Financial Statements

Independent Auditors' Report

To the Board of Directors of
New York Independent System Operator, Inc.

We have audited the accompanying statements of financial position of New York Independent System Operator, Inc. ("NYISO") as of December 31, 2003 and 2002, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of NYISO'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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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, such financial statements present fairly, in all material respects, the financial position of NYISO as of December 31, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 26, 2004

STATEMENTS OF FINANCIAL POSITION

	December 31, 2003	December 31, 2002
ASSETS		
Current Assets:		
Cash and cash equivalents	**$ 48,930,462**	$ 33,552,160
Accounts receivable, net (Note 2)	**13,810,170**	31,678,822
Prepaid expenses	**6,417,675**	5,289,445
Restricted cash	**210,467,802**	107,301,025
Regulatory assets - current portion (Note 3)	**13,241,667**	3,500,000
Other assets - current portion	**257,405**	-
Total current assets	**293,125,181**	181,321,452
Noncurrent Assets:		
Regulatory transition asset, net (Note 3)	**10,988,489**	21,976,978
Regulatory assets (Note 3)	**39,591,666**	5,833,333
Property and equipment, net (Note 4)	**69,593,658**	29,549,070
Other noncurrent assets	**2,428,310**	3,782,363
Total noncurrent assets	**122,602,123**	61,141,744
Total Assets	**$415,727,304**	$ 242,463,196
LIABILITIES		
Current Liabilities:		
Accounts payable and accrued expenses	**$ 16,811,758**	$ 14,966,567
Market participant security deposits	**187,353,080**	82,303,164
Long-term debt - current portion (Note 6)	**25,898,628**	15,299,241
Capital lease obligations - current portion (Note 9)	**-**	116,602
Working capital reserve (Note 10)	**48,785,895**	48,422,459
Deferred revenue - current portion (Note 11)	**39,783,261**	29,008,566
Regulatory liabilities - current portion (Note 12)	**3,289,497**	8,167,476
Other current liabilities	**1,436,425**	2,088,223
Total current liabilities	**323,358,544**	200,372,298
Noncurrent Liabilities:		
Accrued pension liability (Note 8)	**662,246**	1,260,094
Accrued postretirement liability (Note 8)	**2,161,503**	-
Deferred revenue (Note 11)	**46,830,327**	18,110,758
Regulatory liabilities (Note 12)	**2,730,107**	3,634,685
Other noncurrent liabilities (Note 8)	**392,910**	595,067
Long-term debt (Note 6)	**39,591,667**	18,490,294
Total noncurrent liabilities	**92,368,760**	42,090,898
Commitments and Contingencies (Note 13)		
Total Liabilities	**$415,727,304**	$ 242,463,196

See notes to financial statements.

STATEMENTS OF ACTIVITIES

	Years Ended December 31, 2003	2002
Revenues:		
Rate Schedule 1 tariff charge	**$116,822,858**	$ 98,379,114
Fees and services	**755,936**	839,089
Interest income	**240,475**	192,729
Total revenues	**117,819,269**	99,410,932
Operating Expenses:		
Compensation and related benefits (Note 8)	**32,742,038**	30,580,920
Professional fees and consultants	**24,972,472**	21,987,327
Depreciation and amortization	**17,570,115**	8,420,385
Amortization of regulatory transition asset (Note 3)	**10,988,489**	10,988,489
Rent, equipment leases and other facility costs	**10,627,028**	10,134,706
Federal Energy Regulatory Commission fees	**7,862,930**	6,234,908
Administrative and other expenses	**4,137,937**	2,901,535
Telecommunications	**3,110,895**	2,236,580
Training, travel and meeting expenses	**2,986,814**	2,574,766
Northeast Power Coordinating Council fees	**1,496,308**	1,374,043
Total operating expenses	**116,495,026**	97,433,659
Interest Expense	**$ 1,324,243**	$ 1,977,273
Net Results of Activities	**$ -**	$ -

See notes to financial statements.

STATEMENTS OF CASH FLOWS

	Years Ended December 31, 2003	2002
Cash Flows from Operating Activities:		
Net results of activities	**$ -**	$ -
Adjustments to reconcile net results of activities to net cash provided by operating activities:		
Depreciation and amortization	**17,570,115**	8,420,385
Amortization of regulatory transition asset	**10,988,489**	10,988,489
Change in operating assets and liabilities:		
Decrease (increase) in accounts receivable and prepaid expenses	**16,740,422**	(17,832,906)
Increase (decrease) in accounts payable and accrued expenses	**1,845,193**	(577,179)
(Increase) in restricted cash	**(103,166,777)**	(58,858,738)
(Increase) in regulatory assets	**(43,500,000)**	(7,583,333)
Decrease (increase) in other assets	**1,096,650**	(881,081)
Increase in working capital reserve	**363,436**	754,076
Increase in market participant security deposits	**105,049,916**	47,176,198
Increase in deferred revenue and other liabilities	**34,421,404**	27,857,215
Net cash provided by operating activities	**41,408,848**	9,463,126
Cash Flows from Investing Activities:		
Acquisition of property and equipment (including capitalized interest)	**(57,614,703)**	(23,945,493)
Net cash used in investing activities	**(57,614,703)**	(23,945,493)
Cash Flows from Financing Activities:		
Repayment of term credit loan	**(11,799,241)**	(11,018,351)
Proceeds from 2003 budget facility loan	**47,000,000**	-
Proceeds from equipment term loan	**-**	8,700,000
Repayment of equipment term notes	**(3,500,000)**	(1,116,667)
Decrease in capital lease obligations	**(116,602)**	(275,122)
Net cash provided by (used in) financing activities	**31,584,157**	(3,710,140)
Net (Decrease) Increase in Cash and Cash Equivalents	**15,378,302**	(18,192,507)
Cash and Cash Equivalents, Beginning of Year	**33,552,160**	51,744,667
Cash and Cash Equivalents, End of Year	**$ 48,930,462**	$ 33,552,160
Supplemental Disclosure of Cash Flow Information – Cash paid during the year for interest	**$ 2,316,991**	$ 2,266,334

See notes to financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business Description - The New York Independent System Operator, Inc. ("NYISO") was formed in April 1997 and commenced operations on December 1, 1999. NYISO is incorporated in the State of New York as a not-for-profit organization. NYISO assumed the responsibilities of its predecessor, the New York Power Pool ("NYPP"), which had coordinated the reliability of New York's electric power grid for more than 30 years. Formed as a result of Federal Energy Regulatory Commission ("FERC") policies, NYISO monitors a network of more than 10,612 miles of high-voltage transmission lines and serves approximately 230 market participants.

NYISO's principal objective is to ensure the reliable, safe and efficient operation of the New York State transmission system and to administer an open, competitive and nondiscriminatory wholesale market for electricity in New York State. NYISO facilitates fair and open competition in the wholesale power market and creates an electricity commodity market in which power is purchased and sold on the basis of competitive bidding. NYISO utilizes a bid process for electricity and transmission usage, which enables New York State's utilities and other market participants, to offer electricity at competitive prices, rather than regulated rates. Billing invoices are issued to each market participant by NYISO each month to settle transactions occurring in the previous month.

NYISO is governed by an independent board of directors as well as a committee structure consisting of market participant representatives. In addition to FERC oversight, NYISO is also subject to regulation in certain aspects by the New York State Department of Public Service.

Basis of Accounting - The accompanying financial statements have been prepared on an accrual basis of accounting in accordance with accounting principles generally accepted in the United States.

Regulation - NYISO's financial statements are prepared in accordance with generally accepted accounting principles for rate-regulated entities. Statement of Financial Accounting Standards ("SFAS") No. 71, *Accounting for the Effects of Certain Types of Regulation*, requires an entity that is rate regulated on a cost-of-service basis, to recognize regulatory assets and liabilities for amounts, which would otherwise be included in earnings, when authorized to do so.

Revenue Recognition - Monthly settlements of market participants' energy transactions are not reflected in NYISO's Statement of Activities since they do not represent revenues or expenses of NYISO as NYISO merely acts as an intermediary in the settlement process. In this role, NYISO receives and disburses funds to/from market participants in the month following the month transactions occurred. See Note 15 for a summary of transactional volumes occurring in 2003 and 2002.

NYISO's two FERC-approved tariffs, the Open Access Transmission Tariff ("OATT") and the Market Administration and Control Area Services Tariff ("Services Tariff"), allow recovery of NYISO's operating expenses through a surcharge assessed to market participants. The revenue from this surcharge, Rate Schedule 1, is earned when energy is scheduled and dispatched. Market participants are then billed for such charges in the subsequent month.

Cash Equivalents - NYISO considers short-term marketable securities with original maturities of three months or less to be cash equivalents. The cash equivalents at December 31, 2003 and 2002 were held in short-term United States government obligations. NYISO's cash and cash equivalents consist primarily of funds accumulated for the working capital reserve and for general operating purposes.

Restricted Cash - Restricted cash consists primarily of market participant security deposits held in escrow accounts, amounts prepaid by market participants in advance of settlements billing dates, amounts retained by NYISO pursuant to setoff, amounts due to market participants for overcollections on the voltage market, and amounts reserved for funding employee benefit plans.

Other Assets - Other assets consist primarily of the intangible asset on NYISO's pension plan, the fair value of securities held by the Trust Share Option Agreement, the fair value of an interest rate cap agreement, and other deferred charges.

Property, Equipment and Capital Leases - Property and equipment are recorded at cost. NYISO capitalizes property and equipment additions in excess of $1,000 with a useful life greater than one year. Depreciation is computed on the straight-line method over the assets' estimated useful lives of three to five years. Building improvements are depreciated on a straight-line basis over forty years. When assets are retired or otherwise disposed of, the cost and related depreciation are removed, and any resulting gain or loss is reflected in income for the period. Repairs and maintenance costs are charged to expense when incurred.

In accordance with Statement of Position 98-1, *Accounting for Costs of Computer Software Developed or Obtained for Internal Use*, labor, overhead, interest, consulting and related costs incurred to acquire and develop computer software for internal use are capitalized and amortized using the straight-line method over three years. Costs incurred prior to the determination of feasibility of developed software and following the in-service date of developed software are expensed.

Capital lease obligations are recorded at the present value of future minimum lease payments. Assets under capital leases are amortized on the straight-line method over the life of the leases, which approximates their useful lives of three to five years.

Long-lived assets are recorded at cost, and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. Management is not aware of any events or changes in circumstances that would necessitate a review of any long-lived assets as of the years ending December 31, 2003 or 2002.

Working Capital Reserve - In order to maintain the liquidity and stability of NYISO's markets, NYISO has accumulated a working capital fund through amounts charged to market participants under Rate Schedule 1. Any additional working capital needs would be billed to market participants in future Rate Schedule 1 charges.

Deferred Revenue - Amounts collected from market participants through Rate Schedule 1 for capital expenditures are deferred and recognized over the depreciable period of the assets' lives. Such amounts are included in deferred revenue - long term.

Amounts received from certain market participants who do not provide an alternate form of financial assurance and must prepay their obligations to NYISO in advance of settlements billing dates, and amounts retained by NYISO pursuant to setoff are recorded as deferred revenue.

Fees for participation in NYISO's governance process are billed to market participants in advance of the year for which they apply and are amortized over the related governance period.

Income Taxes - NYISO is not subject to income taxes because it is operating as a corporation described in Section 501(c)(3) of the Internal Revenue Code, exempt under Section 501(a) of the Internal Revenue Code.

Fair Value of Financial Instruments - The carrying amount of current assets and liabilities, and long-term debt approximates their fair values. See additional details in Note 7.

Concentration of Credit Risk - Financial instruments that subject NYISO to credit risk consist primarily of accounts receivable billings due from market participants. As provided in the OATT and Services Tariff, market participants are required to either maintain approved credit ratings, to post specified financial security in an amount sufficient to cover their outstanding liability to NYISO, or to prepay their obligations in advance of settlement billing dates. NYISO also mitigates credit risk by procuring credit insurance on receivables for certain market participants.

NYISO's tariffs establish specific periods for the adjustment of settlement invoices as originally billed and for challenges to amounts billed for a particular service month. Subsequent invoices issued during the settlement adjustment period "true up" amounts previously billed. After all true-up invoices are issued during the settlement adjustment period, market participants may challenge the amounts billed for a particular service month. If NYISO agrees with the provisions of the challenge, a final invoice is issued for that service month. As a result, NYISO is exposed to credit risk until all settlement adjustment and final invoices for each service month are finalized and liquidated. However, Rate Schedule 1 of the OATT allows NYISO to recover bad debt losses from remaining market participants in future billings.

For original invoices issued prior to October 2002, settlement invoices may be adjusted up to two years after the date of original issuance, and these invoices may be challenged for an additional one year after the issuance of all settlement adjustment invoices. Effective with the October 2002 settlement invoice, these periods were shortened to one year for adjustments and four months for invoice challenges.

Use of Estimates - Accounting principles generally accepted in the United States of America require management to make estimates and assumptions that affect 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 reporting period. Actual results could differ from those estimates.

Reclassifications - Certain reclassifications of prior period data have been made to conform with the current year presentation.

Derivative Financial Instruments - NYISO records derivative financial instruments in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("SFAS No. 133"). SFAS No. 133 requires that all derivative financial instruments be recognized as either assets or liabilities, measured at fair value. The accounting for changes in fair value of derivatives (i.e. gains and losses) depends on the intended use of the derivative and the corresponding designation. The fair values of NYISO's derivative instruments are quoted by an external source. The changes in the fair value of these derivatives qualify as cash flow hedges and are recorded as interest expense. Due to NYISO's regulated rates, the offset to the changes in fair value of these derivatives is recorded as other assets. See additional details in Note 7.

Recently Issued Accounting Pronouncements - Effective January 1, 2003, NYISO adopted SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* ("SFAS No. 146"), which requires that a liability for costs associated with an exit or disposal activity be recognized when the liability is incurred, rather than at the date of a commitment to an exit or disposal plan. The adoption of SFAS No. 146 had no effect on NYISO's statement of position or results of operations.

In April 2003, the FASB issued SFAS No. 149, *Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities* ("SFAS No. 149"), which amends and clarifies accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS No. 133. The adoption of SFAS No. 149 had no effect on NYISO's statement of position or results of operations.

In December 2003, the FASB revised SFAS No. 132, *Employers' Disclosures About Pensions and Other Postretirement Benefits*, by requiring additional plan disclosures, such as listing plan assets by category, investment strategies and assumptions, estimated future contributions, cash flows, and measurement dates. Nonpublic companies are required to provide such additional disclosures for fiscal years ending after June 15, 2004. NYISO will adopt this pronouncement effective January 1, 2004. The adoption of the revisions to SFAS 132 is not expected to have any effect on NYISO's statement of position or results of operations.

In January 2004, the FASB issued FSP 106-1, which allows a one-time deferral of the recognition of the effects of the Medicare Prescription Drug Act in regard to benefit plan accounting and disclosures. NYISO has elected the one-time deferral, which will remain in effect until authoritative guidance is issued on accounting for the federal subsidy.

2. ACCOUNTS RECEIVABLE

NYISO's accounts receivable at December 31, 2003 and 2002 consisted of the following:

	2003	2002
Billed:		
Past due settlement invoices	**$ 11,378,143**	$ 11,390,024
Miscellaneous billings	**152,821**	401,380
Reserve for doubtful accounts - past due settlement invoices	**(11,377,080)**	(11,305,465)
	$ 153,884	$ 485,939
Unbilled:		
Operating expenses for December	**$ 10,414,258**	$ 9,212,091
Other unbilled receivables	**3,232,339**	10,675,327
Bad debt loss recoverable from market participants	**9,689**	11,305,465
	$ 13,656,286	$ 31,192,883
Total	**$ 13,810,170**	$ 31,678,822

Rate Schedule 1 of the OATT allows NYISO to recover bad debt losses from market participants and provides guidance on the provisions of such recoveries. NYISO's reserve for doubtful accounts at December 31, 2003 and 2002, respectively, results primarily from past due settlement invoices related to two subsidiaries of Enron Corporation. As of December 31, 2003, NYISO recorded an unbilled receivable of $9,689 to reflect the residual amount recoverable from remaining market participants in connection with such bad debt losses.

Other unbilled receivables relate to payments made by NYISO out of the working capital reserve primarily for timing differences on the recovery of certain transmission service agreements. These unbilled receivables are recoverable from market participants via future Rate Schedule 1 charges.

NYISO recovers its operating expenses via Rate Schedule 1 in the month following the month of service. Therefore, the unbilled operating expenses for December are billed and recovered in January of the subsequent year.

3. REGULATORY TRANSITION ASSETS AND REGULATORY ASSETS

NYISO's regulatory transition asset represents costs incurred and paid by the member companies of the NYPP to prepare NYISO for initial operations. In accordance with NYISO's tariffs, such costs are recovered from market participants through Rate Schedule 1 over a five-year period, and are amortized over such same period, beginning in January 2000.

At December 31, 2003 and 2002, the regulatory transition asset was comprised of:

	2003	2002
Computer and software development	**$ 24,363,819**	$ 24,363,819
Administrative and organizational development	**29,356,643**	29,356,643
Power control center building and land	**1,221,982**	1,221,982
	54,942,444	54,942,444
Accumulated amortization	**(43,953,955)**	(32,965,466)
Regulatory transition asset, net	**$ 10,988,489**	$ 21,976,978

Certain amounts recovered under NYISO's ratemaking mechanisms are based on estimates. The difference between actual results and estimates that result in under collections are reflected as regulatory assets due from market participants. NYISO's regulatory assets represent amounts to be recovered in future periods for repayment of debt incurred to fund budgetary needs through December 31, 2003 and 2002, respectively.

4. PROPERTY AND EQUIPMENT

Property and equipment, which includes capitalized interest of $211,351, at December 31, 2003 and 2002 consisted of the following:

	2003	2002
Computer hardware, software and accessories	**$ 55,554,092**	$ 24,477,631
Software developed for internal use	**20,905,911**	7,357,655
Assets under capital leases	**-**	3,636,205
Building and leasehold improvements	**2,966,071**	1,187,065
Furniture and fixtures	**2,165,383**	1,521,742
Machinery and equipment	**1,479,052**	1,271,117
Work in progress	**19,878,914**	5,885,981
	102,949,423	45,337,396
Accumulated depreciation and amortization	**(33,355,765)**	(15,788,326)
Property and equipment, net	**$ 69,593,658**	$ 29,549,070

5. SHORT-TERM DEBT

NYISO has a $50 million Revolving Credit Facility that expires on October 26, 2005. The proceeds from this facility are to be used for working capital purposes. Interest on borrowings under this agreement is based on NYISO's option of varying rates of interest tied to either the prime rate or the London Interbank Offering Rate ("LIBOR"). At December 31, 2003 and 2002, respectively, there were no amounts outstanding on the Revolving Credit Facility.

6. LONG-TERM DEBT

On September 8, 2000, NYISO borrowed $48,460,444 under a Term Credit Loan to reimburse NYPP member companies for their investment in the transition of the NYPP to the NYISO, and for the purchase of certain NYPP assets. Principal and interest payments are due monthly until December 2004. Under the Term Credit Loan, interest is variable based on the 30-day LIBOR plus 125 basis points. The interest rate on the Term Credit Loan at December 31, 2003 and 2002 was 2.42% and 2.63%, respectively. In January 2001, NYISO entered into an interest rate swap agreement on the Term Credit Loan, which fixed the interest rate on this loan at 6.99%. See additional information in Note 7.

On November 1, 2001, NYISO entered into a $6.5 million line of credit facility to be utilized for the purchase of information technology equipment. This facility was subsequently increased to $10.5 million on November 8, 2002. By December 31, 2002, the entire $10.5 million on this line of credit facility was drawn and converted into Equipment Term Notes with principal and interest payable over three years. Interest on borrowings under this facility is based on NYISO's option of varying rates of interest tied to either LIBOR plus 125 basis points or the prime rate. At December 31, 2003 and 2002, the interest rate on the Equipment Term Notes ranged from 2.37% to 2.44% and 2.63% to 2.69%, respectively. Computer hardware, software and accessories with a book value of $10.5 million were pledged as collateral for the Equipment Term Notes.

On February 13, 2003, NYISO entered into a $59.3 million unsecured line of credit facility, the proceeds of which may be drawn until February 29, 2004 to fund the 2003 development of significant information technology projects. Principal repayment of borrowings under this 2003 Budget Facility Loan will be made over four years, beginning in March 2004. Interest on borrowings under this facility is based on NYISO's option of varying rates of interest tied to either LIBOR plus 137.5 basis points or the prime rate. Interest payments on borrowings during the draw period are due according to the LIBOR period chosen or quarterly for prime, and monthly thereafter. At December 31, 2003, NYISO borrowed $47.0 million on this facility, with interest rates on these borrowings ranging from 2.53% to 2.55%. On December 19, 2003, NYISO entered into an interest rate cap agreement on this debt, effective January 2, 2004, which caps the maximum interest rate at 5.375%. See additional information in Note 7.

At December 31, 2003, the following amounts were outstanding on the Long-Term Debt:

	Term Credit Loan	Equipment Term Notes	2003 Budget Facility Loan	Total
Outstanding balance	$ 12,656,961	$ 5,833,334	$ 47,000,000	$ 65,490,295
Less: Current portion	12,656,961	3,450,000	9,791,667	25,898,628
Long-term portion	$ -	$ 2,383,334	$ 37,208,333	$ 39,591,667

At December 31, 2003, scheduled maturities of Long-Term Debt are as follows:

	Term Credit Loan	Equipment Term Notes	2003 Budget Facility Loan	Total
2004	$ 12,656,961	$ 3,450,000	$ 9,791,667	$ 25,898,628
2005	-	2,383,334	11,750,000	14,133,334
2006	-	-	11,750,000	11,750,000
2007	-	-	11,750,000	11,750,000
2008	-	-	1,958,333	1,958,333
Total	$ 12,656,961	$ 5,833,334	$ 47,000,000	$ 65,490,295

7. DERIVATIVES AND HEDGING ACTIVITIES

In January 2001, NYISO entered into an interest rate swap agreement with a commercial bank to fix interest payments on its Term Credit Loan. The notional amount of the swap on the date of the agreement was $45,157,860. Under the swap agreement, NYISO pays a fixed interest rate of 6.99% on the outstanding principal amount of the Term Credit Loan on payments from February 2001 through December 2004. As of December 31, 2003 and 2002, the fair value of the interest rate swap was $313,811 and $1,096,388, respectively. For the years ended December 31, 2003 and 2002, NYISO recorded revenue of $782,577 and $250,806, respectively, related to this derivative instrument.

In December 2003, NYISO entered into an interest rate cap agreement with a commercial bank to cap interest payments at 5.375% on its 2003 Budget Facility Loan. The notional amount of the debt on the date of the cap agreement was $47,000,000. Under the cap agreement, NYISO pays a variable interest rate tied to LIBOR on the outstanding principal amount of the 2003 Budget Facility Loan from January 2004 through February 2008; however, this variable interest rate cannot exceed 5.375%. As of December 31, 2003, the fair value of the interest rate cap was $414,405. For the year ended December 31, 2003, NYISO recorded revenue of $56,405 related to this derivative instrument.

NYISO is exposed to credit loss in the event of nonperformance by the commercial bank under the swap or cap agreements. However, NYISO does not anticipate nonperformance by the commercial bank.

8. EMPLOYEE BENEFIT PLANS

Pension Plans - NYISO has a defined benefit pension plan covering substantially all employees. Plan benefits are based on employee compensation levels and years of service, including service for certain employees previously employed by an NYPP member company. Employees become vested in pension benefits after five years of credited service.

NYISO also has an unfunded nonqualified pension plan to provide employees with the full level of benefits as stated in the qualified plan without reductions due to various limitations imposed by the provisions of federal income tax laws and regulations.

NYISO expects to contribute $2.0M to the pension plan for 2004.

The schedules that follow show the benefit obligations, the plan assets, and the funded status as of December 31, 2003 and 2002, and the change in benefit obligations and the components of net periodic cost for NYISO's pension plans for the years ended December 31, 2003 and 2002.

For the year ended December 31,	2003	2002
Change in benefit obligation:		
Benefit obligation, beginning of year	**$ 10,353,083**	$ 7,509,131
Service cost	**1,520,613**	1,213,271
Interest cost	**684,055**	553,360
Actuarial loss	**108,272**	1,077,321
Benefits paid	**(15,488)**	-
Benefit obligation, end of year	**$ 12,650,535**	$ 10,353,083
Change in plan assets:		
Fair value of plan assets, beginning of year	**$ 5,094,395**	$ 3,570,159
Actual return on plan assets	**1,335,622**	(302,808)
Employer contributions	**1,966,515**	1,868,638
Benefits paid	**(15,488)**	-
Expenses paid	**(16,956)**	(41,594)
Fair value of plan assets, end of year	**$ 8,364,088**	$ 5,094,395
Funded status	**$ (4,286,447)**	$ (5,258,688)
Unrecognized prior service cost	**2,374,785**	2,846,089
Unrecognized loss	**2,550,763**	3,192,478
Additional minimum pension cost	**(1,301,347)**	(2,039,973)
Total accrued liability	**$ (662,246)**	$ (1,260,094)

Amounts recognized in the Statement of Financial Position consist of:

	2003	2002
Benefit obligation	**$ (662,246)**	$ (1,260,094)
Intangible asset	**1,270,841**	2,039,973
The components of net periodic pension cost are as follows:		
Service cost	**$ 1,520,613**	$ 1,213,271
Interest cost	**684,055**	553,360
Expected return on plan assets	**(522,418)**	(402,303)
Amortization of unrecognized prior service cost	**295,326**	295,326
Amortization of unrecognized loss	**129,717**	53,453
Total	**$ 2,107,293**	$ 1,713,107

The following table shows the assumptions used to calculate the pension benefit obligations and net periodic costs as of December 31, 2003 and 2002:

	2003	2002
Benefit obligations:		
Discount rate	**6.25%**	6.50%
Rate of compensation increases	**5.06%**	5.56%
Net cost or credit:		
Discount rate	**6.50%**	7.25%
Rate of compensation increases	**5.56%**	5.56%
Expected return on plan assets	**8.00%**	9.00%

The targeted allocation and actual investment mix of the pension plan's assets are as follows:

	Target Allocation	December 31, 2003	2002
Equity securities	**60%**	**63%**	59%
Fixed income	**40%**	**37%**	41%
Total	**100%**	**100%**	100%

Postretirement Plan - NYISO committed to sponsor a defined benefit postretirement plan to provide medical and life insurance benefits for eligible retirees and their dependents. The terms of the plan were finalized during 2003. Substantially all employees who retire from NYISO become eligible for these benefits provided they have been credited with at least five years of NYISO service. The benefits are contributory based upon years of service, with NYISO paying up to 50% of costs for retired employees and up to 25% for their dependents (subject to specified dollar limits). Medical coverage becomes secondary upon Medicare eligibility and life insurance coverage is reduced upon reaching age 65. Prior to 2003, amounts recovered through Rate Schedule 1 for estimated costs before the plan coverage and terms were finalized were classified as regulatory liabilities. At December 2003 the plan has been finalized, but not funded and the estimated benefit obligations are recorded as a noncurrent liability. See additional information on Regulatory Liabilities in Note 12.

Amounts recognized in the Statement of Financial Position at December 31, 2003 consist of:

	2003
Benefit obligations as of fiscal year end	**$ 2,161,503**
Fair value of plan assets at fiscal year end	-
Funded Status	**$ (2,161,503)**
Accrued benefit cost recognized in balance sheet	**$ (2,161,503)**

Weighted-average rate assumptions:	
Discount rate	6.25%
Expected return on plan assets	N/A
Accrued benefit	$ 543,312

The assumed health care cost trend rates for the postretirement plan are 11% for 2004, decreasing to 4.5% in 2010. A one percentage point change in the assumed health care cost trend rate would change the 2003 postretirement benefit obligation as follows:

	1% increase	1% decrease
Effect on postretirement benefit obligation	$14,000	($19,000)

401(k) Plan - NYISO has a 401(k) Retirement and Savings Plan open to all nontemporary employees. This plan provides for employee contributions up to specified limits. NYISO matches 100% of the first 3% of employee contributions, and 50% of the next 2% of employee contributions. Employees are immediately vested in NYISO's matching contributions, which were $975,066 and $849,523 for 2003 and 2002, respectively.

Long Term Incentive Plan – NYISO's Long Term Incentive Plan provides certain members of senior management with deferred compensation benefits. Benefits are based upon the achievement of three-year performance goals established by the Board of Directors, with participants becoming fully vested in these deferred amounts after the completion of the third year. For the first three performance cycles (2000-2002, 2001-2003 and 2002-2004) annual distributions are payable in the year following completion of the cycle. In 2005, there will be a one-year performance cycle, payable in 2006. After 2005, distributions will be payable after the completion of each three-year cycle. Accrued Long Term Incentive Plan benefits included in Other Noncurrent Liabilities at December 31, 2003 and 2002, respectively, were $392,910 and $595,067. The short-term portion of such liability at December 31, 2003 and 2002, respectively were $565,315 and $507,333.

Trust Share Option Agreement - NYISO has entered into a nonqualified share option agreement with a key officer whereby NYISO has granted to such officer the right to acquire debt and equity securities held by NYISO in a trust for an amount equal to 25% of the fair value of such securities. The options are immediately vested and are subject to certain restrictions of transferability. At December 31, 2003 and 2002, respectively, the fair market value of securities held by the trust was $743,065 and $646,003. Options outstanding at December 31, 2003 expire from November 16, 2009 through February 19, 2012. NYISO records compensation expense for 75% of the fair value of the options granted at the date of grant. A corresponding liability is established until such time as the options are exercised. No options were exercised as of December 31, 2003.

9. LEASE COMMITMENTS

Operating Leases - NYISO has obligations under three operating lease agreements primarily for rental of office space. One lease agreement for property in Altamont, NY, expires in February 2006. Another lease agreement for property in Albany, NY, expires in January 2006. NYISO has the option to renew both leases for two additional five-year periods at the current lease rate. The third lease was entered into in February 2003 for facilities in Albany, NY, and is cancelable after April 2006.

Rent expense related to these leases amounted to $925,392 and $727,144 in 2003 and 2002, respectively. The future minimum lease payments under these operating leases at December 31, 2003 are as follows:

2004	$ 1,032,394
2005	1,032,394
2006	181,372
Total	$ 2,246,160

Capital Leases - Certain lease obligations assumed from NYPP for computers, furniture and fixtures include provisions, which at the termination of the lease, either transfer ownership of the leased property to NYISO or allow NYISO the option to purchase the leased equipment for a nominal cost. Accordingly, the cost of these agreements has been recorded as capital leases. At December 31, 2003, there were no amounts outstanding under these capital lease obligations.

10. WORKING CAPITAL RESERVE

At December 31, 2003 and 2002, the working capital reserve consisted of:

	2003	2002
Market participant contributions through Rate Schedule 1	**$ 46,451,950**	$ 46,446,627
Interest on market participant contributions	**2,333,945**	1,975,832
Total	**$ 48,785,895**	$ 48,422,459

Market participants are entitled to interest on their principal contributions to the working capital reserve. Each market participant is allocated interest based on the ratio share of each market participant's principal contributions to the total working capital fund.

11. DEFERRED REVENUE

Deferred revenue at December 31, 2003 and 2002 consisted of the following:

	2003	2002
Amounts collected through Rate Schedule 1 for capital expenditures, net	**$ 69,593,658**	$ 29,455,282
Prepayments received in advance of settlement dates	**15,962,630**	17,316,742
Amounts collected for insurance fund	**710,000**	-
Governance participation fees	**347,300**	347,300
Total	**86,613,588**	47,119,324
Less: current portion	**(39,783,261)**	(29,008,566)
Long-term portion	**$ 46,830,327**	$ 18,110,758

12. REGULATORY LIABILITIES

Certain amounts recovered under NYISO's rate-making mechanisms are based on estimates. The difference between actual results and estimates that result in over collections are reflected as regulatory liabilities due to market participants. At December 31, 2003 and 2002, respectively, NYISO recorded the following amounts as regulatory liabilities:

		2003		2002
Funding for deferred charges	**$**	**2,730,107**	$	929,870
Rate Schedule 1 underspending		**1,362,376**		2,860,236
Voltage (reactive power) market		**1,013,781**		3,347,106
Rate Schedule 1 load overcollections		**913,340**		1,960,134
Future funding of postretirement plan		-		2,704,815
Total		**6,019,604**		11,802,161
Less: current portion		**(3,289,497)**		(8,167,476)
Long-term portion	**$**	**2,730,107**	$	3,634,685

13. COMMITMENTS AND CONTINGENCIES

NYISO is routinely involved in regulatory actions. In the opinion of management, none of these matters will have a material adverse effect on the financial position, result of operations or liquidity of NYISO.

The most significant legal proceeding affecting NYISO is a civil suit, filed by New York State Electric and Gas, seeking recovery of $6.6 million in compensatory damages and unspecified punitive damages, associated with alleged excessive payments for reserves of electricity during the period January to March 2000.

14. SUBSEQUENT EVENT

On March 17, 2004, NYISO entered into an unsecured $100 million line of credit facility, the proceeds of which may be drawn until December 2006 to fund the development of significant information technology projects during 2004-2006. NYISO has the option to convert borrowings under this facility up to three times to term loans, with principal repayments made over four years. Interest on borrowings under this facility is based on NYISO's option of varying rates of interest tied to either the prime rate or LIBOR. Interest payments on borrowings are due monthly.

15. MARKET ACTIVITY (UNAUDITED)

The following amounts represent the transactional volume of energy and energy-related products in NYISO's markets during the years ended December 31, 2003 and 2002 (in $ billions). There was no appreciable increase in volume of gigawatt hours.

		2003		2002
Energy	**$**	**6.1**	$	4.5
Installed capacity		**0.7**		0.6
Transmission congestion contracts		**0.2**		0.1
Total	**$**	**7.0**	$	5.2