

NYISO 2007 BUDGET OVERVIEW

Prepared for:

Budget, Standards & Performance Subcommittee

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NYISO 2007 BUDGET OVERVIEW:

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BUDGET SUMMARY INFORMATION

NYISO 2007 BUDGET OVERVIEW: Highlights

THEMES:

- *Within Budget Target:* 2007 Rate Schedule 1 charge of \$0.821/MWH is within budget target established in 2003;
- *RTO Cost Consciousness:* Controllable costs within NYISO's 2007 budget reflect a ~\$3.7M decrease from 2006;
- *Sensitivity to Debt Levels:* NYISO is continuing to reduce levels of outstanding debt (reducing annual financings, shortening length of repayments, and utilizing available funds to repay outstanding debt);
- *Overall Focus:* 2007 will continue NYISO's focus on Excellence in Execution initiatives and software development projects launched in prior years (see details below)

MAIN 2007 PRIORITIES:

1. Complete migration to new headquarters facility (expected completion is Q1 2007)
2. Institutionalize process & control improvements and initiatives, including Lean Six Sigma quality program
3. Continue process to replace the Settlements System (phased implementation scheduled for completion in 2009)
4. Continue process to replace Market Information System (phased implementation scheduled for completion in 2009)
5. Complete Enhanced Price Validation project
6. Continue technology infrastructure initiatives to optimize and consolidate computer platforms allowing reduction of required footprint and associated costs
7. Implement proposed shortened billing timeframes (assuming approvals received in late 2006)
8. Implement appropriate metering strategy as relates to settlement cycle intervals
9. Continue TCC and UCAP automation / enhancement initiatives
10. Continue automation efforts for manual billing processes

Net of new building costs in 2006, spending decrease of ~\$3.7M from prior year

NYISO 2007 BUDGET OVERVIEW: Summary Budget

<u>Cost Category</u> <i>(\$ in millions, excluding RS#1/MWH)</i>	<u>2007 Draft</u>	<u>2006 Budget</u>	<u>2005 Actuals</u>	<u>2004 Actuals</u>	<u>2003 Actuals</u>
Current Year Needs (excl. FERC Fees)	\$117.9	\$130.1	\$127.4	\$132.1	\$139.8
Plus: Debt Service from Prior Year Financings	35.4	31.2	25.7	29.0	15.9
Cash Budget	\$153.3	\$161.3	\$153.1	\$161.1	\$155.7
Less: Miscellaneous Revenues	(2.3)	(2.5)	(4.3)	(\$1.1)	(\$1.0)
Less: Prior Year Underrun/Overcollection applied	(5.0)	(12.5)	-	-	-
Less: Net Proceeds on Current Year Financings	(14.5)	(23.1)	(31.2)	(\$41.5)	(\$45.8)
Net Budget Needs – in \$\$	\$131.5	\$123.2	\$117.6	\$118.5	\$108.9
FERC Fees – in \$\$	8.2	9.9	8.9	5.3	7.9
Total RS#1 Rev. Requirement – in \$\$	\$139.7	\$133.1	\$126.5	\$123.8	\$116.8
Net Budget Needs – in \$/MWH	\$0.773	\$0.742	\$0.745	\$0.736	\$0.686
FERC Fees – in \$/MWH	\$0.048	\$0.060	\$0.043	\$0.033	\$0.050
Total RS#1 Rev. Requirement - \$/MWH	\$0.821	\$0.802	\$0.788	\$0.769	\$0.736
RS#1 Charge/MWH: Purchasers @ 80% (85% pre-2005)	\$0.657	\$0.642	\$0.630	\$0.654	\$0.626
RS#1 Charge/MWH: Sellers @ 20% (15% pre-2005)	\$0.164	\$0.160	\$0.158	\$0.115	\$0.110

For Discussion Only

BUDGET DETAIL INFORMATION

NYISO 2007 BUDGET OVERVIEW:

Detail Budget by Cost Category

(\$ in millions, except RS#1/MWH)	<u>2007 Draft</u>	<u>2006 Budget</u>	<u>2005 Actuals</u>	<u>2004 Actuals</u>	<u>2003 Actuals</u>	<u>Details Page Ref.</u>
Capital	\$4.4	\$21.0	\$22.7	\$12.1	\$30.3	Page 10
Salaries & Benefits	50.6	49.3	45.8	42.1	37.6	Page 11
Professional Fees (including Legal)	32.2	29.2	30.0	49.2	49.2	Pages 12-13
Building Services	4.0	4.4	4.9	4.2	3.3	Page 14
Computer Services	13.0	10.5	9.8	8.7	4.2	Page 15
Insurance	3.7	4.6	4.3	6.4	6.7	Page 16
Telecommunications	5.0	5.1	4.6	4.5	3.1	
Other Expenses (BOD, Travel/Training, NPCC Fees)	5.0	6.0	5.3	4.9	5.4	Page 17
Current Year Needs (excl. FERC Fees)	\$117.9	\$130.1	\$127.4	\$132.1	\$139.8	
Debt Service	35.4	31.2	25.7	29.0	15.9	Pages 18-19
Cash Budget	\$153.3	\$161.3	\$153.1	\$161.1	\$155.7	
Less: Miscellaneous Revenues	(2.3)	(2.5)	(4.3)	(1.1)	(1.0)	
Less: Proceeds from Current Year Budget Debt/Carryovers	(20.0)	(28.0)	(18.0)	(42.0)	(47.0)	Pages 18-19
Less: Proceeds from Mortgage/Renovations Debt	-	(8.5)	(16.1)	-	-	
Add: Interest on Current Year Budget Debt	0.5	0.5	0.4	0.5	1.2	Pages 18-19
Add: Principal & Interest on Mortgage/Renovations Debt	-	0.4	2.5	-	-	
Net Budget Needs	\$131.5	\$123.2	\$117.6	\$118.5	\$108.9	
FERC Fees	8.2	9.9	8.9	5.3	7.9	Page 20
Rate Schedule #1 Revenue Requirement in \$\$	\$139.7	\$133.1	\$126.5	\$123.8	\$116.8	
Budgeted MWH Hours (budget)	170.1	166.0	163.7	161.0	158.8	
Rate Schedule #1 Revenue Requirement in \$/MWH (budget)	\$0.821	\$0.802	\$0.788	\$0.769	\$0.736	

For Discussion Only

NYISO 2007 BUDGET OVERVIEW: Summary of Significant Changes

Comparison of "Current Year Budget Needs" (i.e. Controllable Annual Spending):

2006 Current Year Budget Needs	\$130.1
Less: Cost of KCC Building directly financed in 2006	<u>(\$8.5)</u>
Equals: 2006 Current Year Budget Needs – Restated for Comparability	\$121.6
Compared to: 2007 Current Year Budget Needs	<u>\$117.9</u>
Equals: Net Savings on annual Current Year Budget Needs	\$ 3.7

The decrease in Current Year Budget Needs is primarily driven by a net decrease in Capital/Computer Services costs, lower insurance costs, and lower NPCC costs. These decreases are partially offset by increases in Salaries & Benefits and Professional Fees. Additional details on these items and others are provided on the following slide.

NYISO 2007 BUDGET OVERVIEW:

Summary of Significant Changes *(cont'd)*

2006 Rate Schedule 1 Revenue Requirement		\$133.1
➤ <u>Less: Efficiencies and reductions</u>		
Reductions in total capital/computer services <i>(excl. KCC building renovations in 2006)</i>	(\$5.5)	
Reduction in FERC Fees assessment	(\$1.7)	
Savings on annual insurance premiums	(\$0.9)	
Reduction in meeting costs	(\$0.6)	
Reduction in NPCC Fees	(\$0.6)	
Reduced building services – KCC consolidation	(\$0.4)	
		(\$9.7)
➤ <u>Plus: Budget increases</u>		
Reduction in funds to carryforward for debt reduction	\$7.5	
Increase in debt service payments from prior year obligations	\$4.2	
Increase in consultants	\$2.5	
Increase in Salaries & Benefits (~2.6%)	\$1.3	
Increase in external legal costs	\$0.5	
Misc. other increases	\$0.3	
		\$16.3
➤ Subtotal: Increase in Rate Schedule 1 Revenue Req.		\$ 6.6
Equals: 2007 Rate Schedule 1 Revenue Requirement		\$139.7

NYISO 2007 BUDGET OVERVIEW: Line Item Details - CAPITAL

(\$ in millions)	2007 Draft	2006 Budget	\$ Change
Replacement of Existing Hardware	\$2.0	\$3.6	(\$1.6)
Additional Software Licenses (capitalized)	\$1.3	\$2.0	(\$0.7)
Renovations to Power Control Center	\$0.6	\$0.8	(\$0.2)
Acquisition and Renovation of New Headquarters Facility	\$0.4	\$11.2	(\$10.8)
Replacement of Existing Furniture	\$0.1	\$ 0.1	\$ -
Additional Hardware/Software for Product Enhancements	\$ -	\$3.3	(\$3.3)
Total Capital Costs	\$4.4	\$21.0	(\$16.6)

Replacement of Existing Hardware:

To maintain current technology, NYISO's strategy is to replace existing hardware every three years. The 2007 level of capital spending on upgrading existing hardware is lower than 2006 as certain anticipated 2007 hardware purchases were accelerated into 2006.

Additional Software Licenses (Capitalized):

The level of capitalized software licenses decreased from 2006 to 2007 as certain software licenses previously considered capital for budget purposes have now more accurately been reflected as computer services expenses (see corresponding increase in this line item).

Acquisition and Renovation of New Headquarters Facility:

The majority of the renovations on the KCC building were completed in 2006, with certain minor costs remaining for 2007.

Hardware/Software for Product Enhancements:

None of the product enhancements anticipated for 2007 will require capital costs. During 2006, NYISO incurred the capital investment for such projects as the Settlements System Replacement and additional DSS datamarts.

NYISO 2007 BUDGET OVERVIEW:

Line Item Details – SALARIES & BENEFITS

(\$ in millions)	2007 Draft	2006 Budget	\$ Change
Salaries	\$35.2	\$34.5	\$0.7
Incentive Bonuses	\$5.2	\$4.9	\$0.3
Payroll Taxes	\$2.7	\$2.7	\$ -
Benefit Programs	\$7.5	\$7.2	\$0.3
Total Salaries & Benefits	\$50.6	\$49.3	\$1.3
<p><i>NYISO's total headcount complement is 425 FTEs, although an average of approximately 20 openings is expected. Therefore, the 2007 budget reflects Salaries & Benefits for 405 FTEs.</i></p>			
<p><i>The increase in Salaries & Benefits is primarily driven by an average salary increase of ~4%. The increase in Salaries has a corresponding impact on benefit costs.</i></p>			

NYISO 2007 BUDGET OVERVIEW:

Line Item Details – PROFESSIONAL FEES

(\$ in millions)	2007 Draft	2006 Budget	\$ Change
<i>Note: Individual initiatives and/or vendors exceeding \$250K are listed below.</i>			
Product Enhancement Consultants (<i>several vendors</i>)	\$9.1	\$7.0	\$2.1
External Legal Fees	\$6.0	\$5.5	\$0.5
SMD 2.0 Onsite Support and Ranger Enhancements	\$1.6	\$1.2	\$0.4
Security Guards	\$1.5	\$1.4	\$0.1
Lean Six Sigma Quality Initiative Consultants	\$1.5	\$0.6	\$0.9
Market Advisor & related consulting	\$1.2	\$1.1	\$0.1
Market Design, Price Validation assistance & related consulting	\$1.1	\$1.2	(\$0.1)
External Audits (fin'l audit, SAS 70) and Internal Audit Co-sourcing	\$1.0	\$0.8	\$0.2
Staff augmentation to support integration of certain IT processes	\$0.7	\$ -	\$0.7
Subtotal (see additional details on next page)	\$23.7	\$18.8	\$4.9
<p>Product Enhancement Consultants: The 2007 budget for consultants to assist with product enhancement initiatives reflects an increase of \$2.1M as several multi-year enhancements (i.e. Settlements System Replacement, Comprehensive Bid Management System Replacement, Enhanced Price Validation, etc.) are in phases requiring expertise from external consultants. In comparison, during 2006, many of these projects were in initial phases that did not require as much reliance on consultants. Details on intended product enhancements will be provided in a separate presentation.</p>			
<p>External Legal Fees: In 2007, NYISO increased the external legal budget from \$5.5M to \$6.0M, partly in consideration of increased litigation and FERC filings. Note that the 2006 actuals are targeted at \$6.3M.</p>			
<p>Lean Six Sigma Quality Initiative Consultants: Consulting resources will be used during 2007 to assist in training NYISO's employees in the LSS methodology and developing process improvement projects. Currently an additional ~140 employees are expected to receive LSS training and begin Green Belt projects in 2007.</p>			

NYISO 2007 BUDGET OVERVIEW:

Line Item Details – PROFESSIONAL FEES (*cont'd*)

(\$ in millions)	2007 Draft	2006 Budget	\$ Change
<i>Note: Individual initiatives and/or vendors exceeding \$250K are listed below.</i>			
Subtotal (from previous page)	\$23.7	\$18.8	\$4.9
Consultants to assist with Oracle upgrade / Oracle Forms	\$0.5	\$0.4	\$0.1
Attachment N Support Consultants	\$0.5	\$0.5	-
Staff augmentation to assist with Business Requirements for Financial Systems	\$0.5	\$0.2	\$0.3
ICAP Demand Curve Study	\$0.4	\$ -	\$0.4
Consultant to assist with QA tools	\$0.4	\$ -	\$0.4
Strategic Planning Process	\$0.3	\$ -	\$0.3
Consultant to assist with TCC Auction Support	\$0.3	\$0.1	\$0.2
Consultant to assist with Application Support for Data Warehouse	\$0.2	\$0.6	(\$0.4)
Consultants for Long-Term Reliability Studies	\$ -	\$0.4	(\$0.4)
Other Misc. Professional Fees (all individually < \$250K)	\$5.4	\$8.2	(\$2.8)
Total Professional Fees	\$32.2	\$29.2	\$3.0

NYISO 2007 BUDGET OVERVIEW: Line Item Details – BUILDING SERVICES

<i>(\$ in millions)</i>	<u>2007 Draft</u>	<u>2006 Budget</u>	<u>\$ Change</u>
Total Building Services	\$4.0	\$4.4	(\$0.4)

The \$0.4M reduction in Building Services costs from 2006 to 2007 is primarily due to:

- \$0.7M decrease in rental & other costs associated with previously-leased facilities. NYISO vacated Washington Avenue in early 2006 and plans to vacate the the Annex and Wolf Road facilities in early 2007.
- Offset by: approximately \$0.3M in increases for utilities and maintenance costs for NYISO's owned facilities, due primarily to increased occupation of the KCC building.

NYISO 2007 BUDGET OVERVIEW: Line Item Details – COMPUTER SERVICES

<i>(\$ in millions)</i>	<u>2007 Draft</u>	<u>2006 Budget</u>	<u>\$ Change</u>
Hardware Maintenance and related costs	\$4.1	\$2.0	\$2.1
Software Licenses (not capitalized) and Maintenance costs	\$8.4	\$7.8	\$0.6
Computer and Electronics Supplies	<u>\$0.5</u>	<u>\$0.7</u>	<u>(\$0.2)</u>
Total Computer Services Costs	\$13.0	\$10.5	\$2.5

Hardware Maintenance and Software Licenses/Maintenance:

The increase in hardware maintenance and software licenses/maintenance costs from 2006 to 2007 is primarily the result of higher maintenance for SMD2 equipment, which was under warranty through 2006. \$1.3M is included in the 2007 budget for such maintenance costs.

Additionally, certain software licenses previously classified as Capital for budget purposes have now more accurately been reflected as computer services expenses (see corresponding decrease in the Capital line item).

The increases in these line items are also driven by increases in vendor maintenance rates and the volume of hardware/software maintained by NYISO.

NYISO 2007 BUDGET OVERVIEW: Line Item Details - INSURANCE

(\$ in millions)	2007 <u>Draft</u>	2006 <u>Budget</u>	\$ <u>Change</u>
Property & Liability Insurance	\$2.8	\$3.4	(\$0.6)
Directors' & Officers' Insurance	<u>\$0.9</u>	<u>\$1.2</u>	<u>(\$0.3)</u>
Total Insurance	\$3.7	\$4.6	(\$0.9)

Property & Liability Insurance and D&O Insurance:

In 2006, NYISO aggressively worked with its insurance broker to drive NYISO's **actual** insurance costs to \$3.6M, or ~\$1.0M under budget. NYISO's 2007 budget reflects a minor expected increase in premiums from the 2006 actuals.

NYISO 2007 BUDGET OVERVIEW: Line Item Details – OTHER EXPENSES

(\$ in millions)	<u>2007 Draft</u>	<u>2006 Budget</u>	<u>\$ Change</u>
BOD Fees and Expenses	\$1.4	\$1.3	\$0.1
Travel, Meetings, Training Costs	\$2.4	\$3.0	(\$0.6)
NPCC Fees	<u>\$1.2</u>	<u>\$1.8</u>	<u>(\$0.6)</u>
Total Other Expenses	\$5.0	\$6.1	(\$1.1)

BOD Fees and Expenses:

Minor increases are expected in BOD fees and expenses.

Travel, Meetings, Training Costs:

The decrease in this line item reflects lower costs for MP meetings once such meetings can be held at the NYISO KCC facility rather than at offsite venues.

NPCC Fees:

In 2006, FERC appointed NERC as the Electric Reliability Organization (ERO), with funding allocated 100% to LSEs. NPCC has provided NYISO with correspondence indicating the portion of NPCC's 2007 budget related to ERO vs. non-ERO funding. The non-ERO funding for NPCC is included in NYISO's 2007 budget and is reflected above. NYISO has recommended that NERC invoice NY LSEs directly, and therefore, ERO funding is not included within NYISO's 2007 budget.

NYISO 2007 BUDGET OVERVIEW:

Line Item Details – DEBT SERVICE

Major Assumptions:

- NYISO plans to obtain debt financing of \$80M to cover capital acquisitions and product enhancements during 2007-2010 (~\$20M is available for borrowings each year during this period). This debt will be repaid over a three-year life to coincide with the average life of the underlying assets. This is a reduction from a four-year life utilized in prior debt facilities.
- \$15M will be borrowed in 2007 to fund capital acquisitions and product enhancements (PSC approval for new debt facility is scheduled for January 2007)
- \$5M is expected to be available from 2006 budget spending underruns and/or transactional volume overcollections to use in lieu of additional 2007 debt borrowings
- Interest on 2007 debt borrowings is estimated at 7%. Interest hedging will be completed in early 2007.
- Interest on all existing debt is hedged at slightly <5% for 2003-2006 budget loans and slightly <6% for the KCC building 20-year financing.

NYISO 2007 BUDGET OVERVIEW:

Line Item Details – DEBT SERVICE (*cont'd*)

ANNUAL PRINCIPAL AND INTEREST REPAYMENTS **									
(\$ in millions)									
<u>Debt Facility</u>	<u>Repayment Period</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
2003 Budget Loan	4 years	\$12.7	\$12.2	\$2.0	\$ -	\$ -	\$ -	\$ -	\$ -
2004 Budget Loan	4 years	12.0	11.5	10.7	-	-	-	-	-
2005 KCC Bldg Mortgage & Renov.	20 years	0.9	1.7	1.7	2.1	2.1	2.1	2.1	2.1
2005 Budget Loan	4 years	5.2	5.0	4.8	4.6	-	-	-	-
2006 Budget Loan	4 years	0.3	4.5	4.3	4.1	4.0	-	-	-
2007 Budget Loan	3 years		0.5	5.9	5.5	5.2			
2008 Budget Loan	3 years			0.6	7.8	7.3	6.9		
2009 Budget Loan	3 years				0.6	7.8	7.3	6.9	
2010 Budget Loan	3 years					0.6	7.8	7.3	6.9
Bank Fees	n/a	0.4	0.5	0.5	0.5	0.6	0.6	0.6	0.6
Total		\$31.5	\$35.9	\$30.5	\$25.2	\$27.6	**	**	**

*** Note: Totals after 2010 are not presented as additional loans after 2010 are not factored into this table.*

NYISO 2007 BUDGET OVERVIEW:

Line Item Details – FERC FEES

- NYISO includes FERC Fees within its annual RS#1 budget revenue requirements. Other ISOs do not utilize this practice, and instead, assess FERC Fees as a direct passthrough to MPs.
- The historical level of FERC Fees is presented in the tables to the right, and illustrates the variation in annual FERC Fee assessments.
- FERC has estimated its program costs to increase 4.7% in 2007. NYISO's 2007 budget for FERC Fees is \$8.2M, which represents a corresponding ~6% increase from the 2006 actuals.

NYISO History of FERC Fees					
(\$ in millions)	2002	2003	2004	2005	2006
Annual Budget	\$5.0	\$5.0	\$8.0	\$7.0	\$9.9
FERC Annual Assessment	\$6.2	\$7.7	\$6.7	\$8.3	\$7.8
FERC Adj. to Prior Year	\$-	\$0.2	(\$1.4)	\$0.3	\$-
Total Annual FERC Fees	\$6.2	\$7.7	\$5.3	\$8.6	\$7.8
% Change in FERC Fees	n/a	24%	(31%)	62%	(10%)

Other ISOs History of FERC Fees					
(\$ in millions)	2002	2003	2004	2005	2006
NYISO	\$6.2	\$7.7	\$5.3	\$8.6	\$7.8
CAISO	\$9.1	\$11.3	\$7.8	\$12.3	\$10.8
PJM	\$1.7	\$25.2	\$14.1	\$21.4	\$32.7
MISO	\$-	\$1.4	\$30.0	\$30.0	\$29.2
ISO-NE	\$-	\$-	\$-	\$-	\$6.3

SUPPLEMENTAL INFORMATION

NYISO 2007 BUDGET OVERVIEW: Other ISOs Comparison

(\$ in millions)					
ISO/RTO	2007 Revenue Requirement	Less: 2007 FERC Fees	2007 Rev. Req. excluding FERC Fees	Debt Outstanding at 12/31/07	FTEs at 12/31/07
MISO	\$250.0M	-	\$250.0	\$352.5M	646
PJM	\$240.0	-	\$240.0	\$30.0	Not available
CAISO		-			
ERCOT		-			
NYISO	\$139.7	(8.2)	\$131.5	\$70.4	425 (target)
ISO-NE	\$115.1	-	\$115.1	\$88.1	432

NYISO 2007 BUDGET OVERVIEW:

Recap

Schedule:

- **September 27:** BSP subcommittee review of draft 2007 budget
- **September 29:** Information on draft 2007 budget provided to Management Committee for review
- **October 16:** NYISO presents draft 2007 budget to BOD Finance Committee for review
- **Mid-October (TBD):** BSP meeting to discuss feedback received from Management Committee and BOD Finance Committee
- **October 25:** Management Committee vote on final 2007 budget for recommendation to BOD Finance Committee
- **November 21:** BOD Finance Committee approval of final 2007 budget

Summary Points:

- **NYISO has prioritized all budget requests to allow completion of priority initiatives, while staying within the budget target established during 2003 for 2007**
- **Net NYISO controllable spending reflects a decrease from 2006 to 2007**
- **2006 will continue the focus of improving NYISO's existing processes and procedures rather than significant market or technology changes**

Wrap-Up:

- **Refer to separate presentation for composition of 2007 anticipated product enhancements**
- **Refer to separate presentation for details on budget targets for 2008 – 2011**
- **Market Participant Questions / Concerns???**