## Appendices

(click on the links below to access the appendices in the AESO's website)

- A. [Information Request Letter 1 \(IR1\) template – Initial Notification of Compliance Monitoring Audit and Request for Summary of Project Materials](#)
- B. [Summary of Project Materials template](#)
- C. [Information Request Letter 2 \(IR2\) template – Request for TFO records](#)
- D. [Pre-audit Conference Meeting Agenda](#)
- E. [Compliance Monitoring Audit Query Form template](#)

## 1 Introduction

This document is intended to provide market participants with a comprehensive description of the Alberta Electric System Operator's (AESO) Compliance Monitoring Audit process for monitoring Transmission Facility Owner's (TFO's) compliance with Subsection 9.1.5 of the ISO Rules while carrying out Transmission Facility Projects. This Compliance Monitoring Audit process document is a guide and not an authoritative document.

A Compliance Monitoring Audit is conducted in accordance with Subsection 103.12 of the ISO Rules *Compliance Monitoring*, which describes the processes and guiding principles by which the AESO monitors and investigates the compliance of market participants with applicable rules and standards. This document describes the development of the process as well as the procedures used in carrying out the audit.

## 2 ISO rule 9.1.5

Subsection 9.1.5 of the ISO Rules describes the procurement requirements which pertain to the Designated TFO when carrying out the construction of transmission facilities during a Transmission Project. It requires that the Designated TFO solicit written bids from not less than three (3) arm's length suppliers when procuring Project Materials forecasted to exceed \$10,000 in cost. It further requires that the lowest priced, fully compliant bid be selected to provide those materials. The rule allows exceptions to one or both of these requirements in certain specific situations.

Subsection 9.1.5.8 of the ISO Rules identifies the AESO's right to examine the books and records of the Designated TFO, including all written bids relating the procurement of Project Materials, to the extent reasonably necessary to verify, with respect to any Project, compliance by the TFO with Subsection 9.1.5 of the ISO Rules.

## 3 Compliance Monitoring Audit Objective

The objective of each Compliance Monitoring Audit is to assess the Designated TFO's compliance with Subsection 9.1.5 of ISO Rules in carrying out the construction of transmission facilities during a Transmission Project.

If during the course of the Compliance Monitoring Audit the AESO identifies possible contravention(s) of other subsections of the ISO Rules, such potential contravention(s) will be dealt with through a separate ISO Rule Subsection 103.12 process outside of the audit. The AESO may however identify any such possible contravention(s) as an observation in the Compliance Monitoring Audit Report.

## 4 Scope of the Compliance Monitoring Audit

- Project

The term 'Project' is defined within the Consolidated Authoritative Document Glossary as "...the means or manner by which a constraint or condition affecting the operation or performance transmission system could be alleviated as identified in a NID approved by the EUB pursuant to s.34(3) of the Act..."

- Procurement records

The scope of the Compliance Monitoring Audit includes all procurement records for all Project Materials subject to the requirements of Subsection 9.1.5 of the ISO Rules. This includes, for each Project Material selected for testing, records which demonstrate the following, as applicable:

- a) that a minimum of three bids were solicited from arm's length suppliers and that the bidder with the lowest price, fully compliant bid was selected;
- b) that, where the lowest priced, fully compliant bid was not selected, the TFO's decision is in compliance with the acceptable conditions outlined in Subsection 9.1.5.6 (a) (i-iii) of the ISO Rules; and
- c) that, for sole source arrangements, the TFO's decision is in compliance with at least one of the acceptable conditions outlined in Subsection 9.1.5.6 (b) (i-iii) of the ISO Rules.

- Project reports

Project reports required in Subsection 9.1.3, as they relate to the requirements of Subsection 9.1.5 of the ISO Rules.

## 5 Compliance Monitoring Audit Approach

### 5.1 Audit types

There are two types of Compliance Monitoring Audits as follows:

a) Full Audit

The AESO will determine which Transmission Projects will be audited in a given year. The AESO will make best efforts to give reasonable notice to the Designated TFOs that one or more particular Projects have been selected for a Compliance Monitoring Audit together with a tentative schedule of the audit.

b) Focused Audit

Focused audits are typically not scheduled and are generally limited in scope. Focused audits may arise from:

- i) a request from the MSA to verify self-reporting made by a TFO; or
- ii) other requests, such as:
  - o a complaint by a market participant or other interested person relating to compliance with ISO rules; or
  - o to perform any other ad-hoc assessments of compliance.

### 5.2 The approach

The approach taken to conducting a Compliance Monitoring Audit is designed to ensure thoroughness and accuracy in audit results while allowing the audit to be carried out in a reasonably efficient manner. Compliance Monitoring Audit design steps include:

- a) Identifying any risks in Project procurement and ensuring that the Compliance Monitoring Audit is tailored to these risks;
- b) Assessing the complexity of the Project and ensuring the Compliance Monitoring Audit takes this into account;
- c) Reviewing the contents of both Project Progress Reports and any Final Cost Reports and tailoring the Compliance Monitoring Audit to take into account any potential concerns raised in these reports;
- d) Considering the quantitative and qualitative aspects of each transaction relative to the value of the Project; and
- e) Applying judgment in a manner that is defensible, consistent, transparent and fair in areas where application of the rules requires such judgment.

### 5.3 Selecting the Transmission Facility Project to audit

Determining which Transmission Projects will be audited in a given year is a consultative process which takes into account some or all of the following factors:

- Status of the Transmission Facility Project (complete or ongoing);
- Comparison of final costs vs. original estimates (i.e. Projects with cost escalations are more likely to be audited);
- Assessment of the potential impact of non-compliance (i.e. large scale Transmission Facility Projects that have higher financial repercussions from non-compliance);

- Evidence provided in reporting (e.g. Final Cost Reports, Project Progress Reports, etc.) that competitive procurement is not carried out to significant extent;
- Compliance Review Right Period pursuant to Subsection 9.1.5.8 of the ISO Rules;
- The results of past Compliance Monitoring Audits for those TFOs;
- Consultation with AESO project personnel; and
- Reasonable distribution across TFOs and Projects.

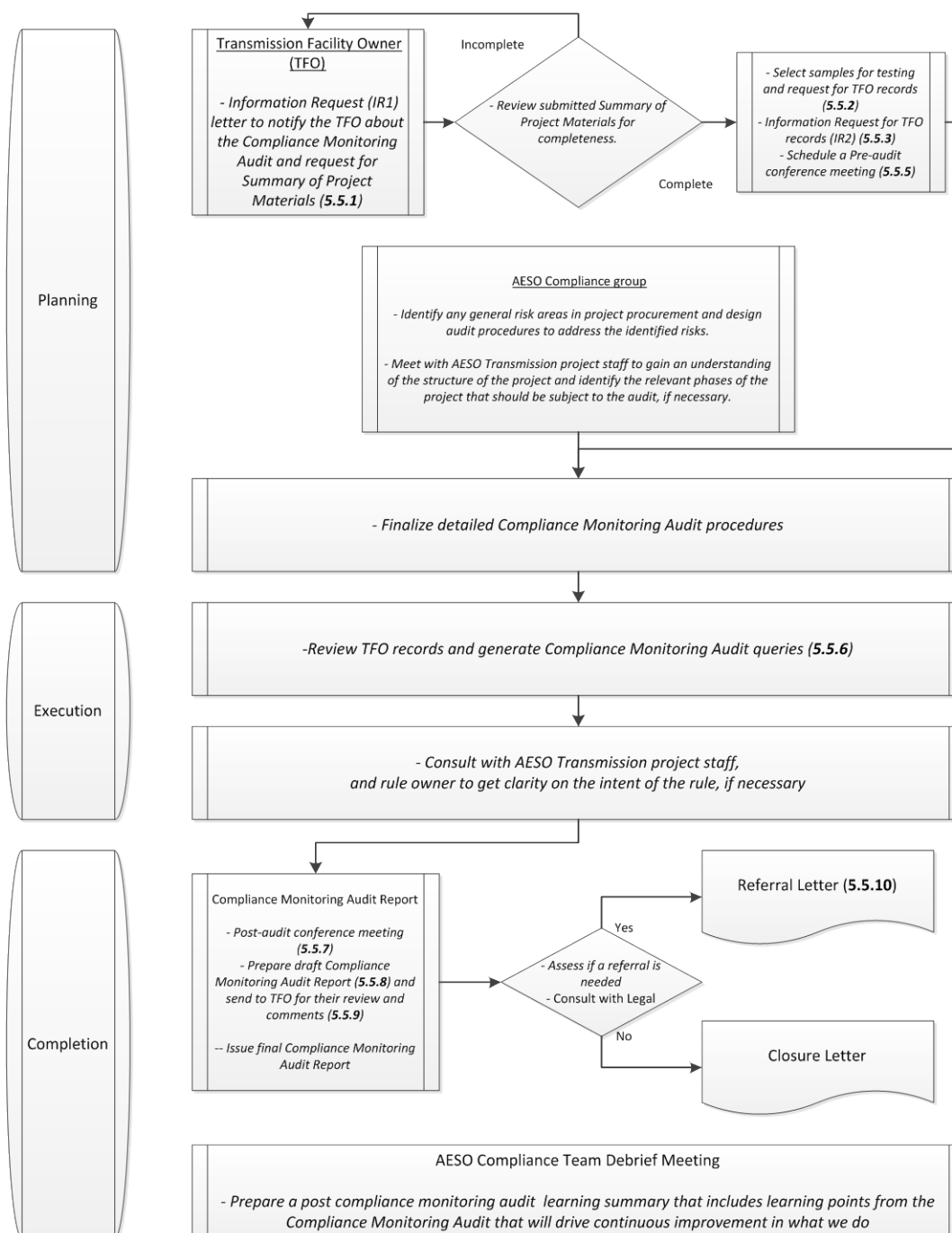
## 5.4 Risk and Planned AESO Approach

The Compliance Monitoring Audit is designed in the manner outlined below to address certain specific contraventions of the rule:

Assertion	Risk	Planned AESO Approach
The procurement data (i.e. Summary of Project Materials, refer to <a href="#">Appendix B</a> ) obtained from the TFO is accurate and complete.	<ul style="list-style-type: none"> <li>• Procurement data may be inaccurate and/or incomplete.</li> </ul>	<ul style="list-style-type: none"> <li>• Compare totals of the procurement data against the total Project Material costs reported in the Final Cost Reports and/or the Project Progress Reports. Investigate and assess reasonableness of variances.</li> </ul>
<p>Major and minor acquisitions subject to competitive bidding are in compliance with the ISO Rules.</p> <p>ISO rule reference: 9.1.5.2 9.1.5.3 9.1.5.5</p>	<ul style="list-style-type: none"> <li>• Written bids from at least 3 arm's length suppliers were not solicited.</li> <li>• Contract was not awarded to the party that submitted the lowest priced, fully compliant bid.</li> </ul>	<ul style="list-style-type: none"> <li>• Select a sample of Project Material costs that underwent the competitive bidding process for testing. Ensure written bids and/or short form written bids were solicited from at least 3 arm's length suppliers.</li> <li>• From the selected sample of Project Material costs that underwent the competitive bidding process, ensure lowest price, fully compliant bid was selected.</li> </ul>
<p>Contracts that are not awarded to the party that submitted the lowest priced, fully compliant bid are in compliance with the ISO Rules.</p> <p>ISO rule reference: 9.1.5.6 (a) (i) to (iii)</p>	<p><u>Lowest price bid not obtained</u></p> <ul style="list-style-type: none"> <li>• Exceptions are not supported by: <ul style="list-style-type: none"> <li>a) Commercial viability.</li> <li>b) Reasonable management explanations.</li> </ul> </li> <li>• Reasons for not awarding the contract to the lowest price fully compliant bid are not included in the Project Progress Report to the AESO.</li> </ul>	<ul style="list-style-type: none"> <li>• Obtain and corroborate explanations from the TFO supporting their decision not to go with the lowest bidder.</li> <li>• Assess based on judgment if the awarded supplier is the most commercially viable for the Project.</li> <li>• Ensure that the reasons for not awarding the contract in compliance with Subsection 9.1.5 of the ISO Rules were included in its Project Progress Report to the AESO.</li> </ul>
<p>Sole sourced arrangements are in compliance with the ISO Rules.</p> <p>ISO rule reference: 9.1.5.6 (b) (i) to (iii)</p>	<p><u>Bids not obtained</u></p> <p>Exceptions are not supported by one of the following:</p> <ol style="list-style-type: none"> <li>1) Evidence that only the entity is capable of providing the Project Material.</li> <li>2) Evidence that there was insufficient time to solicit bids.</li> <li>3) Evidence that there was insufficient information on which to base a bid.</li> </ol>	<ul style="list-style-type: none"> <li>• Obtain and corroborate explanations from the TFO supporting their decision not to obtain bids and assess based on judgment if the explanations are acceptable.</li> </ul>

## 5.5 Overview of the Compliance Monitoring Audit Process

The diagram below provides an overview of the Compliance Monitoring Audit process for a full audit.



In a focused audit, only a subset of the Compliance Monitoring Audit procedures for a full audit will be applicable.

In a focused audit in response to an MSA request to verify a self-report, the following procedures will apply:

- Information Request for TFO Records (see section 5.5.3)
- Submission of TFO Records (see section 5.5.4)
- Review of TFO records and generation of Compliance Monitoring Audit queries (see section 5.5.6)
- Compliance Monitoring Audit closure (see section 5.5.11)

In a focused audit in response to other requests, the following procedures will apply:

- Initial Notification of Compliance Monitoring Audit (IR1) (see section 5.5.1)
- Select samples for testing, if applicable (see section 5.5.2)
- Information Request for TFO records (IR2) (see section 5.5.3) (may be combined with IR1 if applicable)
- Submission of TFO Records (see section 5.5.4)
- Review of TFO records and generation of Compliance Monitoring Audit queries (see section 5.5.6)
- Post-audit conference meeting, Issuance of draft Compliance Monitoring Audit Report and TFO's review of the draft Compliance Monitoring Audit report (optional, subject to agreement with the TFO) (see sections 5.5.7, 5.5.8 and 5.5.9)
- Referral to the MSA, if applicable (see section 5.5.10) or Compliance Monitoring Audit closure, if applicable (see section 5.5.11)

A description of each of the procedures performed in the Compliance Monitoring Audit process is detailed below:

### **5.5.1 Initial Notification of Compliance Monitoring Audit (IR1)**

The AESO will notify the TFO of the scheduled Compliance Monitoring Audit, through an Information Request (IR) letter. A sample of the IR letter can be found in [Appendix A](#).

The IR letter will provide details regarding the Compliance Monitoring Audit and request the submission of specific information. The letter will:

- Identify the Transmission Facility Project selected for the Compliance Monitoring Audit;
- Request detailed description of, but not limited to, the following:
  - i. A Summary of Project Materials for the Project, and
  - ii. A breakdown of Engineering Costs for the Project;
- Indicate the deadline for the response to the IR; and
- Provide AESO contact information.

The Summary of Project Materials will be used to identify the Compliance Monitoring Audit samples for testing (refer to Subsection 6.4.2 of this document). Each Project procurement which qualifies as a major or minor acquisition as defined in Subsection 9.1.5 of the ISO Rules should be included in the list along with the following information:

- i. Purchase Order Number/Sub-contract Number;
- ii. Vendor/Sub-contractor Name;
- iii. Description; and

- iv. An indication of whether the Project Material was:
  - a. "Competitively Procured", including dollar values (on awards to lowest and non-lowest priced, fully compliant bids); or
  - b. "Sole sourced", including dollar values.

The Purchase Order/Sub-contract values should be the estimated total value that appears in the signed contract with the awarded vendor/sub-contractor, including any change orders that would have been approved thereafter. A sample template of the Summary of Project Materials can be found in [Appendix B](#).

The breakdown of Engineering Costs will be used to assess the appropriateness of excluding these costs from Project Materials as defined in the ISO *Consolidated Authority Document Glossary*.

### **5.5.2 Select samples for testing**

The Summary of Project Materials will be reviewed by the AESO for completeness through comparison with the most recent Project Progress Reports and/or Final Cost Reports for the relevant Project. A reconciliation of the differences should be included in the response to IR1 for us to understand what purchases were included or excluded from the Summary of Project Materials.

Once completeness has been ascertained samples for testing will be selected from the Summary of Project Materials. The goal of the Compliance Monitoring Audit is to ensure compliance with Subsection 9.1.5 of the ISO Rules. Reviewing all procurement of Project Materials that qualify as major or minor acquisition in relation to a Transmission Facility Project may not be possible and the cost of testing 100% of the information may not be warranted. In this regard, testing is typically carried out on only a sampling of the Project Materials.

The AESO currently applies a non-statistical, judgment-based selection sampling technique. The following are some of the criteria which will be applied when selecting the samples for testing:

- a) Value of the items – ensuring sufficient number of samples will be included to provide adequate coverage;
- b) Relative risk – ensuring that items prone to error due to their nature are given special attention; and
- c) Representativeness – ensuring that the AESO is satisfied that the samples provide breadth and coverage over all types of items in the population.

### **5.5.3 Information Request for TFO Records (IR2)**

Once sample selection has been completed the TFO will be notified through a second IR letter of the Compliance Monitoring Audit samples that the AESO has selected for testing. This letter will include the following details:

- the list of samples selected, with Purchase Order Number/Sub-contract Number references;
- the deadline for the response to the IR; and
- a description of the evidence that would allow the AESO to determine the compliance or non-compliance of the samples selected.

This evidence may include such things as the original bid request form sent to a vendor evidencing solicitation of bids, including evidence that it was actually sent to the solicited vendor; original bid response from all vendors that responded to the solicitation or decline to bid responses; documentation of explanations for contracts not awarded to lowest priced, fully compliant bid and sole source arrangements (i.e. email correspondences, letters, Project Progress Reports, etc.) that are dated during the time of the procurement.

A sample of the IR2 letter can be found in [Appendix C](#).



#### 5.5.4 Submission of TFO Records

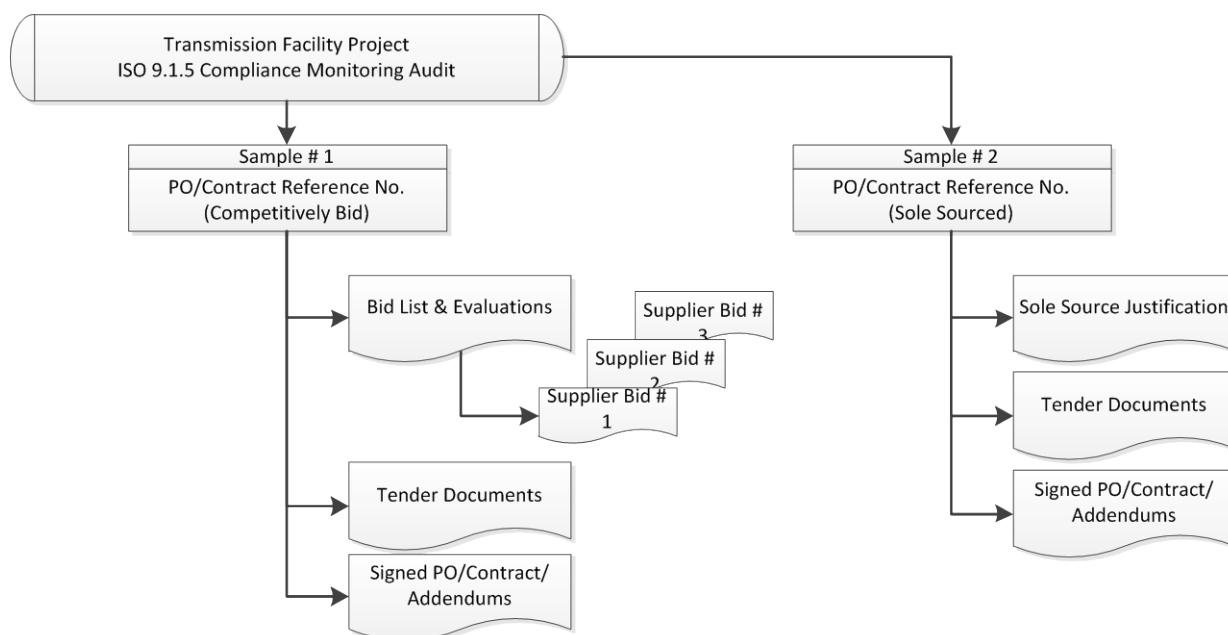
The TFO must submit the TFO records to the AESO by the date specified in the IR letter, as discussed in the preceding Subsection.

The TFO records must be submitted in one of the following forms:

- Electronic submission – Data submitted electronically through an email must be transmitted to Transmission Project Compliance via [tpcompliance@aeso.ca](mailto:tpcompliance@aeso.ca) on or before 11:59 p.m. MT on the due date specified. An electronic record of the submission must be retained by both the AESO and the TFO as proof of timely submission. The receipt of the email will be confirmed by the AESO.
- Physical submission of hardcopies or electronic storage devices (using Mailing Services; Canada Post, FedEx, UPS, DHL, etc.) – Physical data submissions which are submitted through federal or commercial mailing service must be postmarked on or before the due date specified. The AESO will confirm to the TFO the receipt of the physical data.
- Physical Submittal of hardcopies or electronic storage devices (Personal Delivery) – Physical data submissions by personal delivery to the offices of the AESO by the TFO must be received at the AESO office by the close of business on the date specified. The AESO's office hours are 8:00 a.m. – 5:00 p.m. MT. The AESO will confirm to the TFO the receipt of the physical data.

The TFO records should be organized in a manner that would allow for ease in identification of evidences related to a sample selected. Documentation of the organization should be provided as part of the response.

An example organization is described below:



In addition, to ensure usability and integrity of the TFO records, the following guidelines should be followed when submitting files as evidence to the AESO:

- Documents, irrespective of electronic format or papers, should be clearly organized, and indexed to ensure a quick referencing to the required documents.
- The AESO requests all data, files, information, and documents submitted as audit evidence should be in electronic format which can be sent by email or stored in CD/DVD media unless it is not practical to do so.
- The AESO recommends electronic documents submitted as evidence should be in a Portable Document Format (PDF) unless is specified otherwise by the AESO. The PDF is requested to be text searchable, where possible.
- Where data or files are used for numeric data analysis and calculation, they should be submitted in spreadsheet (.xls) format.
- Records may be submitted via e-email as an attachment. Each submitted electronic file by email should be 10 Mb or smaller in size. Where more than one submission by email are required, they should be numbered and clearly identified in the subject (e.g. Email #1 of 3).
- Where the total size of the records exceed 50 Mb, physical submittal of electronic storage devices such as CD/DVD is required. Each CD/DVD must have an external label that identifies the name of the Project, name of the TFO, date of submission and volume number (e.g. Volume # 1 of 3) and other essential identifiers.
- Files must not contain macros or scripts referencing information not included in the files.

#### **5.5.5 Pre-audit conference meeting**

The AESO will offer to organize a pre-audit conference call with the TFO. The purpose of this meeting would be to discuss the expectations of both parties and to answer any general questions that the TFO may have in relation to the Compliance Monitoring Audit. This meeting will also allow both the TFO and the AESO to establish the appropriate primary and secondary contacts during the Compliance Monitoring Audit and the appropriate TFO official that would be addressed in the draft and final Compliance Monitoring Audit Report.

A sample agenda for the pre-audit conference meeting is included in [Appendix D](#).

#### **5.5.6 Review of TFO records and generation of Compliance Monitoring Audit queries**

The records submitted to the AESO in response to IR2 will be reviewed to verify that the records submitted demonstrate compliance with Subsection 9.1.5 of the ISO Rules.

The review of the TFO records will take place over a period of at least ten (10) business days.

Throughout the course of the audit, the AESO may issue Compliance Audit Query Forms as questions and the need for clarifications arise as a result of the review of the TFO records. The TFO is expected to respond to these queries during the Compliance Monitoring Audit, and will be provided at least five (5) business days to respond.

A sample query form is included in [Appendix E](#).

#### **5.5.7 Post-audit conference meeting**

Following the substantial completion of the audit execution phase, the AESO will offer to arrange a post-audit conference meeting with the TFO. The purpose of this meeting will be to discuss the Compliance Monitoring Audit findings at a high level and to answer any general questions that the TFO may have in relation to the Compliance Monitoring Audit to this stage. At this stage, the AESO will not have determined whether or not there are any suspected contraventions.

#### **5.5.8 Issuance of the draft Compliance Monitoring Audit Report**

The AESO will then issue a draft Compliance Monitoring Audit Report (Report) based on the AESO's assessment findings. All queries, the TFO's response to the queries and AESO conclusions will be summarized and included in the Report. If any findings are considered potential suspected contraventions, these will be reported in the "Potential Suspected Contraventions" subsection of the Report.

The Report shall include, without limitation, the following:

- i) a description of the objective, scope, and methodology of the Compliance Monitoring Audit;
- ii) a description of the Compliance Monitoring Audit procedures and results, including any potential suspected contraventions with applicable rules and standards; and
- iii) the nature of any confidential information provided.

#### **5.5.9 TFO's review of the draft Compliance Monitoring Audit Report**

The TFO will be provided at least ten (10) business days to review and comment on the draft Report.

The TFO may include comments relevant to the Compliance Monitoring Audit findings in the TFO comments Subsection of the draft Report. The TFO may also include:

- the identification of records previously submitted which do not appear to have been reviewed or considered in support of the findings; and/or
- a different interpretation which does not appear to have been reviewed or considered in the AESO's findings.

The AESO, upon receipt of the draft Report will review the TFO's comments and determine whether further review of the TFO records is required. If it is determined that any record previously submitted was not reviewed or considered by the AESO, the TFO will be notified by the AESO that the previously submitted TFO record will be reviewed. Furthermore, the AESO will make the necessary internal consultations and then revise the draft Report for substantial changes needed.

If there are no substantial changes necessary, the AESO will finalize the Report. However, if there are substantial changes to the draft, a revised draft will be sent to the TFO for final review and comments. After receipt of the TFO's final comments, the AESO will finalize the Report.

Once the final Report is issued to the TFO, the Compliance Monitoring Audit process is considered closed.

#### **5.5.10 Referral to the Market Surveillance Administrator (MSA)**

Where, as a result of a full Compliance Monitoring Audit and documented in the final Report or a focused audit in response to other requests, the AESO has identified that there are one or more suspected contraventions of an ISO rule; the AESO will refer the matter to the MSA through the referral process in accordance with Subsection 103.12 of the ISO Rules. Referrals will be issued on a confidential basis.

To protect the confidentiality of TFO/vendor relationships, the vendor names are masked in the referral letter and associated audit report. Additionally Information Requests and Audit Query responses which contain these vendor names are omitted from the report. These details will be provided to the MSA upon request.

The AESO will notify the TFO when a suspected contravention is referred to the MSA in accordance with Subsection 103.12 of the ISO Rules. The copy of the referral to the MSA will be issued to the appropriate TFO official assigned by the TFO.

#### 5.5.11 Compliance Monitoring Audit closure

Where the AESO performed a full audit or a focused audit in response to an external request other than an MSA request, and has not identified suspected contraventions of an ISO rule as a result of the Compliance Monitoring Audit, the AESO will notify the TFO with a closure letter indicating that the Compliance Monitoring Audit is closed.

Where the AESO performed a focused audit in response to an MSA request, the AESO will notify the MSA with a closure letter indicating the results of the AESO's verification.

#### 5.5.12 Request for deadline extension

In the event the TFO is unable to meet the specified timeline in any of the above procedures, the TFO may request an extension of the due date for consideration. The request should be made in writing and include the new proposed due date for submission and the justification for the request. The AESO will work with the TFO to ensure a reasonable period of time is provided to respond to each request. In reviewing such requests, the AESO must also ensure TFOs are treated fairly and in a consistent manner.

#### 5.5.13 Retention of TFO records

In accordance with Subsection 103.12.14 of the ISO Rules, the AESO may retain in its possession information obtained in relation to the Compliance Monitoring Audit for as long as the AESO, in its sole discretion, deems necessary.

## 6 Confidentiality

Compliance Monitoring Audits conducted by the AESO will be done on a confidential basis. To protect any sensitive commercial information that would be exposed during the Compliance Monitoring Audit, the AESO will ensure that any letters and/or documents coming from the AESO that may contain sensitive commercial information will be protected with passwords.

Confidentiality of TFO records submitted to the AESO is governed under Subsection 9.1.6, Subsection 103.12.6 and Subsection 103.1 of ISO Rules.

## 7 Revision History

Revisions to this document may be made from time to time by the AESO. Market participants will be notified of revisions through the AESO Stakeholder Newsletter.

Revision	Date	Comments
1.0	May 4, 2012	Initial version of the document.
2.0	February 28, 2013	<ul style="list-style-type: none"> <li>Section 4 Compliance Monitoring Objective – added handling of possible contraventions outside the scope of the audit.</li> <li>Section 5 Scope of the Compliance Monitoring Audit – added Project Reports as part of the scope.</li> <li>Section 6.4.1 Initial Notification of Compliance Monitoring Audit (IR1): <ul style="list-style-type: none"> <li>added further details of the information request,</li> <li>added a request for breakdown of engineering costs.</li> </ul> </li> <li>Section 6.4.6 Letter of Representation – removed.</li> <li>Section 6.4.6 Review of TFO records and generation of Compliance Monitoring Audit queries:</li> </ul>

Revision	Date	Comments
		<ul style="list-style-type: none"> <li>○ removed references to a letter communicated substantial completion of the audit fieldwork,</li> <li>○ added minimum number of days to respond to a query</li> <li>• Section 6.4.12 Retention of TFO records – updated to reflect Subsection 103.12 of the ISO Rules.</li> <li>• Updated Appendices to reflect the above changes</li> <li>• Other changes including formatting section headings and correcting rule references.</li> </ul>
2.1	May 16, 2013	<ul style="list-style-type: none"> <li>• Section 1 Introduction – added an indication that this document is a guide and not an authoritative document.</li> <li>• Section 3 ISO rule 9.1.5, Section 5 Scope of the Compliance Monitoring Audit, and Subsection 6.3 Risk and Planned AESO Approach – revised references to “solicitation of not less than three (3) arm’s length suppliers.”</li> <li>• Section 5 Scope of the Compliance Monitoring Audit – removed discussion about what constitutes a Project.</li> <li>• Other minor formatting changes.</li> </ul>
2.2	September 30, 2013	<ul style="list-style-type: none"> <li>• Section 5.1 Audit Types – added a description of two (2) types of audit that can be initiated.</li> <li>• Section 5.5 Overview of the Compliance Monitoring Audit Process – added a description of procedures applicable to focused audits.</li> <li>• Section 5.5.10 Referral to the MSA – added reference to focus audit in response to other requests and protection of confidentiality of TFO/vendor relationships.</li> <li>• Section 5.5.11 Compliance Monitoring Audit closure – added new section to describe audit closure process.</li> </ul>