



Draft NYISO 2004 Budget Report

BS&P Report to
Management Committee
October 17, 2003
Agenda #8



Objective of Today's Report

- Provide overview of 2004 Budget to MC for November 12 budget vote
- Review budget targets for 2005 - 2008
- Receive MC input on BS&P recommendations
- Receive further MC input on draft 2004 budget and budget targets
- Review of next steps
 - October 28 BS&P meeting
 - Review NYISO employee incentive goals
 - Executive goals



NYISO 2004 Budget Schedule

- ☑ September 26: Draft 1 presented to BSP
- ☑ October 1: PPT reviews projects
- ☑ October 10: BS&P reviews revised draft budget
- ☑ October 10: PPT reviews updated projects
- ☑ October 17: BSP presents draft 2 to MC
- October 20: Detailed summary of draft 2 to NYISO Board
- October 28: BS&P reviews draft 3
- October 28: PPT finalizes project priorities
- November 12: MC vote on draft 3
- November 18: BOD approves 2004 Budget



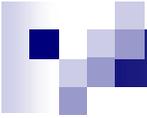
Budget Actions

- NYISO Process
 - Consistent with last year's projections
 - Transition from contractors to employees while reducing combined head count
 - Eliminated \$15 million from budget before coming to BS&P
 - Followed key principals of BSP project financing guidelines
- NYISO response to 9/26 meeting BS&P concerns
 - Financing of Blackout costs – **Draft 2 doesn't finance blackout**
 - Increase legal headcount – **Legal headcount to increase from 4 to 6**
 - Use outside counsel located in lower cost area - **Currently doing so**
 - Eliminate or reduce credit insurance – **NYISO is considering and reviewing**
 - Restructure debt – **Positive ongoing dialog. NYISO evaluating.**

Budget Trends & Projections

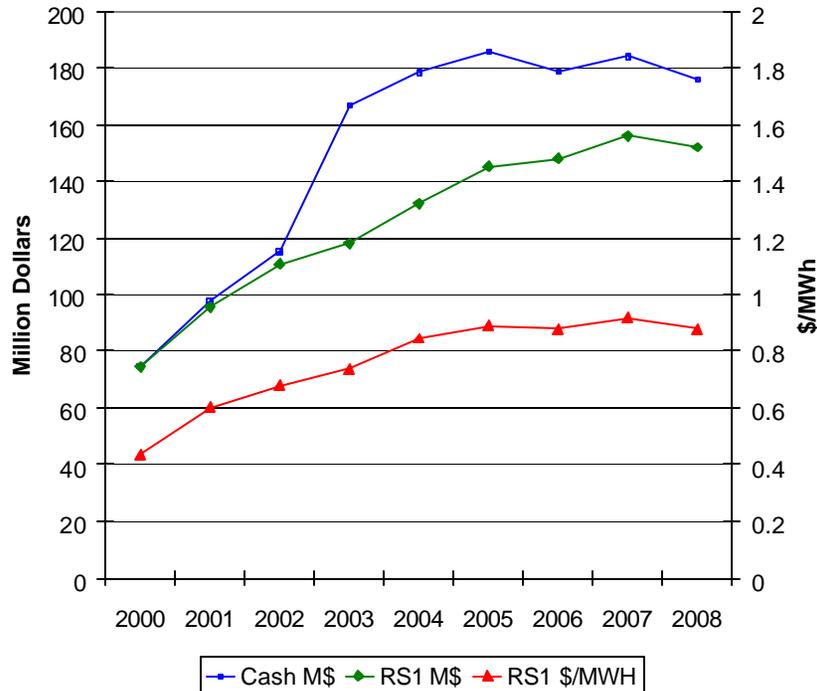
Cost in millions of dollars except Rate Schedule #1

	2003 Final	2004 Draft 1	2004 Draft 2	2005 Target	2006 Target	2007 Target	2008 Target
Baseline (<i>current year needs</i>)	\$99.2	98.3	\$98.3	\$108.0	\$109.0	\$112.0	\$113.0
Projects (<i>current year needs</i>)	\$50.0	45.2	\$45.2	\$44.0	\$32.0	\$27.0	\$23.0
Debt Service (<i>prior year financings</i>)	\$17.6	30.2	\$30.2	\$29.0	\$38.0	\$45.0	\$40.0
Blackout costs	<u>\$ 0.0</u>	<u>5.0</u>	<u>\$5.0</u>	<u>\$5.0</u>	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 0.0</u>
Cash Budget	\$166.8	178.7	\$178.7	\$186.0	\$179.0	\$184.0	\$176.0
Less: Net proceeds on CY financings	(47.0)	(45.4)	(\$41.6)	(\$40.0)	(\$30.0)	(\$27.0)	(\$23.0)
Less: Misc. Revenues	<u>(1.6)</u>	<u>(1.1)</u>	<u>(\$1.1)</u>	<u>(\$1.0)</u>	<u>(\$1.0)</u>	<u>(\$1.0)</u>	<u>(\$1.0)</u>
RS#1 Revenue Requirement	<u>\$118.2</u>	<u>132.2</u>	<u>\$136.0</u>	<u>\$145.0</u>	<u>\$148.0</u>	<u>\$156.0</u>	<u>\$152.0</u>
Rate Schedule #1 (\$/MWH)	<u>\$0.74</u>	<u>\$0.82</u>	<u>\$0.845</u>	<u>\$0.89</u>	<u>\$0.88</u>	<u>\$0.92</u>	<u>\$0.88</u>

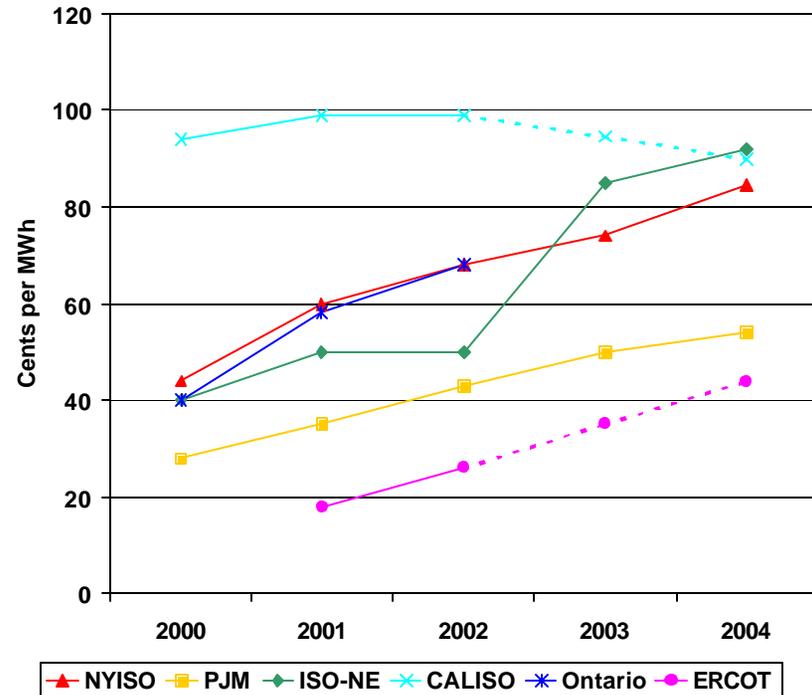


Draft 2004 Budget Trends

NYISO Budget Trends



Comparison with other ISOs



Note: Dashed lines indicate interpolation

Draft 2 Budget Trends by Category

Costs in millions of dollars except Rate Schedule #1

Line Item	Baseline	Projects	Debt Service	Blackout	2004 Draft 2 Budget	2004 Projected Budget*	2003 Final Budget
Capital	\$8.3	\$12.2	\$ -	\$ -	\$20.5	\$17.7	\$31.9
Salaries & Benefits	\$33.8	\$9.5	\$ -	\$0.6	\$43.9	\$42.0	\$38.0
Consultants	\$16.0	\$9.2	\$ -	\$1.3	\$26.5	\$22.0	\$28.7
Legal	\$6.0	\$ -	\$ -	\$3.1	\$9.1	\$6.0	\$6.5
Building Services	\$3.5	\$ -	\$ -	\$ -	\$3.5	\$4.1	\$3.8
Computer Services	\$6.9	\$14.2	\$ -	\$ -	\$21.1	\$21.9	\$20.5
Insurance	\$7.7	\$ -	\$ -	\$ -	\$7.7	\$8.2	\$6.1
Telecommunications	\$2.9	\$ -	\$ -	\$ -	\$2.9	\$2.9	\$3.3
BOD / Training, Meetings, etc. / NPCC Fees	\$5.2	\$0.1	\$ -	\$ -	\$5.3	\$5.7	\$5.5
FERC Fees	\$8.0	\$ -	\$ -	\$ -	\$8.0	\$5.2	\$5.0
Debt Service (from prior years)	\$ -	\$ -	\$30.2	\$ -	\$30.2	\$30.8	\$17.5
TOTAL CASH BUDGET	\$98.3	\$45.2	\$30.2	\$5.0	\$178.7	\$166.5	\$166.8
Less: Net Proceeds from CY financing	(\$8.3)	(\$45.2)	\$11.9	\$ -	(\$41.6)	(\$27.0)	(\$47.0)
Less: Misc. Revenues	(\$1.1)	\$ -	\$ -	\$ -	(\$1.1)	(\$1.4)	(\$1.6)
TOTAL CASH BUDGET, NET OF FIN'GS	\$88.9	\$ -	\$42.1	\$5.0	\$136.0	\$138.1	\$118.2
RATE SCHEDULE #1 (\$/MWH)	\$0.55	\$0.00	\$0.27	\$0.03	\$0.845	\$0.87	\$0.74

* Fall 2002 of projection of 2004 budget



Key Budget Changes (Draft 2)

- Total cash expenses increase 11.9 million or 7.1%
- Rate schedule 1 increases \$0.105 or 14%
- Major cost shifts
 - Completion of RTS project
 - Strategic Projects down \$20.5 million to \$27.8 million. Further reductions planned for 2005
 - Other projects up \$12.3 million to \$17.4 million.
 - Transition from contractors to staff
 - Staff up \$5.9 million as they replace contractors
 - Contractors down from 89 to 17. Costs down from \$12.9 million to \$7.4 million in 2004. Further decreases to \$2.5 million in 2005.
 - \$3 million FERC fee increase
 - \$5 million Blackout costs
 - \$12.7 million debt service cost increase from 2003 financing

FERC Fees and Program Costs

FERC Fees and Program Costs			
	2002	2003	Percent Change
NYISO Assessment	\$6.24 M	\$7.69 M	↑23%
FERC Program Costs	\$65.6 M	\$77.8 M	↑18%

Inter ISO Activity

- Task force formed to discuss impact of FERC fees on ISOs and to identify potential actions

Regulatory Proceedings

- MISO/NYISO/PJM filed petition for rulemaking on 12/2/02 (RM00-7-008)
 - 4/11/03 FERC Order denied petition for rulemaking
 - MISO requested rehearing of the Order on 5/12/03 (RM00-7-009)
 - 7/10/03 FERC Order denied request for rehearing
- MISO sought review of the 4/11/03 and 7/10/03 orders in the U.S. Court of Appeals, DC Circuit
 - NYISO filed intervention on 9/10/03
- PJM requested rehearing of the 2003 FERC fee invoice (RM00-7-010)
 - NYISO filed intervention on 9/10/03
 - FERC issued tolling order on 9/24/03

Change in Headcount

HEADCOUNT SUMMARY	FTEs	Contractors	Total
12/31/02 Totals	312	34	346
Staff additions in 2003	<u>46</u>	<u>55</u>	<u>101</u>
12/31/03 Totals (projected)	358	89	447
Conversions of contractors to FTEs in 2004	34	(34)	-
Reduction of contractors in 2004 (SMD-related)	=	(38)	(38)
12/31/04 Totals	392	17	409

Project Budget Comparison

Projects costs in millions of dollars

2004 Budget	Pre 03	2003	2004	Post 04	Total
Strategic Initiatives	14.7	48.3	27.8	2.5	93.3
2003 Funded Projects		4.1	4.1	0.5	8.7
Funded 2004 Projects			11.0	11.0	22.0
Flexible 2004 Project Budget			2.3	0.0	2.3
Total	14.7	52.4	45.2	14.0	126.3

2003 Budget	Pre 03	2003	2004	Post 04	Total
Strategic Initiatives	14.7	48.0	25.0	7.7	95.3
2003 Funded Projects		5.1	0.0	0.0	5.1
Total	14.7	53.1	25	7.7	100.4

Projects Detail (Draft 2)

Costs in millions of dollars

Project Name	Labor	Capital	Other	Total
SMD 2.0	\$4.6	\$8.8	\$9.6	\$23.0
DSS	\$0.9	\$0.3	\$ 1.3	\$ 2.5
Facilitated Checkout	\$0.8	\$0.0	\$ 1.5	\$ 2.3
Market Data Ex. Enhancements (Portal)	\$0.7	\$0.7	\$ 0.7	\$ 2.1
Billing Simulator	\$0.4	\$0.2	\$1.3	\$ 1.9
Computer System Availability Monitoring	\$0.4	\$0.7	\$ 0.5	\$ 1.6
TCC & UCAP Automation	\$0.7	\$0.0	\$ 0.8	\$ 1.5
New Technology Initiatives	\$0.6	\$0.2	\$ 0.2	\$ 1.0
Billing Projects	\$0.9	\$0.0	\$ 0.1	\$ 1.0
Controllable External Tie Scheduling	\$0.4	\$0.0	\$ 0.5	\$ 0.9
Software Dev. Lifecycle Tools (Rational)	\$0.3	\$0.5	\$ 0.0	\$ 0.8
Operational Information to the Marketplace	\$0.2	\$0.3	\$ 0.3	\$ 0.8
Documentum Implementation	\$0.3	\$0.1	\$ 0.3	\$ 0.7
Enhanced Market Access & Security (LDAP / SSO)	\$0.1	\$0.4	\$ 0.1	\$ 0.6
Inter-ISO Standards for Market Messages	\$0.3	\$0.0	\$ 0.3	\$ 0.6
Develop a Virtual Regional Dispatch	\$0.1	\$0.0	\$ 0.5	\$ 0.6
Assess Options to Shorten Billing Cycle	\$0.1	\$0.0	\$ 0.4	\$ 0.5
Consolidated NYISO Offices	\$0.1	\$0.0	\$ 0.4	\$ 0.5
Flexible Projects	<u>\$1.4</u>	<u>\$0.0</u>	<u>\$ 0.9</u>	<u>\$ 2.3</u>
Total	\$13.3	\$12.2	\$19.7	\$45.2

Flexible Projects (Draft 2)

Project Numbers: A564, A625, A630, A668, A676, A687, A690, TBD

(Bi-Directional Modeling of Generators, Direct Generator Communications, Automate Voltage Support Billing Calculation, Scheduling & Pricing Non-Competitive Proxy interfaces, Automate DAM Congestion Billing Calculation, Automate Local Black Start Billing Calculation, Separate Grouped Units Billing Data)

This category, Other Projects, is meant to capture 1) new projects that may potentially arise during 2004 and 2) existing projects that have not been otherwise detailed throughout this presentation. A pool of resources, totaling approximately 20,000 hours and 11 FTEs is available for assignment to such projects, which would be prioritized through the Projects Priority Team (PPT) process.

However, NYISO anticipates that new initiatives arising during 2004 will consume this entire resource allocation. Therefore, the projects listed above are not likely to be undertaken during 2004, unless the level of new 2004 initiatives is significantly lower than previous years.

(\$ in millions)	Labor	Capital	Other	Total
2004	\$1.4	\$0.0	\$0.9	\$2.3
Post-2004	<u>TBD</u>	<u>TBD</u>	<u>TBD</u>	<u>TBD</u>
Total	TBD	TBD	TBD	TBD

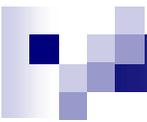
BS&P Budget Report to Management
Committee



BS&P Recommendations

Flexible Projects Budget

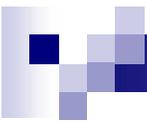
- BS&P recommends special treatment for flexible projects
 - Intent would be for listed projects to be funded according to priorities set by PPT
 - In the event new needs come up, resources could be redirected using the Project Financing Process
 - Funds cannot be shifted to other approved projects unless approval received from PPT and BS&P
 - Use of funds for new projects reviewed and approved by BS&P Project Financing process and priority approved by PPT.
 - Subject to limits of project amount thresholds
 - Subject to exceptions to emergencies



BS&P Recommendations

Blackout Funding

- Blackout costs are a large unknown.
 - Current rate of spending is \$250,000 per month
 - Future costs driven by FERC, NERC and other external entities
 - \$5.0 million breakdown – 0.6 internal labor, 3.1 external legal, 0.5 transmission studies, 0.5 reliability studies, 0.3 public relations
- BS&P concerned with with open funding of project and interaction with employee performance incentives.
- BS&P Recommendations for blackout funding
 - The \$4.4 million external blackout costs be segregated from rest of budget.
 - The \$0.6 million internal costs handled through regular project management
 - Funds cannot be shifted to other uses.
 - Any surplus refunded to market participants.
 - Employee performance incentive should not count savings from under spending blackout budget.
 - Executive goals should include keeping costs under control
- Alternative approaches to be discussed

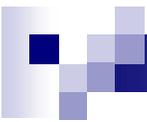


NYISO Debt Structure

- Debt structure is key driver to cost increases
- For 2003 budget, recommendation made by MC and accepted by NYISO Board to finance projects in 2003 to defer rate increase with the understanding that this would place upward rate pressure in future years
 - Rational was that the strategic initiatives would have a multi-year payback for future market participants
- The MC made a commitment to pay this back in the future.
- Need to develop long term financing plan that manages future rate increases while assuring necessary projects get done

Debt Service Summary (Draft 2)

	Scheduled Annual Repayments (p&i)				
	2004	2005	2006	2007	2008
Term Loan re: Start-Up Costs (2000)	\$12.1	\$ -	\$ -	\$ -	\$ -
Hardware Financings (2001-2002)	\$3.6	\$2.2	\$ -	\$ -	\$ -
Budget Financing (2003)	\$13.8	\$13.2	\$12.7	\$12.1	\$ -
Budget Financing (2004)	\$ -	\$12.9	\$12.0	\$11.6	\$11.4
Budget Financing (2005)	\$ -	\$ -	\$12.6	\$11.5	\$11.0
Budget Financing (2006)	\$ -	\$ -	\$ -	\$9.1	\$8.7
Budget Financing (2007)	\$ -	\$ -	\$ -	\$ -	\$8.2
Bank Fees	<u>\$0.7</u>	<u>\$0.7</u>	<u>\$0.7</u>	<u>\$0.7</u>	<u>\$0.7</u>
Subtotal: Debt Service Payments (prior year financings)	\$30.2	\$29.0	\$38.0	\$45.0	\$40.0
Initial year funding (current year financing)	<u>\$11.9</u>	<u>\$11.3</u>	<u>\$8.6</u>	<u>\$7.8</u>	<u>\$6.6</u>
Total: Debt Service	\$42.1	\$40.3	\$46.6	\$52.8	\$46.6
RS#1 Impact per Year	\$0.26	\$0.25	\$0.28	\$0.31	\$0.27



BS&P Recommendations

Financing Guidelines

- Objective is to avoid creating a structural deficit or unacceptable rate increases in future years
- Generally, financing should only be used when necessary to stabilize rates from year to year.
 - Financing should be tied to specific items or projects to prevent structural deficits
 - Financing should be commensurate with the expected life of the item financed
 - If not required to moderate rate increases, projects should be expensed
- Items eligible for financing
 - Capital investments (buildings, furniture, computer equipment, etc.) with multi-year life
 - Software without annual license fees
 - Project costs with a long-term expected use (including hardware, software, man-power costs, building overhead, etc.)
- Items not eligible for financing
 - Operating costs (Recurring annual or ongoing expenses such as payroll, taxes, debt service, fees, telecommunications, building services, insurance, utilities, etc.)
 - Costs for studies, reports, evaluations, ongoing consulting activities
 - Legal costs



BS&P Recommendations

Target Rate Increases

- BS&P recommends adopting target rate increases. For example:
 - 5 – 7 % in 2004
 - 3% in 2005
 - 0% in 2006 and beyond
- To accomplish this some debt structure approaches might include
 - Defer financing of 2004 projects to take advantage of ending of startup financing
 - Finance 2004 non-computer hardware strategic initiative costs over 10 year time frame
 - Consider re-financing 2003 non-computer hardware strategic initiative costs over 9 or 8 year period starting in 2004 or 2005
 - Generally finance other projects over 5 year time frame
 - Limit total amount of future project budgets to control costs
- In a non-debt area, look at whether projected 10 million increase in base costs from 2004 to 2005 is necessary

Debt Service Summary

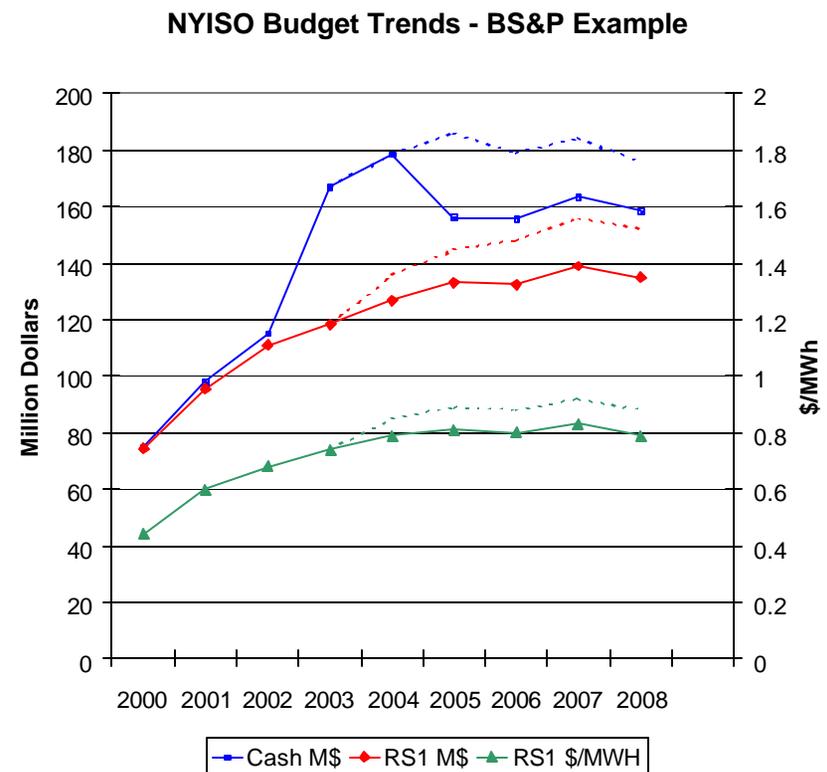
BS&P Recommendation

	Scheduled Annual Repayments				
	2004	2005	2006	2007	2008
Term Loan re: Start-Up Costs (2000)	\$12.1	\$ -	\$ -	\$ -	\$ -
Hardware Financings (2001-2002)	\$3.6	\$2.2	\$ -	\$ -	\$ -
Budget Financing (2003)	\$13.8	\$13.2	\$12.7	\$12.1	\$ -
Budget Financing (2004) – 5 year financing	\$ -	\$8.2	\$7.6	\$7.0	\$6.4
Budget Financing (2004) – 10 year financing	\$ -	\$3.8	\$3.6	\$3.4	\$3.2
Budget Financing (2005)	\$ -	\$ -	\$5.7	\$5.2	\$5.0
Budget Financing (2006)	\$ -	\$ -	\$ -	\$6.0	\$5.7
Budget Financing (2007)	\$ -	\$ -	\$ -	\$ -	\$6.7
Bank Fees	<u>\$0.7</u>	<u>\$0.7</u>	<u>\$0.7</u>	<u>\$0.7</u>	<u>\$0.7</u>
Subtotal: Debt Service Payments (prior year financings)	\$30.2	\$28.2	\$30.4	\$34.4	\$27.7
Initial year funding (current year financing)	<u>\$0.0</u>	<u>\$5.1</u>	<u>\$5.6</u>	<u>\$6.4</u>	<u>\$6.6</u>
Total: Debt Service	\$30.2	\$33.3	\$36.0	\$40.8	\$34.3
RS#1 Impact per Year	\$0.19	\$0.20	\$0.22	\$0.24	\$0.20

Draft 2004 Budget Trends

Impact of BS&P Recommendations

- Illustrative example
 - Needs to be reviewed and worked out in detail by NYISO finance
 - Dependent upon banks and NYISO Board willingness accept longer-term financing
 - Numbers may change significantly as details are worked out
- In this example
 - 2005 and beyond base costs reduced \$5 million
 - Future project funding reduced from ISO proposed 44 to 23 million level to 20 to 23 million.
 - 10 year financing for 2004 strategic initiatives non-computer expenses. No refinancing of 2003.
- Result is
 - 6% increase in 2004
 - 3% increase in 2005
 - Average of a 0% change in 2006 and beyond



Note: Dashed lines indicate Draft 2 Budget



MC Discussion of Issues

1. Input on conditions for blackout funding
 - Alternative approaches
2. Input on conditions for flexible project funding
3. Are rate increase guidelines acceptable or should we recommend cutting additional projects?
4. If the MC recommends cutting projects, which projects should be eliminated or deferred?
5. Is the long term trend acceptable?
6. Other issues.



BS&P Next Steps

- Next meeting – October 28, 9:30 am
 - Further refinement of budget and financing plan
 - Drafting of budget resolution
 - Further employee goal input and review

Proposed NYISO Incentive Goals Comparison 2004 to 2003

Proposed 2004

- Reliability Gateway
- Market Gateway
- **Comprehensive Planning**
- Operating Standards
- Market Availability
- Real-Time Price
Certainty/Accuracy
- Billing and True-Up
- **Budget Accuracy**
- **Manual Update**
- Improve Customer Satisfaction
- Project Management

Comparison to 2003

- Continuation
- Continuation
- **New**
- Similar, adds new aspect
- Continuation
- Similar
- 3 parts, 1 similar, 2 new
- **New**
- **New**
- Continuation
- Continuation



BS&P Next Steps

- Future meeting - Executive goals
 - Long Term Goals to be set for a 3 year period
 - Meeting with NYISO will be scheduled in Nov. for MP Input
 - Areas currently under consideration
 - Reliability
 - Market Efficiency
 - Reduction of Seams
 - Customer Billing
 - Transition Year Goals
 - Implementation of SMD 2.0
 - System Planning
 - Customer Satisfaction