



2011 Financial Report

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2011 Financial Statements

Letter from the CEO

ISO New England is pleased to issue its *2011 Financial Report*. This document includes a summary of last year's operations and our financial position, as well as our financial statements audited by independent public accounting firm KPMG LLP.

For the past several years, ISO New England has produced a Regional Electricity Outlook (REO) to update stakeholders on current ISO New England initiatives and provide a perspective on regional issues that may affect power grid operations. The most recent REO, the [2011-2012 Regional Electricity Outlook](#), detailed the region's multiyear Strategic Planning Initiative.

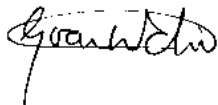
The New England energy climate is evolving at a rapid pace. Federal and state energy and environmental policies, market pressures, and technological innovation are driving a major transition in the electric power industry that will affect the way the power grid looks, functions, and operates in the future. To prepare for this new paradigm, ISO New England, market participants, legislators and regulators, end-users, and other industry stakeholders have identified five key challenges that could affect power system reliability in the short and long terms. They are resource performance and flexibility, increased reliance on natural-gas-fired capacity, the retirement of generators, the integration of variable resources, and the alignment of markets and planning.

The *2011 Financial Report* reflects ISO New England's extensive work last year on the initiative. In 2012 and beyond, we will continue to focus on these issues and as well as market enhancements that can guide the development of cost-effective investment in the resources and infrastructure that will prepare the New England power grid for the future.

As a not-for-profit, ISO New England largely measures success through its ability to provide quality services, resulting in high levels of customer satisfaction. We are dedicated to being efficient and responsive and place great emphasis on controlling costs, being accountable and transparent, and maintaining strong internal controls. This is evident in our ability to develop a responsible annual budget with the support of our stakeholders.

On behalf of ISO New England, I thank our market participants, state officials, consumers, and other electricity stakeholders for a productive year in 2011. I look forward to working with you in the future, as we continue to serve the 14 million New England residents who depend on us for a reliable power system and competitively priced electricity.

Sincerely,



Gordon van Welie
President and Chief Executive Officer

Management's Discussion and Analysis

The Company

ISO New England Inc. (ISO) is a regional transmission organization serving Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, and Vermont. The ISO meets the electricity demands of the region by fulfilling three primary responsibilities:

- Minute-to-minute reliable operation of New England's bulk electric power system, providing centrally dispatched direction for the generation and flow of electricity across the region's interstate high-voltage transmission lines and thereby ensuring the constant availability of electricity for New England's residents and businesses.
- Development, oversight, and fair administration of New England's wholesale electricity marketplace, through which bulk electric power has been bought and sold since 1999. These competitive markets provide positive economic and environmental outcomes for consumers and improve the ability of the power system to meet ever-increasing demand efficiently.
- Management of the comprehensive planning processes for the bulk electric power system and wholesale markets to address New England's electricity needs well into the future.

The ISO is an entity organized as a nonstock corporation under the *General Corporation Law, as amended*, of the State of Delaware. The company has been recognized by the US Internal Revenue Service as an organization described in Internal Revenue Code (IRC) 501(c)(3) and is generally exempt from income taxes under IRC Section 501(a).

Current Environment

ISO New England has identified numerous priorities for 2012 and beyond that correspond to its three core objectives. ISO New England fulfills these responsibilities while ensuring that its business operations are well managed, cost effective, and responsive to New England's market participants, state officials, and other electricity stakeholders.

Projects and initiatives for 2012 will encompass three major strategic areas: planning and operations, wholesale markets, and, capital project plans. More specifically, the strategic planning process has identified the following near-term challenges: the retirement of uneconomic capacity, the dependence of power system operations on natural gas system infrastructure, and the performance and flexibility of current power system resources. Major projects and initiatives the ISO will undertake in 2012 that incorporate all the strategic areas of focus are described in the ISO's *2012 Wholesale Markets Project Plan* and *Roadmap for New England: A Proposal for Meeting the Challenges Identified in the Strategic Planning Initiative*. Both of these documents are available on ISO New England's website.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the following tasks:

- Management must make estimates and assumptions that affect the reported amounts of assets and liabilities.
- Contingent assets and liabilities must be disclosed at the date of the financial statements.
- The amounts of revenues and expenses during the reported period must be reported

Significant items subject to such estimates and assumptions include the useful lives of fixed assets; pension and postretirement benefits, including earnings rates, discount rates, healthcare cost trends, and reserve for employee benefit obligations; and other contingencies.

Accounting Policies

The *Fair Value Option for Financial Assets and Financial Liabilities Topic* of the Financial Accounting Standards Board Accounting Standards Codification gives entities the option to measure many financial instruments and certain other items at fair value. The ISO has elected to forgo the fair valuing of financial assets and financial liabilities for the year ending December 31, 2011, and believes that this decision has no material impact on the financial statements.

In compliance with the *Subsequent Event Topic* of the Financial Accounting Standards Board Accounting Standards Codification issued in May 2009, the ISO considered and determined that no events or transactions occur after the Statements of Financial Position but before the issuance of financial statements on March, 16, 2012. This provides added evidence regarding certain estimates or identifies matters that require additional disclosure.

The ISO implemented *Sarbanes Oxley 302* (SOX 302) compliance in 2003. SOX 302 is a set of internal procedures designed to ensure accurate financial disclosure as well as the disclosure of material information about the ISO to its signing officers. In 2009, the ISO added a critical vendor matrix to its SOX 302 disclosure. This matrix, prepared by the vice president of information services and the chief operating officer (COO), identifies those companies that provide very specialized goods or services to the ISO. The critical vendor matrix identifies the risk as well as a mitigation plan for the risk, where applicable. The ISO also developed disclosure checklists, which represent the essential internal controls for maintaining financial accuracy. The disclosure checklists are completed quarterly by department managers, senior officers, and the chief executive officer (CEO). The chief financial officer (CFO) reports the results of the disclosures and matrices quarterly to the Audit and Finance Committee of the board of directors. The Audit and Finance Committee must review the SOX 302 disclosure before the release of the quarterly unaudited financial statements.

In 2010, the ISO implemented a modified *Sarbanes Oxley 404* (SOX 404) compliance process to complement the SOX 302 procedures. SOX 404 is used to evaluate the control environment associated with financial reporting. To perform this evaluation, the ISO developed a principle evaluation matrix, which contains specific questions covering each of the seven principles that address the control environment component of the Committee of Sponsoring Organizations' guidance. Key individuals in the company complete the matrix annually, and the CEO and CFO review it for completeness and effectiveness. In addition, the accounts and amounts included on the Statement of Financial Position and the Statement of Activities are assessed annually to evaluate the risk of fraud, control effectiveness, and

various other risk considerations. The CEO and CFO review the results of the risk assessment and make recommendations for additional controls, as needed.

Tariff Recovery

Each year since its inception, the ISO has filed a new tariff with FERC to recover its operating costs and fund its capital expenditure program for the subsequent year. The ISO's funding recovery process is defined in Section IV of the *Transmission, Markets, and Services Tariff*.¹ The funding recovery process begins with the development of the annual budgets, which ultimately become the revenue requirement collected under Section IV.A of the tariff (Recovery of ISO Administrative Expenses) and the anticipated capital expenditures. In preparing the budgets, the ISO executes a rigorous process to ensure that the budgets submitted to stakeholders for review and FERC for approval are in line with the ISO's initiatives and goals and are just and reasonable.

The budgets are constructed on the basis of business plan initiatives the ISO sets for the coming five years. Senior management begins to develop the business plan at the start of the year preceding the budget year. The ISO reviews the plan with the board of directors as well as the stakeholders in the spring and early summer before establishing the budgets. The ISO meets with and obtains feedback from the New England Power Pool (NEPOOL), the New England Conference of Public Utilities Commissioners, the New England States Committee on Electricity, other state officials, and other interested stakeholders.

In July of each year, ISO department managers submit their budgets based on the business plan. Senior managers, including the CFO and CEO, review the budgets. Based on the outcome of this review, the ISO prepares a comprehensive presentation for discussion with the ISO's Board Audit and Finance Committee. The presentation includes information on the budget process, new initiatives, summarized budget data, budget details, depreciation and interest rates, the capital budget with explanations for each project, cash flow and pro forma financial projections for future years, and a comparison of cost data and services provided by other Independent System Operators and Regional Transmission Organizations.

Subsequent to the meeting with the Board Audit and Finance Committee, the budgets are presented in August to the NEPOOL Budget and Finance Subcommittee for review, input, and recommendation to the NEPOOL Participants Committee, which reviews and votes its recommendation to the board on the budget at its October meeting. During this August to October timeframe, the ISO solicits input on the budget from state officials. In October of each year, the ISO's full board of directors must approve the budgets before the budgets are considered complete and ready for filing with FERC.

The administrative costs budget and the capital budget approved by the NEPOOL Participants Committee and the board of directors provide the basis for Section IV.A of the tariff filed with FERC on November 1 of each year. Pursuant to Section IV.A, the ISO recovers its operating costs through the following three tariff schedules:

- Schedule 1— Scheduling, System Control, and Dispatch Service
- Schedule 2—Energy Administration Service
- Schedule 3—Reliability Administration Service

¹ *ISO New England Inc. Transmission, Markets, and Services Tariff* (ISO tariff), Section IV (2011), http://www.iso-ne.com/regulatory/tariff/sect_4/index.html.

Each year during the budget completion process, department managers allocate their budgeted costs by activity. Each activity has an allocation to the three schedules. An activity can be attributable to one, two, or all three tariff schedules. This process allows the ISO to compile the applicable year's budget broken down by the three tariff schedules. The costs applicable to each schedule or set of activities become the revenue requirement for that schedule. To arrive at billable rates, the costs are then allocated to market participants on the basis of the billing determinants that comprise the collection of the revenue requirements for that schedule. The billing determinants are based on both volumetric and transactional units, depending on the schedule.

Because actual costs will vary from the budgeted costs, as well as the projected billing determinants, Section IV.A of the tariff contains a true-up provision. Any over- or undercollection is recorded as deferred charges or deferred income, and the adjustment for the true up either increases or decreases the cost recovery in a subsequent tariff filing.

Liquidity and Capital Resources

As a nonstock, nonprofit organization, the ISO has neither equity nor any accumulated reserves. To fund its working capital needs, the ISO has a \$15 million line of credit provided by a bank. In addition, to support shortfall payments under the ISO New England Billing Policy, the ISO has a \$4 million line of credit provided by a bank. In July 2009, the ISO refinanced the expiring lines of credit for a new three-year term, which will expire on July 1, 2012. Section IV.B of the tariff (Capital Funding Arrangements) is the backstop to all of the ISO's borrowings in the event that any of the debt repayments are accelerated. The ISO will be renewing the lines of credit in June 2012.

In 2004, the ISO completed a 10-year plan of funding for future capital expenditures. The program included funding for an average of \$20–\$24 million in capital spending for the next 10 years. The ISO reviewed many available financing options for cost effectively meeting the needs of the spending program. As a result, the ISO issued 10-year private-placement fixed-rate notes in the amount of \$39 million and discontinued its practice of securing new term-loan debt each year. The fixed rate for the private placement debt is 5.6%. By issuing the 10-year notes, the ISO saves the cost of borrowing new money each year, as well as the cost of filing with FERC, and instills budgetary discipline in the capital expenditure program. As projects are placed in service and begin to depreciate, the depreciation expense is recovered under Section IV.A of the tariff and becomes available for funding future capital spending requirements.

In 2005, the ISO secured \$45.5 million of tax-exempt debt to finance its new control center and renovate and consolidate its existing office facilities. The debt is comprised of multimode, variable-rate, civic-facility revenue bonds, which reprice weekly. The bonds were issued by the Massachusetts Development Finance Agency and are being repaid over 25 years. The current weekly interest rate is 0.18%. The weighted average cost of the debt for 2011, including the direct-pay letter of credit, was 1.37%.

The ISO is in the process of reviewing with its stakeholders plans for a new backup control center (BCC) in order to continue to meet the needed expansion of systems and people due to the complexity of the operating environment that has increased greatly over the last seven years. The ISO will seek the authorization for spending and financing the new BCC through the necessary FERC filings. The current targeted completion date of the project is mid-2014.

Regulatory Update

Federal lawmakers continue to consider energy policies that will have an impact on the ISO, including those that address incentives for renewable and alternative energy sources, the domestic production of oil and gas resources, and strengthened cyber security laws. The US Environmental Protection Agency has issued a final rule limiting mercury and other toxic air emissions from power plants that could result in moderate retirements of older, fossil-fired power plants in the next three or four years. A cooling water rule (expected to be final in 2012) also could affect the operation of generating facilities beginning in 2018.

The ISO continues to participate in the Eastern Interconnection Planning Collaborative (EIPC) in support of the US Department of Energy's interconnection-wide transmission analysis project. Phase 1 of the project focused on the formation of a diverse stakeholder group, the modeling of 80 public policy "futures" through the use of macroeconomic models, and the selection of three of these "futures" for in-depth transmission analysis. A Phase 1 report was issued in December 2011.² The EIPC is now focusing on Phase 2 of the project—the development of transmission build-out options for the three selected scenarios. Like Phase 1, Phase 2 will culminate with a report, currently scheduled for completion by mid-2013.

The ISO and transmission owners are implementing the Smart Grid Investment Grant from DOE. The goal of this project is the installation of approximately 40 phasor measurement units (PMUs, or synchrophasors) as well as communications infrastructure across the transmission system. To date, 12 PMUs have been installed and are streaming test data to the ISO. The full implementation of the project is expected by June 2013.

The Federal Energy Regulatory Commission issued orders in 2011 that require significant implementation and compliance efforts of the ISO. Modifications to the energy market to allow for the participation of price-responsive demand is set to be implemented in two phases, beginning with a transition in 2012 followed by full integration in future years. Modest reforms to the Forward Capacity Market will be needed in 2012 for the seventh Forward Capacity Auction (FCA). The ISO also will submit to FERC in 2012 compliance filings for the implementation of changes for the eighth FCA. The ISO and stakeholders are aiming for the development of longer-term structural improvements. Conceptual development and market design will begin in 2012 and continue through 2013. However, the full implementation of the needed changes in New England is expected to take several years.

FERC-ordered enhancements to the transmission planning process include the addition of capability and processes to plan for transmission infrastructure driven by public policies. Compliance through the regional stakeholder process will take place throughout 2012 and into the first quarter of 2013.

Results of Actual Operations

Table 1 summarizes the actual amounts and percentage of total expenses for the years ending December 31, 2011, and 2010:

² The EIPC report is available at <http://www.eipconline.com>.

Table 1
Actual Amounts and Percentage of Total Expenses (millions of \$)

Year Ending December 31,	2011	2011	2010	2010
Salaries and benefits	\$ 78.6	56.3%	\$ 70.8	55.3%
Depreciation and amortization expense	24.6	17.6	22.2	17.3
Professional and consultants fees	12.3	8.8	13.1	10.2
Computer services	6.8	4.9	5.7	4.4
Northeast Power Coordinating Council dues	4.5	3.2	4.2	3.3
Communication expense	2.0	1.4	1.8	1.4
Interest expense	1.7	1.2	1.9	1.5
Insurance expense	1.7	1.2	1.7	1.3
Board of directors	1.1	0.8	0.9	0.7
Building Services	0.9	0.7	1.1	0.9
Utilities	0.9	0.7	0.9	0.7
Other	4.5	3.2	3.8	3.0
Total	\$ 139.6	100.0%	\$ 128.1	100.0%

Total expenses increased by \$11.5 million, or 9.0%, in 2011 over 2010. Expenses net of depreciation, amortization, and interest increased \$9.3 million, or 8.9%, in 2011 over 2010. The changes primarily were the result of the following factors:

- Salaries and benefits increased \$7.8 million, or 11.0%, in 2011. The increase was attributable to cost-of-living increases and an increased headcount to support initiatives and other identified company needs. The initiatives include System Planning work to increase the throughput of analyzing transmission solutions and Market Operations and Information Technology work to improve the delivery of information and user-interface technology and to evaluate new applications that provide for the increased optimization of the power system. Additional staff also was added in Market Monitoring to improve data analysis and systems support, in Human Resources to improve recruiting and retention efforts, and in Information Technology support to position the company to be able to provide around-the-clock support for the backup control center.
- Depreciation and amortization expense increased by \$2.4 million, or 10.8%, in 2011. The increase is due to a number of projects going live in mid-2010 or 2011, including the third phase of the Forward Capacity Market project, demand-resource integration, phase two of the Standard Market Design upgrade, and phase one of Business Continuity Plan infrastructure improvements. These depreciation increases were partially offset by projects that became fully depreciated in 2010 or mid-2011, including the first phase of the Forward Capacity Market and the Energy Management System (EMS) upgrade project.
- Professional and consultants fees decreased \$0.8 million, or 6.1%, in 2011 compared with 2010. The decrease was largely a result of reduced legal fees in 2011 because of less development work for the

Forward Capacity Market redesign filings, fewer answers to protests in 2010, and other miscellaneous reductions. Other costs for professional fees were flat overall from 2010 to 2011; however, many of these costs are nonrecurring from year to year. In 2011, costs included consulting on the Strategic Planning Initiative to assist senior management with addressing a number of key risks identified through the corporate risk management function. These risks include resource performance and system flexibility, increased reliance on natural- gas-fired capacity, potential retirement of generators, integration of variable resources, and alignment of markets with planning. Additionally, 2011 costs included preliminary work on determining a solution for replacing the backup control center and easing space requirements at the company's main operating facility. Certain costs from 2010 were not repeated in 2011, including those for the Information Delivery Operational Excellence project and a wind study, which was conducted to determine measures needed for incorporating wind forecasting and wind resources into ISO processes, scheduling, and dispatch services.

- Computer services increased by \$1.1 million, or 19.3%, in 2011. This increase was due to added licenses for database and applications software to handle a growing number of users of company data, both internal and external to the ISO; increased maintenance costs of the Forward Capacity Auction software; and hardware servers purchased in 2010, in addition to increased licenses related to cyber security.
- Interest expense decreased \$0.2 million, or 10.5%, in 2011. The decrease is attributable to a reduction in interest expense on the company's working capital line of credit resulting from lower borrowing needed in 2011 and a reduction on the company's tax-exempt debt, primarily due to lower rates and a slightly lower balance in 2011.
- The expense for the board of directors increased \$0.2 million, or 22.2% in 2011. The increase in these expenses primarily is attributable to an increase in the annual board member retainer and for additional board committee meetings to meet operational requirements.
- Building services decreased \$0.2 million, or 18.2% in 2011 due to nonrecurring battery maintenance costs incurred in 2010.
- The "Other" expense line shown in Table 1 increased \$0.7 million or 18.4% in 2011. The increase includes losses on the disposal of capitalized loan fees upon the midterm repricing of the company's working capital line of credit. It also includes tax-exempt debt to take advantage of lower interest rates and the write off of accumulated costs for two capital projects that had initially been capitalized but were deemed to be obsolete. Other increases over 2010 were for the purchase of credit rating subscriptions to ensure compliance with FERC Order 741 and increased training and travel costs as a result of the additional company headcount.

Capital Spending

The FERC-approved capital expenditure budget for 2011 was \$26.5 million. Actual spending was under budget by \$1,829,000, primarily as a result of delays in the design and approval for the Forward Capacity Market reform and price-responsive demand projects. These projects are expected to span into 2012 and beyond. A number of other smaller dollar changes have occurred in 2011 capital spending.

Major projects in 2011, some of which are ongoing and multiyear, are as follows:

- *Standard Market Design Upgrade Phase III.* Phase III will upgrade the framework of the eMarket and eFTR user interface. The market operator interface also will be enhanced to allow control room operators to send manual dispatch instructions directly to generators, via remote terminal units, when the market system is unavailable.
- *Business Continuity Plan Infrastructure Enhancements, Phase II.* This project was the second of three stages of an initiative that began in 2008 to update the ISO's infrastructure to enhance business continuity. Phase II included synchronization of the master control center and backup control center networks and the creation of a locationally independent web presence, such that external web applications may be available at the BCC independent of other ISO functions. The total project costs were \$2,443,000, and the project was completed in November 2011.
- *Synchrophasor Infrastructure and Data Utilization.* The ISO and the New England transmission owners received a grant, in conjunction with their application under a DOE Funding Opportunity Announcement 0000058 for Smart Grid Investment Grant, to focus on bulk power system operations associated with the installation of phasor measurement units. The company is eligible to receive reimbursement of \$7,900,000, or up to 50% of the total project costs, which were initially estimated at \$18,100,000. The project cost may total less than the \$18,100,000 based on a revision to the budget; however, the scope of the project will remain the same. The ISO and the transmission owners will incur the 50% of the costs that DOE does not reimburse.

The ISO's 2012 capital budget for this project is \$1.6 million. The ISO expects to receive 50% reimbursement from the Department of Energy, resulting in a net spend for the ISO of \$4.8 million, of which \$4.1 million is expected to be for capital expenditures. The remaining project costs will be borne by the participating transmission owners and are not included in the ISO's capital costs. The project is expected to be complete in the second quarter of 2013.

- *Energy Management System (EMS) Upgrade and Enhancements.* This project will upgrade the hardware and software for the existing EMS 2.3 and Habitat 5.6 platforms, communication front-end of the EMS, and testing and training simulator environment system to the EMP 2.6 and Habitat 5.8 platforms to stay current with supported versions. This project allows the ISO to take full advantage of the latest product features and will simplify and reduce the cost of future upgrades. This project will ultimately enhance the reliability of system operation. The estimated total cost for this project is \$4,071,000. The targeted completion date for the project is October 2012.
- *Web Enhancements Phase I.* This project will address the recommendations resulting from the 2010 Information Delivery Operational Excellence initiative. The project encompasses several improvements to the ISO's external website that will add a significant increase in external user functionality, ease maintenance of the website, and improve the reliability of the website. The focus of this project is on the real-time operational data used on a daily basis to make business decisions. The primary scope of this project consists of the design and development of XML operational data feeds, and the implementation of a new portal solution that is flexible and easily maintainable. The estimated total cost for this project is \$1,974,000. The targeted completion date for this project is May 2012.
- *Market Mitigation Automation.* This project will convert a very manual, time-intensive process and integrate mitigation into the real-time dispatch process. Currently, the Internal Market Monitor has the ability to mitigate the marginal unit (i.e., the unit setting the price) one unit at a time only as they sequentially set the price. The implementation of this automated process also will provide full compliance with the tariff in calculating the price impacts as outlined in *Market Rule 1*, Section III, Appendix A III.A.5.5.3. The automated process will provide the necessary precision in determining market impact and will result in identifying not just the marginal unit, as in the current manual process, but all resources within—for example, a constrained area that is affecting market outcomes

as a result of its supply-offer conduct. Additionally, the rule-based logic of automated mitigation will remove any perception of discretion from the market-impact testing and mitigation process. The total estimated project cost is \$2,220,000, and the targeted completion date is May 2012.

- *Generation Control Application (GCA) Phase I.* This project, which was launched in 2010, and placed in service in January 2012, developed a look-ahead commitment and scheduling capability in a study mode within the existing real-time unit-dispatch system, thereby forming the basis for a real-time dispatch mode with look-ahead functionality. This capability is improving (1) accuracy and optimality of the fast-start commitment/decommitment logic, (2) the analysis of intra-day power system trends, (3) the management of system uncertainty and commitment and dispatch instruction, (4) external transaction scheduling, and (5) the analysis tool for supporting operation decisions. The project addresses increased real-time dispatch and scheduling challenges, especially in the emerging area of the smart grid. The total cost for this project was \$1,633,000.
- *Software Development Costs.* In addition to the major projects described above, the ISO incurred \$1.8 million in software development costs. These costs supported a multitude of enhancements to existing software systems.

Risks

The ISO is exposed to financial risk in the three primary areas of interest rates, legal, and regulatory. The ISO historically has included in its annual budget two contingency funds to address unknown costs—a CEO emerging-work allowance and a board contingency. These contingencies typically represent a combined 1.0% to 1.5% of the total amount to be recovered each year under Section IV.A of the tariff. The CEO emerging-work allowance is used as part of the normal course of business, and disbursements are controlled by the CFO and CEO. The board contingency, subject to use only through board approval, has never been used. Because the ISO does not have any capital to draw on for unknown expenses, these two contingencies are necessary for the ISO to operate efficiently.

Fluctuating interest rates can have an impact on the costs of the ISO in several ways. Specifically, as discussed below, the ISO earns interest on the settlement funds it collects from market participants, pays a floating interest rate on its tax-exempt bonds, and uses interest-rate assumptions in establishing costs for its pension and postretirement benefit plans.

Historically the average float in the settlement account has been consistently higher than the outstanding principal of the tax-exempt debt and, therefore, an effective hedge against interest expense rates. A decrease in the settlement float will have a negative impact on the hedge against increasing interest rates. In 2011, the settlement float decreased on average approximately 9% from the 2010 levels. This decrease was primarily due to lower clearing prices in the energy markets. The decrease in float and the low interest rates, combined with the decreasing balance of tax-exempt debt, has had little overall impact to the hedge. Both interest income and interest expense rates have remained very low in 2012. The ISO regularly analyzes the interest-rate environments to ensure that its debt structure is as cost effective as possible, in addition to reviewing all debt and funding needs.

Interest rates also are used in the discount-rate assumptions for establishing the costs and liabilities associated with the pension and postretirement plans. Lower rates result in increased costs.

The ISO also has an exposure to costs resulting from litigation. The ISO does not budget for unforeseen litigation costs during the normal budgeting process. Therefore, any material unexpected litigation that arises during the course of the year would pose a risk to the ISO's ability to operate within the approved budget.

The ISO is always subject to new regulatory orders issued by FERC and NERC. If the ISO is not aware of the new requirement when the budget is prepared and submitted for approval to FERC, the ISO could be at risk for any additional cost associated with the new requirement.

Billing and Credit

The ISO is responsible for billings associated with the wholesale electricity markets for New England's bulk power generation and transmission system, as well as ensuring that proper measures are in place to mitigate participants' exposure to credit risk from transacting in the ISO-administered markets. Since its inception in 1999, the ISO has continually reviewed the billing and financial-assurance policies and, since 2004, has made great strides in reducing the credit risk for market participants.

The most recent modifications to the financial-assurance policy implemented in October 2011 were made in response to FERC's Order on *Credit Reforms in Organized Wholesale Electricity Markets*.³ This credit rule addressed a number of areas, including shortening the settlement cycle, using unsecured credit, eliminating unsecured credit for Financial Transmission Rights, allowing market participants to offset market obligations and the effect of this feature in a bankruptcy, establishing minimum criteria for market participation, using material adverse change, and setting a minimum grace period to "cure" collateral calls. The ISO was compliant with some of the areas addressed in the order as a result of modifications the ISO made to the credit and billing policies over the last several years.

In 2011, the ISO focused on the following principal elements of the order:

- Capping unsecured credit to no more than \$50 million per market participant, and no more than \$50 million per corporate family
- Establishing minimum criteria for market participation
- Clarifying circumstances in which the ISO may invoke a "material adverse change"
- Setting a minimum grace period to "cure" collateral calls

With respect to the ability to offset market obligations, which has a delayed tentative implementation date of December 2012, the ISO fully expects to comply with the order within the established timeframes.

The ISO will continue to work closely with its participants to reduce default risk, including minimizing the settlement cycle time.

Various Market Services and Participation Data

The following table compares key settlement market information for the years ending 2010 and 2011 for the markets the ISO oversees.

³ FERC, *Credit Reforms in Organized Wholesale Electricity Markets* Docket No. RM10-13-000; Order No. 741 (October 27, 2010).

Table 2
Settlement Market Information

Key Settlement Market Data for the Year's Ending:^(a)	2011	2010
	\$ in Millions	
Energy Markets		
Day-Ahead Energy	\$6,455	\$7,095
Real-Time Energy	\$306	\$258
Total Energy Markets	\$6,761	\$7,353
Real-Time Load Obligation (MWh) ^(b)	136,252,110	140,087,869
Net Commitment-Period Compensation (NCPC)	\$74	\$95
Total NCPC	\$74	\$95
Reserve Markets		
Forward Reserve Markets, Net	\$18	\$113
Real-Time Reserve Markets	\$8	\$16
Total Reserve Markets	\$26	\$129
Regulation Market	\$13	\$14
Total Regulation Market	\$13	\$14
ICAP Transition Payments	\$0	\$790
FCM Payments ^(c)	\$1,345	\$856
Total ICAP Transition Payments	\$1,345	\$1,646
Financial Transmission Rights—Long Term Auction	\$16	\$19
Financial Transmission Rights—Monthly Auction	\$7	\$12
Total Auction Revenue Rights	\$23	\$31
Open- Access Transmission Tariff (OATT) Charges		
Regional Network Service/Through or Out	\$1,338	\$1,377
Black Start	\$10	\$10
Volt Ampere Reactive Capacity Cost	\$24	\$23
Total OATT Charges	\$1,372	\$1,410
Demand-Response Payments	\$7	\$8
Total Demand-Response Payments	\$7	\$8

(a) Data shown in the table reflect settled operational days January 1 through December 31 of the respective years.

(b) The real-time load obligation shown in the table reflects load at all pricing locations in New England, including exports at the external nodes.

(c) The FCM was implemented on June 1, 2010.

The ISO's aggregate customer base has decreased year to year, with 460 customers in 2011 down from 479 customers in 2010. The ISO's customers include generators, suppliers, publicly owned entities, transmission owners, demand-response resources, alternative resources, and end users. The cash cleared in 2011 was \$5.8 billion compared with \$6.8 billion in 2010, which is a decrease of approximately 15%. Energy market transactions that cleared through the ISO decreased approximately 8% from 2010 to 2011. In addition, the all-in energy market cost decreased 6%, and average natural gas prices decreased by approximately 5%. All these measures are key indicators of the cash that clears through the ISO.

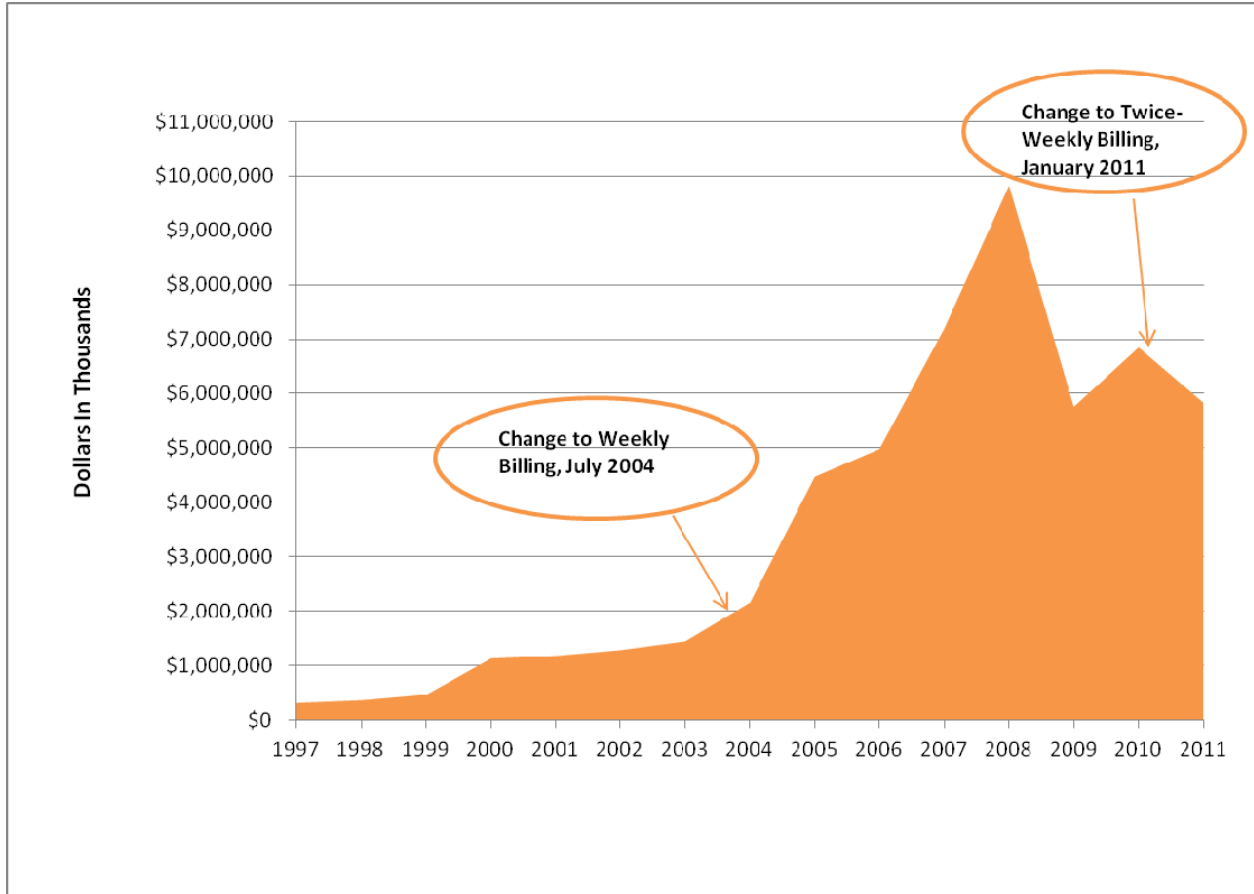


Figure 2: Annual historical market clearing activity.

Note: 1997 & 1998 are estimated data.

Management's Responsibility for Financial Reporting

The management of ISO New England Inc. (ISO) is responsible for the preparation, objectivity, and presentation of the following financial statements, as well as the integrity of these statements. These financial statements have been prepared to conform to accounting principles generally accepted in the United States of America and, where required, include amounts that represent management's best judgments and estimates. The ISO's management also is responsible for the preparation of other information in this annual report and for its accuracy and consistency with the financial statements.

To aid in carrying out this responsibility, we, along with all other members of management, maintain a system of internal accounting control modeled after the Committee of Sponsoring Organizations of the Treadway Commission, or the "COSO" framework. In the opinion of management, the overall system of internal accounting control provides reasonable assurance that the ISO's assets are safeguarded and that transactions are executed in accordance with the management's authorization and are properly recorded for the preparation of financial statements. In addition, management believes the overall system of internal accounting control provides reasonable assurance that, in the normal course of their duties, employees prevent or detect material errors or irregularities on a timely basis. Any system of internal accounting control, no matter how well designed, has inherent limitations, including the possibility that controls can be circumvented or overridden and misstatements due to error or fraud can occur and not be detected. Also, because of changing conditions, the effectiveness of internal control can vary over time. Accordingly, even an effective system of internal control will provide only reasonable assurance about the preparation and reporting of financial statements.

The system of internal accounting control is supported by written policies and guidelines, the selection and training of qualified employees, an organizational structure that provides an appropriate division of responsibility, and a program of internal auditing. The ISO's written policies include a Code of Conduct that states management's policy on conflict-of-interest and ethical conduct. All personnel annually confirm their compliance with the Code of Conduct.

Gordon van Welie
President and Chief Executive Officer

Robert C. Ludlow
Vice President, Chief Financial and
Compliance Officer



ISO New England Inc.

Financial Statements

For the Years Ended December 31, 2011 and 2010

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KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

Independent Auditors' Report

The Board of Directors
ISO New England Inc.:

We have audited the accompanying statements of financial position of ISO New England Inc. as of December 31, 2011 and 2010, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ISO New England Inc. as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

March 16, 2012

ISO New England Inc.
Statements of Financial Position
As of December 31, 2011 and 2010

	2011	2010
	(In thousands)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 42,390	\$ 156,358
Security deposits	332,763	331,579
Unbilled receivable, net	21,837	24,582
Prepaid expenses and other assets	1,107	855
Restricted cash on deposit	2,206	4,445
Noncurrent assets:		
Property and equipment in-service, net	64,491	72,252
Work in process	20,166	12,734
Deferred charges	75	90
Regulatory assets	51,315	21,861
	<u>51,315</u>	<u>21,861</u>
Total assets	<u>\$ 536,350</u>	<u>\$ 624,756</u>
Liabilities and Net Assets		
Current liabilities:		
Accounts payable:		
Settlement, net	\$ 39,899	\$ 146,418
Administration	6,589	5,926
Deposits payable	338,806	339,917
Interest payable	784	834
Accrued compensation	14,447	12,143
Deferred income – current	7,365	9,664
Restricted cash on deposit payable	2,206	4,445
Long-term debt - current portion	1,820	1,820
Long-term liabilities:		
Deferred income, net of current portion	-	5,873
Pension and post retirement benefit liability	50,399	21,861
Long-term debt	74,035	75,855
	<u>74,035</u>	<u>75,855</u>
Total liabilities	536,350	624,756
Unrestricted net assets	<u>-</u>	<u>-</u>
Total liabilities and net assets	<u>\$ 536,350</u>	<u>\$ 624,756</u>

The accompanying notes are an integral part of these financial statements.

ISO New England Inc.
Statements of Activities
For Years Ended December 31, 2011 and 2010

	2011	2010
	(In thousands)	
Changes in unrestricted net assets:		
Revenues:		
ISO tariff revenues	\$ 138,864	\$ 127,342
Grant revenues	309	245
Interest income	57	100
Fees and services	333	437
	<hr/>	<hr/>
Total unrestricted revenues	139,563	128,124
	<hr/>	<hr/>
Expenses:		
General and administrative:		
Salaries and benefits	78,558	70,828
Professional and consultants	12,250	13,093
Computer services	6,785	5,730
Depreciation and amortization expense	24,558	22,190
Communication expense	1,965	1,767
Insurance expense	1,693	1,691
Utilities	936	928
Board of directors	1,109	930
Building services	927	1,049
Northeast Power Coordinating Council dues	4,557	4,214
Interest expense	1,736	1,916
Other	4,489	3,788
	<hr/>	<hr/>
Total expenses	139,563	128,124
	<hr/>	<hr/>
Change in unrestricted net assets	-	-
Unrestricted net assets, beginning of year	-	-
	<hr/>	<hr/>
Unrestricted net assets, end of year	<u>\$ -</u>	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

ISO New England Inc.
Statements of Cash Flows
For Years Ended December 31, 2011 and 2010

	2011	2010
	(In thousands)	
Cash flows from operating activities:		
Increase in unrestricted net assets	\$ -	\$ -
Adjustments to reconcile change in unrestricted net assets to net cash provided by operating activities:		
Depreciation and amortization expense	24,558	22,190
Loss on disposal	456	-
Decrease(increase) in unbilled receivable, net	2,745	(4,210)
(Increase)decrease in prepaid expenses and other assets	(252)	588
(Increase)decrease in regulatory assets	(916)	4,161
(Decrease)increase in accounts payable:		
Settlement	(106,519)	7,329
Administration	1,200	345
Increase in accrued compensation	2,304	707
(Decrease)increase in interest payable	(50)	4
(Decrease)increase in deferred income	(8,172)	13,035
Net cash (used)provided by operating activities	<u>(84,646)</u>	<u>44,149</u>
Cash flows from investing activities:		
Capital expenditures	<u>(25,207)</u>	<u>(22,983)</u>
Net cash used in investing activities	<u>(25,207)</u>	<u>(22,983)</u>
Cash flows from financing activities:		
(Increase) in security deposits	(1,184)	(7,329)
Decrease(increase) in restricted cash on deposit	2,239	(2,647)
(Decrease)increase in restricted cash on deposit payable	(2,239)	2,647
(Decrease)increase in deposits payable	(1,111)	8,495
Repayment on long-term debt	(1,820)	(1,820)
Borrowing on revolving credit	6,500	16,000
Repayment on revolving credit	(6,500)	(21,000)
Net cash used in financing activities	<u>(4,115)</u>	<u>(5,654)</u>
Net (decrease)increase in cash and cash equivalents	(113,968)	15,512
Cash and cash equivalents, beginning of year	<u>156,358</u>	<u>140,846</u>
Cash and cash equivalents, end of year	<u>\$ 42,390</u>	<u>\$ 156,358</u>
Supplemental data:		
Amounts included in Accounts Payable – Administration related to work in process	<u>\$ 1,607</u>	<u>\$ 2,144</u>
Cash paid during the year for interest, net of interest capitalized	<u>\$ 1,746</u>	<u>\$ 1,919</u>
Non-cash activity - Change in pension liability is net of regulatory assets	<u>\$ 28,538</u>	<u>\$ 4,040</u>

The accompanying notes are an integral part of these financial statements.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

1. Summary of Significant Accounting Policies

Description of Business

ISO New England Inc. (the "Company" or "ISO") is the Regional Transmission Organization ("RTO") for New England in compliance with the requirements of the Federal Energy Regulatory Commission ("FERC").

Cash Equivalents

The Company considers cash on hand and short-term marketable securities with original maturities of three months or less to be cash equivalents. The cash equivalents at December 31, 2011 and 2010 were held in overnight repurchase agreements and also in direct and indirect obligations of the United States, with original maturities of three months or less.

Accounts Receivable and Accounts Payable

In the course of bulk power transactions administered by the Company on behalf of the Market Participants ("Participants"), amounts for energy purchased and sold among Participants become payable to and receivable from such Participants. The Company summarizes and prices the energy transactions twice each week and provides an invoice or remittance advice to each Participant that summarizes the amount either receivable from or payable to each Participant.

Accounts payable on the Statements of Financial Position are segregated between (i) the amounts owed for energy transactions and transmission, for which the ISO functions as paying agent, which are included in accounts payable as "settlement, net," and (ii) the administrative expenses incurred by the Company in the course of operations. The reference to "settlement, net" is used due to the nature of billing and payment for the amounts owed for energy transactions and transmission markets, and represents the customer's net amount due, less any amounts which may have been owed to them.

The net unbilled receivables, the majority of which have been determined as a result of the settlement process, include those amounts that will be billed and included in the invoice or remittance advice to Participants on subsequent invoices issued twice per week. The balance at the end of the year represents mainly ISO tariff revenues. The net payables and receivables for those energy transactions stated above are settled with the Participants in the same week.

Restricted Cash on Deposit

The balance of approximately \$2,206,000 and \$4,445,000 at December 31, 2011 and 2010, respectively, recorded as restricted cash on deposit, represents the Congestion Revenue Fund and Forward Capacity Market Forfeited Funds for both years. The balance has a corresponding liability on the Statements of Financial Position. The restricted cash on deposit at December 31, 2011 and 2010 was held in overnight repurchase agreements and also in direct and indirect obligations of the United States, with original maturities of three months or less.

ISO New England Inc.
Notes to Financial Statements for Years Ended December 31, 2011 and 2010

Property and Equipment in Service and Work in Process

Property and equipment is stated at cost, net of accumulated depreciation.

The Company capitalizes the interest and fees associated with borrowings that the Company has entered into for the acquisition of assets related to a project that has a material effect on the Company's financial position as required by the Accounting of Certain Types of Regulation Topic of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC").

In addition, the Company capitalizes internal software development costs as required by the Cost of Computer Service Software Development Topic of the FASB ASC.

Depreciation

Depreciation is generally computed using straight-line methods over an estimated useful life ranging from three years to twenty-five years (e.g., computer hardware, software and accessories – three to five years; software development costs – three to five years; vehicles – three to seven years; furniture and fixtures and machinery and equipment – seven years; building and leasehold/building improvements - one to twenty-five years or remaining life of the lease or building; and building – twenty-five years). Capitalized interest and fees are amortized over the same useful life of the asset to which it pertains, principally software development costs and building. No depreciation is recorded for assets classified as work in process until the assets are placed into service (Note 3).

Deferred Charges and Regulatory Assets and Liabilities

The Company as a regulated entity, in appropriate circumstances, establishes regulatory assets or liabilities, and thereby defers the income statement impact of certain charges or revenues because it is probable to be collected or refunded through future customer billings as required by the Accounting of Certain Types of Regulation Topic of the FASB ASC. The Company incurred costs with the purchase of land located at Sullivan Road. A portion of these costs, which were deferred, have been amortized, as they were included in the current year's filing pursuant to Section IV.A. of the Tariff (titled "Recovery of ISO Administrative Expenses"). The remaining cost, also deferred, will be collected in future filings.

The following table is a detail of the deferred charges and regulatory assets balances as presented in the Statements of Financial Position:

Deferred charges	2011	2010
Land located on Sullivan Road	\$ 75,000	\$ 90,000
	<u>\$ 75,000</u>	<u>\$ 90,000</u>
Regulatory assets, net of current portion	2011	2010
Actual 2011 under collection true-up	\$ 916,000	\$ -
Asset related to pension and postretirement benefit liabilities (Note 5)	\$ 50,399,000	\$21,861,000
	<u>\$ 51,315,000</u>	<u>\$21,861,000</u>

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

Income Taxes

The Company is an entity organized as a non-stock corporation under the General Corporation Law, as amended, of the State of Delaware. The Company has been recognized by The Internal Revenue Service as an organization described in Internal Revenue Code (IRC) 501(c)(3) and is generally exempt from income taxes under IRC Section 501(a).

The Company has determined prior to recording any benefit in the financial statements that it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authorities, as required by the Accounting for Uncertainty in Income Taxes Topic of the FASB ASC. A tax position is measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon settlement.

Security Deposits

The NEPOOL Participants are required to comply with the Financial Assurance Policy under ISO's Tariff. In certain cases, including non-investment grade rated Participants that meet certain criteria and all Participants participating in the Financial Transmission Rights market, the Company's Financial Assurance Policy requires these Participants to put in place alternate forms of financial assurance. There are several options allowed under the Company's Financial Assurance Policy for compliance, one of which is to post cash as collateral. The cash collateral deposits at December 31, 2011 and 2010 were approximately \$332,763,000 and \$331,579,000, respectively, and are recorded in deposits payable.

Revenue Recognition

The Company recovers its operating and debt service costs pursuant to Section IV of the ISO's Tariff, which provides for recovery of expenses through three schedules to Section IV.A. Scheduling, System Control and Dispatch Service (Schedule 1), Energy Administration Service (Schedule 2) and Reliability Administration Service (Schedule 3) recover related costs through a pre-approved rate applied to each month's activity. Schedules 1, 2, and 3 are subject to true-up through subsequent years' rates, and any over or under collection is recorded as deferred charges or deferred income and will be recovered under future filings to recover the ISO's expenses.

Government Grants

The Company recognizes government grants when there is reasonable assurance that the ISO will comply with the conditions attached to the grant arrangement and the grant will be received. Government grants are recognized in the Statement of Activities and in the Statement of Financial Position in the period in which the related costs are recognized that the government grant is intended to compensate.

Deferred Asset/Income

Deferred asset/income represents the amount of the ISO tariff revenues for Schedules 1, 2, and 3 that was over/under collected from 2009 through 2011. The over/under collection amount of the ISO Tariff will be returned to or collected from the Participants through the true-up mechanism provided for within Section IV.A. of the Tariff.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

Concentrations

The Company's top 10 Participants represented approximately 47% or \$60,661,000 and 45% or \$64,720,000 in tariff revenues for the years ended December 31, 2011 and 2010, respectively. The Company's top 10 Participants with accounts receivable balances represented approximately 46% or \$9,880,000 and 45% or \$10,789,000 as of December 31, 2011 and 2010, respectively.

Fair Values of Financial Instruments

The carrying amounts reported in the Statements of Financial Position for assets and liabilities approximate their fair values except as noted in (Note 4) – private placement debt arrangement.

The Fair Value Option for Financial Assets and Financial Liabilities Topic of the FASB ASC gives entities the option to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reporting earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The Company has elected to forgo the fair valuing of financial assets and financial liabilities for the year-ended December 31, 2011 and 2010.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Significant items subject to such estimates and assumptions include the useful lives of fixed assets, allowance for doubtful accounts, reserve for employee benefit obligation and other contingencies.

Liquidity Information

In order to provide information about liquidity, assets have been sequenced according to their nearness to conversion to cash, and liabilities have been sequenced according to the nearness of their resulting use of cash.

Revised Classification

The classification of certain amounts on the financial statements of the prior year have been revised to conform with the current year's basis of presentation.

Recently Issued Accounting Standards

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. The new standards do not extend the use of fair value but, rather, provide guidance about how fair value should be applied where it already is required or permitted under IFRS or U.S. GAAP. For U.S. GAAP, most of the changes are clarifications of existing guidance or wording changes to align with IFRS. A nonpublic entity is required to apply the ASU prospectively for annual periods beginning after December 15, 2011. The Company expects that the adoption of ASU 2011-04 in 2012 will not have a material impact on its consolidated financial statements.

ISO New England Inc.
Notes to Financial Statements for Years Ended December 31, 2011 and 2010

2. Commitments and Contingencies

Capital and Administrative Funding Tariff

The FERC accepted ISO's capital and administrative funding filings to recover administrative expenses for 2011 and 2010. These filings, made pursuant to Section IV of the Tariff, support the ISO's loan arrangements with various banks and note holders to fund the capital and working capital requirements of the Company.

Legal Proceedings

The Company is involved in various claims and legal proceedings of a nature considered normal to its business. The claims are in various stages and some may ultimately be brought to trial. While it is not feasible to predict or determine the outcome of any of these claims, it is the opinion of management that final outcome of these claims will not materially impact the Company's financial position.

3. Property and Equipment In-Service, Net and Work in Process

	December 31,	
	2011	2010
Computer hardware, software and accessories	\$ 184,178,000	\$ 172,674,000
Software development costs	55,049,000	50,380,000
Furniture and fixtures	2,884,000	2,875,000
Machinery and equipment	85,000	82,000
Building and leasehold/building improvements	45,021,000	44,646,000
Capitalized interest and fees	8,270,000	8,314,000
Vehicles	42,000	55,000
	<u>295,529,000</u>	<u>279,026,000</u>
Less: accumulated depreciation and amortization	(231,038,000)	(206,774,000)
Property and equipment in-service, net	<u>\$ 64,491,000</u>	<u>\$ 72,252,000</u>
Work in process ("WIP")	<u>\$ 20,166,000</u>	<u>\$ 12,734,000</u>

Costs represented in WIP include Standard Market Design (SMD) Software Upgrade Phase III, Synchrophasor Infrastructure and Data Utilization (SIDU), Generation Control Applications (GCA), Outage Coordination Economic Analysis Phase II, Energy Management System Upgrade and Enhancement, Information Delivery Web Enhancements and NX9/NX12D Data Integration and Automation which all began in 2010. Additionally, a number of new projects began in 2011, such as Market Mitigation Automation, 2011 Issue Resolution Phase II, Wind Integration, Price Response Demand, Q12012, Balance of Planning Period (BOPP) -Financial Transmission Right Enhancements, Forward Capacity Market Reform and various other market enhancement projects that have not been placed in service as of December 31, 2011.

As required by the Accounting of Certain Types of Regulation Topic of the FASB ASC, the interest capitalized from the revolving credit arrangement, private placement and tax-exempt debt bond financing and recorded on the Statements of Financial Position for the years ended December 31, 2011 and 2010 was \$510,000 and \$494,000, respectively. The amount of the interest capitalized and recorded on the Statements of Financial Position that was included in WIP for years ended December 31, 2011 and 2010 was \$494,000 and \$249,000, respectively.

Depreciation and amortization expense was \$24,558,000 and \$22,190,000 for the years ended December 31, 2011 and 2010, respectively.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

4. Credit Facilities

Revolving Credit Arrangement

In June 2009, the Company entered into a \$15,000,000 revolving credit arrangement that expires on July 1, 2012, and any outstanding balance must be paid by this date. In April 2009, the Company filed a Section 204 filing with the FERC to issue this new debt for which the filing was approved in May 2009. In June 2011, the Company filed a Section 204 filing to continue the authorization to draw down on the existing revolving credit arrangement as required by the April 2009 FERC order. This filing was approved by the FERC in July 2011. In addition, the Company renegotiated certain terms of the credit arrangement effective August 23, 2011, none of which involved a change in the expiration date of the debt. From the period of June 2009 through August 22, 2011, interest accrued on the revolving credit at either Base Rate or a LIBOR of which the Company had the option of selecting the 30, 60, 90, or 180-day rate, plus a 1.50% spread. Effective August 23, 2011, the same interest rate options apply, with the LIBOR spread equal to 1.00%, a reduction from the previous 1.50%. Interest is paid at the earlier of the selected LIBOR term or 30 days. The Company is charged an annual fee of .15% on the entire line of credit.

The outstanding balance for each of the years ended December 31, 2011 and 2010 was \$0. For the years ended December 31, 2011 and 2010, the weighted average interest rate was approximately 3.00% and 2.21% respectively.

The Company entered into a \$4,000,000 revolving credit arrangement on June 30, 2009 that expires on July 1, 2012 and any unpaid balances must be paid as of this date. In April 2009, the Company filed a Section 204 filing with the FERC to issue this new debt for which the filing was approved in May 2009. In June 2011, the Company filed a Section 204 filing to continue the authorization to draw down on the existing revolving credit arrangement as required by the April 2009 FERC order. This filing was approved by the FERC in July 2011. In addition, the Company renegotiated certain terms of the credit arrangement effective August 23, 2011, none of which involved a change in the expiration date of the debt. This arrangement continues to serve as a line of credit to cover any potential payment defaults by a Participant. From the period of June 2009 through August 22, 2011, interest accrued on the revolving credit at either Base Rate or a LIBOR of which the Company had the option of selecting the 30, 60, 90, or 180-day rate, plus a 1.50% spread. Effective August 23, 2011, the same interest rate options apply, with the LIBOR spread equal to 1.00%, a reduction from the previous 1.50%. Interest is paid at the earlier of the selected LIBOR term or 30 days and the Company is charged an annual fee of .15% on the entire line of credit.

The outstanding balance for each of the years ended December 31, 2011 and 2010 was \$0.

The Company incurred \$73,000 in debt issuance costs as a result of the refinancing revolving credit arrangement in 2009. These costs have been capitalized and were being amortized on a straight-line basis over the remaining life of the arrangement. Upon execution of the amendment, the unamortized costs were written off to gains/losses, which are included in other expense on the Statements of Activities, in the amount of \$22,000. The Company incurred \$20,000 in debt issuance costs as a result of the amendment. These costs have been capitalized and are being amortized on a straight-line basis over the remaining life of the arrangement. Total amortization expense was approximately \$17,000 and \$24,000 for the years ended December 31, 2011 and 2010, respectively.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

Private Placement Debt Arrangement

In September 2004, the Company entered into a \$39,000,000 private placement loan, which is made up of ten year 5.60% senior notes. Payment is due in full on September 2, 2014 with no mandatory prepayments and interest accrued and paid semi-annually. This loan is included in long-term debt on the Statements of Financial Position. The fair market value of the private placement loan at December 31, 2011 was estimated at \$42,865,000. The value is based on the current treasury rates which was .36% for December 31, 2011.

In 2004, the Company incurred \$202,000 in debt issuance costs. These costs have been capitalized and are being amortized on a straight-line basis over the term of the loan. Total amortization expense for the years ended December 31, 2011 and 2010 was approximately \$20,000.

Tax-Exempt Bond Financing

In February of 2005, the Company entered into tax exempt financing of \$45,500,000 in the form of Multi-Mode Variable Rate Civic Facility Revenue Bonds ("Bonds"), which were issued by the Massachusetts Development Finance Agency. The proceeds of the Bonds were loaned to the Company to assist in financing and refinancing a project located at the Main Control Center. Principal payments of \$455,000, paid quarterly, began in May 2007 with the final repayment due on February 1, 2032. The tax exempt financing is backed by a letter of credit ("LOC") that the Company entered into in February of 2005, which was replaced in August 2009 with an alternative credit facility not to exceed \$41,609,688 that expires on August 31, 2012. On August 23, 2011, the bank and the Company amended the expiration date of the LOC to be August 31, 2015. Interest accrues quarterly on the \$45,500,000 tax exempt bonds, at a weekly variable rate based upon the Securities Industry and Financial Markets Association "SIFMA" Swap Index with a weighted average of 0.18% and 0.27% for the years ended December 31, 2011 and 2010, respectively. For the years ended December 31, 2011 and 2010, the weighted average floating interest rate on the Bonds was approximately 0.14% and 0.23%, respectively. The Company was charged an annual fee of 1.50% paid quarterly based on the maximum amount available to be drawn under the letter of credit including principal and interest commitments. Effective August 23, 2011 the annual fee charged to the Company was reduced to 0.75% and is calculated on the same basis as previous to the fee amendment.

The Company incurred \$238,000 in debt issuance costs as a result of the refinancing. These costs have been capitalized and were being amortized on a straight-line basis over the remaining life of the Bonds. Upon execution of the LOC amendment, the remaining costs were written off to gains/losses, which are included in other expense on the Statements of Activities, in the amount of \$216,000. Total amortization expense was approximately \$21,000 and \$11,000 for the years ended December 31, 2011 and 2010, respectively.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

The total long-term debt at December 31, 2011 and 2010 was \$75,855,000 and \$77,675,000, respectively. Principal payments on the private placement debt and tax-exempt bonds are due annually as follows:

2012	\$ 1,820,000
2013	1,820,000
2014	40,820,000
2015	1,820,000
2016	1,820,000
Thereafter	27,755,000
	<u>\$ 75,855,000</u>

Interest incurred on the revolving credit arrangement, private placement debt, and tax-exempt bonds for the years ended December 31, 2011 and 2010 was approximately \$2,246,000 and \$2,406,000, respectively.

5. Pension and Other Employee Benefits

The Company sponsors defined benefit pension and postretirement plans (the “plans”), which cover substantially all union and nonunion employees and provide retirement income, medical, dental and life insurance benefits.

The Company sponsors two defined benefit pension plans (one for union and the other for nonunion employees), each of which is funded solely by Company contributions. Benefits are determined based on years of service and average compensation.

The Company sponsors a postretirement benefit plan other than pension that provides medical, dental and life insurance benefits for eligible employees and their beneficiaries. The medical benefits are contributory with participants’ contributions adjusted annually, and participants are responsible for deductible and coinsurance amounts. Dental benefits are non-contributory but participants are responsible for deductible and coinsurance amounts. The life insurance benefits are noncontributory. The measurement date used to determine pension and other postretirement benefit obligations for the pension plans and the postretirement benefit plan is December 31.

The Company accounts for the recording of an asset if the plan is over funded or a liability if the plan is underfunded, rather than disclosing the funded status in a note to the financial statements as required in the Accounting for Defined Benefit Pension and Other Postretirement Plans Topic of the FASB ASC. The amount recorded is the difference between the fair value of plan assets and the benefit obligation. Additionally, the Company discloses net periodic benefit cost for the Defined Benefit Pension and Other Postretirement Benefit Plan Assets for each annual period for which a statement of income is presented as required by the Employers’ Disclosures about Postretirement Benefit Plan Assets Topic of the FASB ASC.

In 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act (collectively, the Health Care Acts) were signed into law by President Obama. The Health Care Acts include several provisions that may affect a company’s postretirement benefit plans, including imposing an excise tax on high cost coverage, eliminating lifetime and annual coverage limits, reducing subsidies to Medicare Advantage plans, and extending coverage for adult children until age 26. The Company has evaluated the effects of the Health Care Acts and concluded that the provision that affects its postretirement benefit plan is the excise taxes on high cost coverage or “Cadillac plans”. The effect of the provision, estimated to be \$12,000, has been included in the measurement of the postretirement benefit obligation as of December 31, 2011. The Company is accounting for the effect of the Health Care Acts as an actuarial loss. The Company does not provide benefits that are actuarially equivalent to the Medicare prescription drug benefit in its postretirement benefit plan.

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Notes to Financial Statements for Years Ended December 31, 2011 and 2010

The following table sets forth the plans' benefit obligations, fair value of the plans' assets, and the plans' funded status:

	Pension Benefits		Other Postretirement Benefits	
	Years Ended December 31,		Years Ended December 31,	
	2011	2010	2011	2010
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 81,887,000	\$ 66,945,000	\$ 12,652,000	\$ 9,836,000
Service cost	4,993,000	4,048,000	1,045,000	946,000
Interest cost	4,530,000	3,986,000	596,000	589,000
Benefits paid	(1,897,000)	(1,649,000)	(403,000)	(324,000)
Plan participants' contributions	-	-	65,000	58,000
Actuarial loss	23,623,000	8,557,000	737,000	1,547,000
Benefit obligation at end of year	<u>113,136,000</u>	<u>81,887,000</u>	<u>14,692,000</u>	<u>12,652,000</u>
Change in plan assets:				
Fair value of plan assets at beginning of year	63,248,000	51,497,000	9,430,000	7,463,000
Actual return on plan assets	454,000	8,639,000	29,000	1,184,000
Employer contributions	5,816,000	4,761,000	688,000	1,049,000
Plan participants' contributions	-	-	65,000	58,000
Benefits paid	(1,897,000)	(1,649,000)	(403,000)	(324,000)
Fair value of plan assets at end of year	<u>67,621,000</u>	<u>63,248,000</u>	<u>9,809,000</u>	<u>9,430,000</u>
Funded status at end of the year	(45,515,000)	(18,639,000)	(4,883,000)	(3,222,000)
Transition obligation	-	-	-	-
Net actuarial (gain) loss	-	-	-	-
Prior service cost	-	-	-	-
Net amount recognized as non-current liabilities	<u>\$ (45,515,000)</u>	<u>\$ (18,639,000)</u>	<u>\$ (4,883,000)</u>	<u>\$ (3,222,000)</u>

The Company has determined that the pension liability is probable of recovery through Section IV.A. of the Tariff and has recorded a regulatory asset as of December 31, 2011 and 2010 in the accompanying Statements of Financial Position.

	Pension Benefits		Other Postretirement Benefits	
	Years ended December 31,		Years ended December 31,	
	2011	2010	2011	2010
Components of net periodic benefit cost:				
Service cost	\$ 4,993,000	\$ 4,048,000	\$ 1,045,000	\$ 946,000
Interest cost	4,530,000	3,986,000	596,000	589,000
Expected return on plan assets	(4,878,000)	(3,976,000)	(723,000)	(582,000)
Amortization of transition obligation	125,000	125,000	56,000	56,000
Amortization of net actuarial loss	761,000	576,000	126,000	223,000
Amortization of unrecognized prior service cost	2,000	2,000	(129,000)	(129,000)
Net periodic benefit cost	<u>\$ 5,533,000</u>	<u>\$ 4,761,000</u>	<u>\$ 971,000</u>	<u>\$ 1,103,000</u>

ISO New England Inc.
Notes to Financial Statements for Years Ended December 31, 2011 and 2010

	Pension Benefits		Other Postretirement	
	Years ended December 31, 2011	2010	Years ended December 31, 2011	2010
Prepaid benefit cost at beginning of year	\$ -	\$ -	\$ -	\$ 54,000
Employer contributions	5,815,000	4,761,000	688,000	1,049,000
Net periodic benefit cost	<u>(5,532,000)</u>	<u>(4,761,000)</u>	<u>(971,000)</u>	<u>(1,103,000)</u>
Prepaid benefit cost at end of year	<u>\$ 283,000</u>	<u>\$ -</u>	<u>\$ (283,000)</u>	<u>\$ -</u>

The following table sets forth the amount expected to be amortized into net periodic benefit cost over the next fiscal year ending December 31, 2012:

	<u>Pension Benefits</u>	<u>Other Benefits</u>
Expected amortization of transition obligation	\$ 125,000	\$ 56,000
Expected amortization of net actuarial loss	2,250,000	295,000
Expected amortization of prior service cost	2,000	(129,000)

The primary economic assumptions used to value these liabilities are summarized in the following chart. These assumptions are selected as the measurement data based on prevailing economic conditions.

Weighted-average assumptions used to determine net periodic benefit cost for the following years ended:

	Pension Benefits		Other Benefits	
	<u>12/31/2011</u>	<u>12/31/2010</u>	<u>12/31/2011</u>	<u>12/31/2010</u>
Discount rate	5.51%	5.98%	5.14%	5.71%
Expected long-term rate of return on plan assets	7.50%	7.50%	7.50%	7.50%
Rate of compensation increase	3.50%	3.50%	3.50%	3.50%
Health Care cost trend rates - initial	-	-	9.00%	8.50%
Health Care cost trend rates - ultimate	-	-	5.00%	5.00%
Ultimate year	-	-	2020	2018

Weighted-average assumptions used to determine benefit obligation for the following years ended:

	Pension Benefits		Other Benefits	
	<u>12/31/2011</u>	<u>12/31/2010</u>	<u>12/31/2011</u>	<u>12/31/2010</u>
Discount rate	4.38%	5.51%	4.12%	5.14%
Rate of compensation increase	3.75%	3.50%	3.75%	3.50%

A one percentage point change in the assumed health care cost trend rates would either increase the Accumulated Post Retirement Benefit (“APBO”) as of December 31, 2011 by approximately \$622,000 or decrease the APBO by approximately \$562,000. Additionally, a one percentage point change in the assumed health care cost trend rates would increase or decrease the net post retirement cost as of December 31, 2011 by approximately \$107,000 and \$95,000, respectively.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

The methodology for selecting the discount rate for the plan is to match the plan's expected benefit payments to that of a yield curve that provides the equivalent yield on zero-coupon corporate bonds and estimate a single interest rate that produces a present value equal to the present value produced by the full yield curve as of the annual measurement date, subject to change each year.

ISO's pension plan and postretirement benefit plan weighted-average asset allocations and expected returns by asset category are as follows:

Pension and Postretirement Plan Assets

	Target Allocation 2012	Percentage of Plan Assets at December 31		Weighted Average Expected Long-Term Rate of Return - 2011
		2011	2010	
Equity Securities	59%	59%	59%	5.25%
Debt Securities	36%	36%	36%	1.84%
Other	5%	5%	5%	0.48%
Total	100%	100%	100%	7.57%

The forward-looking estimates of total return are generated through combined assessment of current valuation measures, income, economic growth and inflation forecasts, historical risk premiums, and universal capital market assumptions. The long-term bond forecast is derived from the expected long-term return of a portfolio of corporate, government and high yield debt instruments. The equity forecasts are based on the long-term real returns of a portfolio of US large cap, US small cap, international developed markets and emerging markets equity securities.

The plan's investment portfolio is to be invested to provide benefits for qualified employees of ISO New England Inc. Investments are to be compatible with the liquidity requirements determined by the plan's actuary. An optimal target allocation of 60/40 between equities and fixed income investments is to be kept with an allowance of fifteen percent (15%) over/under deviation from the optimal allocation target.

ISO New England Inc.
Notes to Financial Statements for Years Ended December 31, 2011 and 2010

The fair values of the pension plan assets at December 31, 2011 and 2010 by asset category are as follows:

	Market Value at 12/31/11	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Long-term investment strategies:				
Fixed income:				
U.S. Treasury inflation-protected	\$ 3,608,000	\$ -	\$ 3,608,000	\$ -
U.S. and global core fixed income funds	19,543,000	-	19,543,000	-
U.S. High Yield Bond Funds	2,045,000	2,045,000	-	-
Total	<u>25,196,000</u>	<u>2,045,000</u>	<u>23,151,000</u>	<u>-</u>
Domestic equities:				
Traditional equity index funds	25,823,000	-	25,823,000	-
Total	<u>25,823,000</u>	<u>-</u>	<u>25,823,000</u>	<u>-</u>
Global (ex-U.S.) equities:				
Developed markets	7,366,000	7,366,000	-	-
Emerging markets value (actively managed)	2,145,000	2,145,000	-	-
Total	<u>9,511,000</u>	<u>9,511,000</u>	<u>-</u>	<u>-</u>
Real assets:				
U.S. real estate investment trust funds	3,315,000	-	3,315,000	-
Commodities - oil and energy	3,169,000	-	3,169,000	-
Total	<u>6,484,000</u>	<u>-</u>	<u>6,484,000</u>	<u>-</u>
Cash and cash equivalents	606,000	606,000	-	-
Total long-term investments	<u>\$ 67,620,000</u>	<u>\$ 12,162,000</u>	<u>\$ 55,458,000</u>	<u>\$ -</u>

The Company's pension plan investments are composed of mutual funds and commingled trust funds that are redeemable at NAV on a daily basis. Redemption of such investments generally requires 1 to 2 days written notice prior to the redemption date.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

	<u>Market Value at 12/31/10</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Long-term investment strategies:				
Fixed income:				
U.S. Treasury inflation-protected	\$ 2,944,000	\$ -	\$ 2,944,000	\$ -
U.S. and global core fixed income funds	16,586,000	-	16,586,000	-
U.S. High Yield Bond Funds	1,952,000	1,952,000	-	-
Total	<u>21,482,000</u>	<u>1,952,000</u>	<u>19,530,000</u>	<u>-</u>
Domestic equities:				
Traditional equity index funds	24,526,000	-	24,526,000	-
Total	<u>24,526,000</u>	<u>-</u>	<u>24,526,000</u>	<u>-</u>
Global (ex-U.S.) equities:				
Developed markets	7,628,000	7,628,000	-	-
Emerging markets value (actively managed)	2,320,000	2,320,000	-	-
Total	<u>9,948,000</u>	<u>9,948,000</u>	<u>-</u>	<u>-</u>
Real assets:				
U.S. real estate investment trust funds	3,518,000	-	3,518,000	-
Commodities - oil and energy	3,308,000	-	3,308,000	-
Total	<u>6,826,000</u>	<u>-</u>	<u>6,826,000</u>	<u>-</u>
Cash and cash equivalents	466,000	466,000	-	-
Total long-term investments	<u>\$ 63,248,000</u>	<u>\$ 12,366,000</u>	<u>\$ 50,882,000</u>	<u>\$ -</u>

The Company's pension plan investments are composed of mutual funds and commingled trust funds that are redeemable at NAV on a daily basis. Redemption of such investments generally requires 1 to 2 days written notice prior to the redemption date.

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Notes to Financial Statements for Years Ended December 31, 2011 and 2010

The fair values of the other postretirement benefit plan assets at December 31, 2011 and 2010 by asset category are as follows:

	Market Value at 12/31/11	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Long-term investment strategies:				
Fixed income:				
U.S. Treasury inflation-protected	\$ 545,000	\$ -	\$ 545,000	\$ -
U.S. and global core fixed income funds	2,867,000	-	2,867,000	-
U.S. High Yield Bond Funds	290,000	290,000	-	-
Total	<u>3,702,000</u>	<u>290,000</u>	<u>3,412,000</u>	<u>-</u>
Domestic equities:				
Traditional equity index funds	3,738,000	-	3,738,000	-
Total	<u>3,738,000</u>	<u>-</u>	<u>3,738,000</u>	<u>-</u>
Global (ex-U.S.) equities:				
Developed markets	1,130,000	1,130,000	-	-
Emerging markets value (actively managed)	278,000	278,000	-	-
Total	<u>1,408,000</u>	<u>1,408,000</u>	<u>-</u>	<u>-</u>
Real assets:				
U.S. real estate investment trust funds	504,000	-	504,000	-
Commodities - oil and energy	447,000	-	447,000	-
Total	<u>951,000</u>	<u>-</u>	<u>951,000</u>	<u>-</u>
Cash and cash equivalents	10,000	10,000	-	-
Total long-term investments	<u>\$ 9,809,000</u>	<u>\$ 1,708,000</u>	<u>\$ 8,101,000</u>	<u>\$ -</u>

The Company's other postretirement benefit plan investments are composed of mutual funds and commingled trust funds that are redeemable at NAV on a daily basis. Redemption of such investments generally requires 1 to 2 days written notice prior to the redemption date.

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Notes to Financial Statements for Years Ended December 31, 2011 and 2010

	Market Value at 12/31/10	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Long-term investment strategies:				
Fixed income:				
U.S. Treasury inflation-protected	\$ 438,000	\$ -	\$ 438,000	\$ -
U.S. and global core fixed income funds	2,489,000	-	2,489,000	-
U.S. High Yield Bond Funds	292,000	292,000	-	-
Total	<u>3,219,000</u>	<u>292,000</u>	<u>2,927,000</u>	<u>-</u>
Domestic equities:				
Traditional equity index funds	3,660,000	-	3,660,000	-
Total	<u>3,660,000</u>	<u>-</u>	<u>3,660,000</u>	<u>-</u>
Global (ex-U.S.) equities:				
Developed markets	1,078,000	1,078,000	-	-
Emerging markets value (actively managed)	361,000	361,000	-	-
Total	<u>1,439,000</u>	<u>1,439,000</u>	<u>-</u>	<u>-</u>
Real assets:				
U.S. real estate investment trust funds	524,000	-	524,000	-
Commodities - oil and energy	495,000	-	495,000	-
Total	<u>1,019,000</u>	<u>-</u>	<u>1,019,000</u>	<u>-</u>
Cash and cash equivalents	93,000	93,000	-	-
Total long-term investments	<u>\$ 9,430,000</u>	<u>\$ 1,824,000</u>	<u>\$ 7,606,000</u>	<u>\$ -</u>

The Company's other postretirement benefit plan investments are composed of mutual funds and commingled trust funds that are redeemable at NAV on a daily basis. Redemption of such investments generally requires 1 to 2 days written notice prior to the redemption date.

ISO New England Inc.
Notes to Financial Statements for Years Ended December 31, 2011 and 2010

The Company expects to contribute \$8,901,000 to its pension plans and \$1,350,000 to its postretirement benefit plan in 2012.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits	Other Benefits
2012	\$ 2,175,000	\$ 535,000
2013	2,438,000	582,000
2014	2,728,000	694,000
2015	3,157,000	801,000
2016	3,590,000	809,000
Years 2017-2021	25,856,000	5,396,000
Total	<u>\$ 39,944,000</u>	<u>\$ 8,817,000</u>

6. 401(k) Savings Plan

The Company has a 401(k) Retirement and Savings Plan open to substantially all employees. This savings plan provides for employee contributions up to specified limits. The Company matches employee contributions up to 3% of eligible compensation and provides a 50% match on the next 2% of eligible compensation. The matching contributions for the Company were \$2,097,000 and \$1,886,000 for the years ended December 31, 2011 and 2010, respectively.

7. Deferred Income

At December 31, 2011 and 2010, the Company recorded the following amounts as regulatory liabilities:

	2011	2010
Actual 2009 over collection	\$ -	\$ 2,502,000
Projected 2010 over collection	-	7,162,000
Additional actual 2010 over collection	5,873,000	5,873,000
Projected 2011 over collection	1,492,000	-
Total	<u>7,365,000</u>	<u>15,537,000</u>
Less current portion	<u>(7,365,000)</u>	<u>(9,664,000)</u>
Long-term portion	<u>\$ -</u>	<u>\$ 5,873,000</u>

The Company recovers its operating expenses through a filed rate assessed to Participants via the Tariff. To the extent that transactional volumes billed under Rate Schedules 1, 2 and 3 of Section IV.A. exceed the amount expected when the rate schedule charges are established, the Company reflects a regulatory liability for the over collection amounts.

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Notes to Financial Statements for Years Ended December 31, 2011 and 2010

8. Leases

The following is a schedule by year of future minimum rental payments for all noncancelable-operating leases:

2012	\$	48,000
2013		48,000
2014		<u>28,000</u>
Total minimum lease payments	\$	<u>124,000</u>

The Company currently houses its back-up facilities at a separate location on a net lease basis, which includes the cost of utilities with three year renewal periods through 2017. For fiscal years 2011 and 2010, rental payments for operating leases were \$47,000 and \$46,000, respectively.

9. Smart Grid Program

On October 27, 2009, the U.S. Department of Energy (“DOE”) announced that the Company will receive \$7.9 million in federal stimulus funding to install about 30 new Phasor Measurement Units with multiple synchrophasors at various transmission locations in New England to communicate to 8 Phasor Data Concentrators executing OpenPDC architecture. This project will provide the Smart Grid technology platform upon which advanced analysis and visualization tools can be deployed to enhance situational awareness. With this project, the entire New England region is expected to realize reliability benefits via increased response time to real time system events and wide area monitoring.

The agreement with the DOE was executed on June 3, 2010 and became effective on July 1, 2010. The Company is eligible to receive reimbursement of \$7,900,000 or up to 50 percent of the total project costs, which were initially estimated at \$18,100,000. The project cost may total less than the \$18,100,000 based on revision to the budget; however, the scope of the project will remain the same. Total project costs incurred through December 31, 2011 were \$900,000 and \$3,900,000 of operating and capital expenses, respectively, and \$400,000 of subrecipient expenses. The Company has submitted requests for reimbursement of \$2,400,000 and has received \$2,200,000 to date. The 50% of costs not reimbursed by the DOE will be incurred by the Company and the transmission owners.

ISO New England Inc.

Notes to Financial Statements for Years Ended December 31, 2011 and 2010

10. Eastern Interconnection Planning Collaborative

On December 18, 2009, the DOE announced that the Eastern Interconnection Planning Collaborative (“EIPC”) will receive \$16,000,000 in federal stimulus funding to perform interconnection-wide transmission analysis. The project cost may total less than the \$16,000,000 however the scope of the project will remain the same. EIPC members have worked together to “roll-up” existing regional plans to craft a model of the Eastern Interconnection that will serve as the platform for the analysis. Under the guidance of a multi-constituency stakeholder steering committee established as a requirement of the DOE project, EIPC will perform economic analysis on eight stakeholder selected scenarios as part of the first phase of the project and then perform transmission expansion and reliability analysis and costing on three stakeholder selected scenarios as part of the second and final phase of the project. The first phase of the project completed in late 2011 with the second phase slated for completion late in 2012.

Although all twenty-six EIPC members will support the DOE project work, eight members will serve as Principal Investigators under the project and are the only EIPC members eligible to receive reimbursements from the funding under a contractual arrangement established between the Principal Investigators and the DOE. The ISO is one of the eight Principal Investigators and is eligible to receive up to \$755,000 in reimbursements for work performed in support of the project. The Company has submitted requests for reimbursement of \$108,000 and has received \$80,000 to date.

11. Subsequent Events

Management has evaluated subsequent events through March 16, 2012 which is the date that the financial statements were available to be issued.