Management Certification

I certify that:

1. I have reviewed this report of the New York Independent System Operator, Inc. ("NYISO") for the year ended December 31, 2005;
2. Based on my knowledge, this report does not contain any untrue statements of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the NYISO as of, and for, the periods presented in this report;
4. The NYISO's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-(f)) for NYISO and have:
   a. *Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the NYISO is made known to us by others within the NYISO, particularly during the period in which this report is being prepared;*
   b. *Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;*
   c. *Evaluated the effectiveness of the NYISO's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and*
   d. *Disclosed in this report any change in the NYISO's internal control over financial reporting that occurred during the NYISO's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the NYISO's internal control over financial reporting; and*
5. The NYISO's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the NYISO's auditors and the audit committee of NYISO's board of directors (or persons performing the equivalent functions):
   a. *All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the NYISO's ability to record, process, summarize and report financial information; and*
   b. *Any fraud, whether or not material, that involves management or other employees who have a significant role in the NYISO's internal control over financial reporting.*

Date: March 31, 2006

Mark S Lynch

Mark S. Lynch
President & Chief Executive Officer

I certify that:

1. I have reviewed this report of the New York Independent System Operator, Inc. ("NYISO") for the year ended December 31, 2005;
2. Based on my knowledge, this report does not contain any untrue statements of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the NYISO as of, and for, the periods presented in this report;
4. The NYISO's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-(f)) for NYISO and have:
   a. *Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the NYISO is made known to us by others within the NYISO, particularly during the period in which this report is being prepared;*
   b. *Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;*
   c. *Evaluated the effectiveness of the NYISO's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and*
   d. *Disclosed in this report any change in the NYISO's internal control over financial reporting that occurred during the NYISO's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the NYISO's internal control over financial reporting; and*
5. The NYISO's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the NYISO's auditors and the audit committee of NYISO's board of directors (or persons performing the equivalent functions):
   a. *All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the NYISO's ability to record, process, summarize and report financial information; and*
   b. *Any fraud, whether or not material, that involves management or other employees who have a significant role in the NYISO's internal control over financial reporting.*

Date: March 31, 2006

Charles N Garber

Charles N. Garber
Vice President & Chief Financial Officer

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, 2005 and 2004, 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 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. 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, 2005 and 2004, 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

New York, New York

March 31, 2006

STATEMENTS OF FINANCIAL POSITION
AS OF DECEMBER 31, 2005 AND 2004

	2005	2004
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 58,180,363	$ 30,630,452
Restricted cash	252,878,234	193,275,340
Accounts receivable, net (Note 2)	12,454,894	15,130,434
Prepaid expenses	4,971,429	5,640,669
Regulatory assets - current portion (Note 3)	-	672,865
Other current assets	361,402	217,173
Total current assets	**328,846,322**	**245,566,933**
NONCURRENT ASSETS:		
Regulatory assets (Note 3)	12,240,143	17,007,859
Property and equipment, net (Note 4)	76,137,208	83,974,918
Other noncurrent assets (Note 1)	15,325,329	3,074,645
Total noncurrent assets	**103,702,680**	**104,057,422**
TOTAL	**$ 432,549,002**	**$ 349,624,355**
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	$ 15,535,507	$ 14,992,304
Market participant prepayments	86,975,384	19,078,241
Market participant security deposits	161,190,024	172,842,650
Long-term debt - current portion (Note 6)	26,780,525	22,250,000
Working capital reserve (Note 10)	49,700,136	46,908,875
Deferred revenue (Note 11)	5,084,117	1,708,203
Regulatory liabilities - current portion (Note 12)	17,514,159	2,057,582
Other current liabilities	595,834	545,709
Total current liabilities	**363,375,686**	**280,383,564**
NONCURRENT LIABILITIES:		
Accrued pension liability (Note 8)	2,168,365	530,675
Accrued postretirement liability (Note 8)	3,425,271	2,724,583
Regulatory liabilities (Note 12)	1,279,459	7,557,893
Other noncurrent liabilities (Note 8)	1,545,550	1,469,307
Long-term debt (Note 6)	60,754,671	56,958,333
Total noncurrent liabilities	**69,173,316**	**69,240,791**
COMMITMENTS AND CONTINGENCIES (Note 13)		
TOTAL	**$ 432,549,002**	**$ 349,624,355**

See notes to financial statements.

STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005	2004
REVENUES:		
Rate Schedule 1 tariff charge	$ 144,882,248	$ 135,620,291
Interest income	2,121,390	254,473
Lease income (Note 9)	1,215,882	-
Fees and services	951,341	786,831
Total revenues	**149,170,861**	**136,661,595**
OPERATING EXPENSES:		
Compensation and related benefits (Note 8)	45,693,068	37,735,650
Depreciation and amortization	35,856,529	24,375,869
Professional fees and consultants	26,327,352	26,999,485
Rent, equipment leases and other facility costs	17,476,454	15,680,042
Federal Energy Regulatory Commission fees	8,893,682	5,311,674
Telecommunications	4,642,278	4,525,625
Administrative and other expenses	2,981,482	4,477,103
Training, travel and meeting expenses	2,459,472	2,635,422
Northeast Power Coordinating Council fees	1,689,802	1,506,734
Amortization of regulatory transition asset	-	10,988,489
Total operating expenses	**146,020,119**	**134,236,093**
INTEREST EXPENSE—Net	**$ 3,150,742**	**$ 2,425,502**
NET RESULTS OF ACTIVITIES	**$ -**	**$ -**

See notes to financial statements.

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005	2004
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	35,856,530	24,375,869
Amortization of regulatory transition asset	-	10,988,489
Loss on disposal of fixed asset	45,917	47,874
Change in operating assets and liabilities:		
Decrease (increase) in accounts receivable and prepaid expenses	3,344,779	(543,257)
Decrease (increase) in regulatory assets	5,440,582	(17,680,725)
(Increase) in other assets	(12,394,913)	(606,103)
(Decrease) increase in accounts payable and accrued expenses	(692,821)	2,851,137
Increase in market participant prepayments	67,897,143	3,115,711
(Decrease) in market participant security deposits	(11,652,627)	(14,510,430)
Increase (decrease) in working capital reserve	2,791,261	(1,877,020)
Increase (decrease) in deferred revenue and other liabilities	15,018,804	(11,896,463)
Net cash provided by (used in) operating activities	**105,654,655**	**(5,734,918)**
CASH FLOWS FROM INVESTING ACTIVITIES:		
(Increase) decrease in restricted cash	(59,602,894)	10,753,351
Acquisition of property and equipment (including capitalized interest)	(26,828,713)	(43,475,593)
Net cash used in investing activities	**(86,431,607)**	**(32,722,242)**
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from mortgage	14,708,750	-
Proceeds from 2004 - 2006 budget facility loan	18,000,000	42,000,000
Repayment of term credit loan	-	(12,656,961)
Repayment of mortgage	(2,131,887)	-
Repayment of 2004 - 2006 budget facility loan	(10,500,000)	-
Repayment of 2003 budget facility loan	(11,750,000)	(9,791,667)
Repayment of equipment term notes	-	(5,833,333)
Net cash provided by financing activities	**8,326,863**	**13,718,039**
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	27,549,911	(24,739,121)
CASH AND CASH EQUIVALENTS—Beginning of year	30,630,452	55,369,573
CASH AND CASH EQUIVALENTS—End of year	$ 58,180,363	$ 30,630,452
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION—Cash paid during the year for interest	$ 3,534,937	$ 1,914,949
NONCASH INVESTING ACTIVITIES:		
Property and equipment additions which were accrued but not paid	$ 2,024,733	$ 788,709
Property and equipment additions previously accrued which were paid	$ 788,709	$ 5,459,300

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2005 AND 2004

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 State'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 10,775 miles of high-voltage transmission lines and serves approximately 300 market participants.

NYISO's principal objectives are 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 of America.

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 Statements 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 14 for an unaudited summary of transactional volumes occurring in 2005 and 2004.

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 capital requirements and 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.

NYISO's Rate Schedule 1 includes a timing mechanism that effectively meets the requirements of an alternative revenue program set forth in Financial Accounting Standards Board's Emerging Issues Task Force Issue No. 92-7, *Accounting by Rate Regulated Utilities for the Effects of Certain Alternative Revenue Programs*. Accordingly, revenue is recognized for net financing obligations and capital costs incurred during the reporting period based on the revenue requirement formula in the tariffs. NYISO has recorded an Other Noncurrent Asset of $11,397,988 in the accompanying 2005 Statement of Financial Position in connection with this rate-making recovery mechanism.

Cash and 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, 2005 and 2004 were held in money market accounts invested primarily in short term United States government obligations. NYISO's cash and cash equivalents consist primarily of funds accumulated for the working capital reserve, amounts due to market participants for overcollections on the voltage market, amounts for funding employee benefit plans, 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, and amounts retained by NYISO pursuant to setoff agreements.

Other Assets — Other assets consist primarily of timing differences on certain rate making recoveries, the intangible asset related to NYISO's pension plan, the fair value of securities held by the Trust Share Option Agreement, the fair value of interest rate cap and swap agreements, and other deferred charges.

Property and Equipment — Property and equipment are recorded at cost. NYISO capitalizes property and equipment additions in excess of $5,000 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, except for building and building improvements, which are depreciated on a straight-line basis over twenty 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 expense 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.

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 ended December 31, 2005 and 2004.

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

Market Participant Prepayments — 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 agreements with bankrupt market participants are recorded as market participant prepayments.

Deferred Revenue — Advance payments from developers for interconnection studies, security deposits and advance rental billings from a tenant leasing office space from NYISO are reflected 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. All such unamortized amounts are included in deferred revenue.

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. NYISO is also exempt from paying New York State income tax or sales tax.

Fair Value of Financial Instruments — The carrying amounts of current assets and liabilities, and long-term debt approximate 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 and Rate Schedule 1 revenue due from market participants. As provided in the OATT and Services Tariff, NYISO reviews the creditworthiness of market participants, who are required to either maintain certain financial statement criteria and/or 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'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. NYISO accrued in accounts payable and accrued expenses amounts related to capital purchases incurred but not yet paid. In prior periods, amounts accrued but not yet paid were classified in the Statement of Cash Flows as cash flows from investing activities and the corresponding change in the related accounts payable as cash flows from operating activities. In 2005, NYISO revised its accounting policy to exclude accrued capital purchases from cash flows from investing and operating activities. Accrued capital purchases were $2,024,733 and $788,709 at December 31, 2005 and 2004, respectively. NYISO revised its 2004 Statement of Cash Flows to conform to this change. As a result, cash flows provided by operating activities and cash flows used in investing activities increased by $4,670,591. NYISO has also reclassified certain amounts previously reported as restricted cash to cash in the accompanying Statement of Financial Position at December 31, 2004, and the Statement of Cash Flows for the period then ended. This reclassification did not have an impact on total current assets.

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 external sources. 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.

2. ACCOUNTS RECEIVABLE

NYISO's accounts receivable at December 31, 2005 and 2004 consisted of the following:

	2005	2004
Billed:		
Past due settlement invoices	$ 9,042,114	$ 12,669,299
Miscellaneous billed receivables	130,822	137,575
Reserve for doubtful accounts—past due settlement invoices	(8,964,782)	(11,410,191)
	208,154	1,396,683
Unbilled:		
Operating expenses for December	11,839,170	10,779,613
Bad debt losses recoverable from market participants	356,997	42,800
Miscellaneous unbilled receivables	41,067	80,000
Replenishments of working capital reserve	9,506	2,831,338
	12,246,740	13,733,751
Total	**$ 12,454,894**	**$ 15,130,434**

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, 2005 and 2004 results primarily from past due settlement invoices related to two subsidiaries of Enron Corporation. The bad debt losses were recovered from market participants in accordance with the OATT and any amounts recovered from the Enron bankruptcy proceedings are refundable to these market participants. During 2005, NYISO recovered $2,759,606 from claims entered in the Enron bankruptcy process. This recovery amount will be refunded to market participants in 2006 and is reflected as a current Regulatory Liability on the 2005 Statement of Financial Position. Additional recoveries, which cannot yet be quantified, are expected and will also be refunded to market participants. As of December 31, 2005 and 2004, NYISO recorded unbilled receivables of $356,997 and $42,800, respectively, to reflect amounts yet to be recovered from remaining market participants in connection with other bad debt losses.

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.

Unbilled replenishments of working capital reserve relate to amounts recoverable from market participants via future Rate Schedule 1 charges to recover amounts temporarily utilized by NYISO out of the working capital reserve.

3. REGULATORY TRANSITION ASSET 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 were recovered from market participants through Rate Schedule 1 over a five-year period ended December 31, 2004 and were amortized over such same period.

At December 31, 2004, the regulatory transition asset was comprised of:

	2004
Computer and software development	$ 24,363,819
Administrative and organizational development	29,356,643
Power control center building and land	1,221,982
	54,942,444
Accumulated amortization	(54,942,444)
Regulatory transition asset—net	$ -

At December 31, 2005 and 2004, regulatory assets were comprised of:

	2005	2004
Replenishment of working capital reserve	$ 12,240,143	$ 17,007,859
Voltage support service (reactive power) market	-	672,865
Total	12,240,143	17,680,724
Less: current portion	-	(672,865)
Long-term portion	$ 12,240,143	$ 17,007,859

During 2004, NYISO entered into a settlement agreement with its market participants to resolve a billing issue in NYISO's Transmission Congestion Contracts market. As of December 31, 2005 and 2004, respectively, NYISO's working capital fund has been temporarily depleted by $12,240,143 and $17,007,859, respectively, as a result of this settlement. NYISO is replenishing this temporary draw on the working capital reserve via a FERC-approved surcharge assessed to certain future transmission congestion contracts. The timing of the replenishments via this surcharge is dependent upon the amount and timing of activity in the transmission congestion contracts market. Remaining future replenishments are reflected as regulatory assets due from market participants.

In order to maintain acceptable transmission voltages on the New York State transmission system, certain market participants within the New York Control Area produce or absorb voltage support service (reactive power). Payments to market participants supplying voltage support service and recoveries from other market participants are assessed via Rate Schedule 2 of the OATT and Services Tariff. Differences between the timing of recoveries and payments for voltage support service that result in undercollections are reflected as regulatory assets. At December 31, 2005 and 2004, respectively, NYISO recognized a regulatory liability of $3,679,480 (see Note 12) and a regulatory asset of $672,865 related to such timing differences.

4. PROPERTY AND EQUIPMENT

Property and equipment includes interest of $82,735 and $292,451 capitalized during 2005 and 2004, respectively. As of December 31, property and equipment consisted of the following:

	2005	2004
Software developed for internal use	$ 67,971,366	$ 23,211,744
Computer hardware and software	64,068,880	61,280,053
Building, building improvements and leasehold improvements	21,355,624	6,201,420
Machinery and equipment	3,655,452	2,430,011
Furniture and fixtures	2,630,143	2,246,494
Land and land improvements	2,007,904	-
Work in progress	4,497,723	45,002,844
	166,187,092	140,372,566
Accumulated depreciation and amortization	(90,049,884)	(56,397,648)
Property and equipment—net	$ 76,137,208	$ 83,974,918

5. SHORT-TERM DEBT

At December 31, 2004, NYISO had a $50 million Revolving Credit Facility that was due to expire on October 26, 2005. On July 21, 2005, NYISO replaced the existing Revolving Credit Facility with a new $50 million Revolving Credit Facility that expires on July 21, 2010. 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 Offer Rate ("LIBOR"). At December 31, 2005 and 2004, respectively, there were no amounts outstanding on the Revolving Credit Facility.

6. LONG-TERM DEBT

On September 8, 2000, NYISO borrowed $48.5 million 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 were due monthly until December 2004, when the Term Credit Loan was fully repaid. Under this facility, interest was variable based on the 30-day LIBOR plus 125 basis points. However, 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%.

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 of this line of credit facility was drawn and converted into Equipment Term Notes with principal and interest payable over three years. Computer hardware and software with a book value of $10.5 million were pledged as collateral for the Equipment Term Notes. In December 2004, the Equipment Term Notes were fully repaid, with $2.4 million representing voluntary prepayments against this debt. All collateral liens for computer hardware and software associated with the Equipment Term Notes were removed in January 2005. Interest on borrowings under this facility was based on NYISO's option of varying rates of interest tied to either LIBOR plus 125 basis points or the prime rate.

On February 13, 2003, NYISO entered into a $59.3 million unsecured line of credit facility ("2003 Budget Facility"), the proceeds of which could be drawn until February 29, 2004 to fund the 2003 development of significant information technology projects. By December 31, 2003, $47.0 million was borrowed on the 2003 Budget Facility, with principal and interest payable over four years, beginning in March 2004. Interest on borrowings under this facility was based on NYISO's option of varying rates of interest tied to either LIBOR plus 137.5 basis points or the prime rate. On April 8, 2005, this loan was refinanced to lower the LIBOR interest rate spread from 137.5 basis points to 65.0 basis points. NYISO has also entered into an interest rate cap agreement on this debt, effective January 2, 2004, which capped the maximum interest rate at 5.375% (4.65% after April 8, 2005 refinancing). At December 31, 2005, the interest rates on these borrowings were at the 4.65% cap level whereas at December 31, 2004, interest rates ranged from 3.38% to 3.66%. See additional information in Note 7.

On March 17, 2004, NYISO entered into an unsecured $100.0 million line of credit facility ("2004 - 2006 Budget Facility"), the proceeds of which may be drawn until December 2006 to fund the development of significant information technology projects during 2004 through 2006. NYISO has the option to convert borrowings under this 2004 - 2006 Budget Facility up to three times to term loans, with principal repayments made over four years. Interest on borrowings under this facility is due monthly and was based on NYISO's option of varying rates of interest tied to either LIBOR plus 60 basis points (for borrowings during the draw period not yet converted to term loans) or 100 basis points (for borrowings converted to term loans) or the prime rate. On April 8, 2005, this facility was refinanced to lower the LIBOR interest rate spread to 52.5 basis points (for borrowings during the draw period) and 80 basis points (for borrowings converted to term loans). NYISO entered into interest rate cap agreements on $82.0 million of this debt, which caps the maximum interest rate at 4.60% for borrowings during the draw periods not yet converted to term loans (4.525% after April 8, 2005 refinancing) and 5.00% for borrowings converted to term loans (4.80% after April 8, 2005 refinancing). See additional information in Note 7.

At December 31, 2004, $42.0 million was drawn on the 2004—2006 Budget Facility, which was converted to a term loan in February 2005 with principal and interest payments payable over four years beginning in March 2005. At December 31, 2005, the interest rate on these borrowings was at the cap level of 4.80% whereas at December 31, 2004, the interest rate was 3.02%. During 2005, an additional $18.0 million was drawn on the 2004—2006 Budget Facility, which will be converted to a term loan in February 2006 with principal and interest payments payable over four years. At December 31, 2005, the interest rate on these borrowings was 4.525%.

On July 8, 2005, NYISO entered into two financing agreements to purchase and renovate a 140,000 square foot office building. The first agreement is a $14.7 million mortgage to finance the building purchase ("Mortgage"), and the second agreement represents a $10.0 million line of credit for renovations during an 18 month period, beginning in July 2005 ("Renovations Loan"). The Mortgage has principal and interest payments payable over 20 years, beginning September 2005. Principal and interest payments on borrowings made during the Renovations Loan draw period are payable over 20 years, beginning in January 2007. Both agreements are secured by liens on the building and subsequent capitalized renovations. Interest on borrowings under both facilities is due monthly and is based on NYISO's option of varying rates of interest tied to either LIBOR plus 100 basis points or the prime rate. On February 15, 2005, NYISO entered into an interest rate swap agreement on the Mortgage, which fixes the interest rate on this loan at 5.79%. On February 15, 2005, NYISO also entered into an interest rate swap agreement on the Renovations Loan, which fixes the interest rate on these borrowings at 5.96%, beginning on January 1, 2007. As of December 31, 2005, $14.7 million was borrowed on the Mortgage, and there were no draws on the Renovations Loan.

At December 31, 2005, the following amounts were outstanding on NYISO's Long-Term Debt:

	2003 Budget Facility Loan	2004-2006 Budget Facility Loan	Mortgage	Total
Outstanding balance	$25,458,334	$49,500,000	$12,576,862	$87,535,196
Less: current portion	(11,750,000)	(15,000,000)	(30,525)	(26,780,525)
Long-term portion	$13,708,334	$34,500,000	$12,546,337	$60,754,671

At December 31, 2005, scheduled maturities of NYISO's Long-Term Debt were as follows:

	2003 Budget Facility Loan	2004-2006 Budget Facility Loan	Mortgage	Total
2006	$11,7500,000	$15,000,000	$30,525	$26,780,525
2007	11,750,000	15,000,000	32,366	26,782,366
2008	1,958,334	15,000,000	32,216	16,990,550
2009	-	4,500,000	455,434	4,955,434
2010			482,901	482,901
Thereafter	-	-	11,543,420	11,543,420
Total	$25,458,334	$49,500,000	$12,576,862	$87,535,196

7. DERIVATIVES AND HEDGING ACTIVITIES

In December 2003, NYISO entered into an interest rate cap agreement with a commercial bank to cap interest payments at 5.375% (4.65% after refinancing on April 8, 2005) on its 2003 Budget Facility. 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 from January 2004 through February 2008; however, this variable interest rate cannot exceed 5.375% (4.65% after refinancing). As of December 31, 2005 and 2004, the fair value of the interest rate cap was $196,073 and $92,215, respectively and is recorded in Other Current and Non-current Assets. For the year ended December 31, 2005 and 2004, NYISO recorded interest income of $191,531 and interest expense of $234,516, respectively, related to this derivative instrument. Such amounts are reflected in Interest Expense, net.

In March 2004, NYISO entered into interest rate cap agreements with a commercial bank to cap interest payments at 4.60% for draws and 5.00% for term loans (4.53% and 4.80% after refinancing on April 8, 2005) on its 2004 – 2006 Budget Facility. The notional amount of the debt on the date of the cap agreements was $82,000,000. Under the cap agreements, NYISO pays a variable interest rate tied to LIBOR on the draws and term loans of the 2004 – 2006 Budget Facility from March 2005 through December 2010; however, this variable interest rate cannot exceed 4.525% for draws or 4.80% for term loans. As of December 31, 2005 and 2004, the fair value of the interest rate cap was $1,161,635 and $878,191, respectively, and is recorded in Other Current and Noncurrent Assets. For the year ended December 31, 2005 and 2004, NYISO recorded interest income of $412,944 and interest expense of $421,809, respectively, related to this derivative instrument. Such amounts are reflected in Interest Expense, net.

In February 2005, NYISO entered into two interest rate swap agreements with a commercial bank to fix interest rate payments on the financing of a new office building purchase. The notional amount of debt on the swap agreement for the Mortgage was $14,708,750, and NYISO will pay a fixed interest rate of 5.79% on the outstanding principal amount of this financing on payments from August 2005 through August 2025. The notional amount of debt on the swap agreement for the Renovations Loan was $10,000,000, and NYISO will pay a fixed interest rate of 5.96% on payments from January 2007 through January 2027. As of December 31, 2005, the fair value of these interest rate swap agreements was $96,395 for the Mortgage and ($49,249) for the Renovations Loan, recorded in Other Noncurrent Assets and Other Noncurrent Liabilities, respectively. For the year ended December 31, 2005, NYISO recorded interest income of $47,146 related to these two swap agreements. This amount is reflected in Interest Expense, net.

NYISO is exposed to credit loss in the event of nonperformance by the commercial banks under the interest rate cap and swap agreements. However, NYISO does not anticipate nonperformance by the commercial banks.

8. EMPLOYEE BENEFIT PLANS

Pension and Postretirement Plans — NYISO has a defined benefit qualified 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 expects to contribute $2.0 million to the qualified pension plan in 2006.

NYISO also has an unfunded nonqualified excess benefit 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. In 2005, this plan was amended such that the timing of payments would be made annually once a five-year vesting period is satisfied. Accordingly, this plan was curtailed in 2005 under SFAS 87, *Employers' Accounting for Pensions.* At December 31, 2005, NYISO has recognized a liability of $66,976, of which $57,825 represents the current portion of this liability.

NYISO sponsors a defined benefit postretirement plan to provide medical and life insurance benefits for eligible retirees and their dependents. 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.

In May 2004, the FASB issued FSP 106-2, which supercedes FSP 106-1, to provide guidance on the accounting for plans under SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, and disclosures for the federal subsidy under SFAS 132R. The provisions of FSP 106-2 are effective for fiscal periods beginning after June 15, 2004. During 2005, NYISO determined that benefits provided by NYISO's postretirement plan are not actuarially equivalent to Medicare Part D and therefore, there is no impact on NYISO's accumulated postretirement benefit obligation and net periodic postretirement cost for the year ended December 31, 2005.

The schedules that follow show the benefit obligations, the plan assets, and the funded status as of December 31, 2005 and 2004, and the change in benefit obligations and the components of net periodic cost for NYISO's qualified pension and postretirement plans for the years ended December 31, 2005 and 2004.

	Pension Plans For the Year Ended December 31,		**Postretirement Plan For the Year Ended December 31,**	
	2005	**2004**	**2005**	**2004**
Change in benefit obligation:				
Benefit obligation - beginning of year	$15,876,054	$12,650,535	$3,712,698	$ 2,161,503
Service Cost	1,933,823	1,713,846	412,631	339,957
Interest Cost	970,357	789,672	234,300	187,114
Actuarial loss	2,177,257	868,922	260,547	1,024,124
Participant contributions	-	-	730	-
Terminated plan	(498,985)	-	-	-
Benefits paid	(517,172)	(146,921)	(1,460)	-
Benefit obligation - end of year	$19,941,334	$15,876,054	$4,619,446	$3,712,698
Change in plan assets:				
Fair value of plan assets—beginning of year	$11,135,501	$ 8,364,088	$ -	$ -
Actual return on plan assets	579,171	998,840	-	-
Employer contributions	1,833,337	1,971,000	730	-
Participant contributions	-	-	730	-
Benefits paid	(517,172)	(146,921)	(1,460)	-
Expenses paid	(63,991)	(51,506)	-	-
Fair value of plan assets - end of year	$12,966,846	$11,135,501	$ -	$ -
Funded status	$(6,974,488)	$(4,740,553)	$(4,619,446)	$(3,712,698)
Unrecognized prior service cost	1,974,440	2,255,437	-	-
Unrecognized loss	5,150,207	2,911,568	1,194,175	988,115
Additional minimum pension cost	(2,318,524)	(957,127)	-	-
Total accrued liability	$(2,168,365)	$(530,675)	$(3,425,271)	$(2,724,583)

Amounts recognized in the Statements of Financial Position consist of:

	Pension Plans		**Postretirement Plan**	
	2005	**2004**	**2005**	**2004**
Benefit obligation	$(2,168,365)	$(530,675)	$(3,425,271)	$ (2,724,583)
Intangible asset	1,974,440	913,555	-	-
The components of net periodic pension and postretirement cost are as follows:				
Service Cost	$1,933,823	$1,713,846	$412,631	$339,957
Interest Cost	970,357	789,671	234,300	187,114
Expected return on plan assets	(921,112)	(721,306)	-	-
Amortization of unrecognized prior service cost	296,835	295,326	-	-
Amortization of unrecognized loss	186,305	106,111	-	-
Total	$2,466,208	$2,183,648	$701,418	$563,080

NYISO uses a December 31 measurement date for its pension and postretirement benefit plans. NYISO's accumulated benefit obligation for the defined benefit pension plans is $15,135,211 and $11,666,176 at December 31, 2005 and 2004, respectively.

The following table shows the assumptions used to calculate the pension and postretirement benefit obligations and net periodic costs as of December 31, 2005 and 2004:

	Pension Plans		**Postretirement Plan**	
	2005	**2004**	**2005**	**2004**
Benefit obligations:				
Discount Rate	5.75 %	6.00 %	5.75 %	6.00 %
Rate of compensation increases	4.50	5.06	4.50	5.06
Net cost or credit:				
Discount rate	6.00 %	6.25 %	6.00 %	6.25 %
Rate of compensation increases	5.06	5.56	5.06	5.56
Expected return on plan assets	8.00	8.00	n/a	n/a

NYISO's expected rate of return on plan assets reflects anticipated returns on the qualified pension plan's current and future assets. To determine this rate, NYISO considers historical returns for equity and debt securities as well as current capital market conditions and projected future conditions. Given the current low interest rate environment, NYISO selected an assumed rate of 8.00%, which is lower than the rate otherwise determined solely on historical returns.

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

		December 31,	
	Target Allocation	**2005**	**2004**
Equity securitites	60%	62%	61%
Debt securitiies	40%	38%	39%
Total	100%	100%	100%

Pursuant to resolutions adopted by NYISO's Board of Directors, NYISO's Retirement Board has been granted the authority to control and manage the operation and administration of NYISO's qualified pension plan, including responsibility for the investment of plan assets and the ability to appoint investment managers. The Retirement Board currently consists of NYISO's Chief Financial Officer, Vice President of Human Resources, General Counsel and Controller. The Retirement Board provides reports to the Finance Committee of the Board of Directors on at least an annual basis.

The long-term investment objective for NYISO's qualified pension plan assets is to maximize the total return on plan assets while limiting risk, reflected in volatility of returns, to prudent levels. To that end, NYISO's Retirement Board has appointed and regularly meets with an investment advisor to review asset performance, compliance with target asset allocation guidelines, and appropriate levels of asset diversification. NYISO's investment advisor operates under written guidelines provided by NYISO, which cover such areas as investment objectives, performance measurement, permissible investments, investment restrictions, and communication and reporting requirements.

The assumed health care cost trend rates for the postretirement plan are 9% for 2005 decreasing to 4.5% in 2010 and 10% for 2004, decreasing to 4.5% in 2010. A one percentage point change in the assumed health care cost trend rate would change the 2005 postretirement benefit obligation as follows:

	1% increase	1% decrease
Effect on postretirement benefit obligation	$275,500	$(243,900)
Effect on total of service and interest cost components	47,600	(44,700)

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

	Pension Plans	Postretirement Plan
2006	$ 490,145	$ 44,123
2007	569,148	76,638
2008	811,306	115,520
2009	1,149,492	161,460
2010	1,604,253	214,718
2011 - 2015	11,475,928	1,891,139

401(k) Plan — NYISO has a 401(k) Retirement and Savings Plan open to all non-temporary 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 $1,234,783 and $1,104,230 for 2005 and 2004, 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, 2001-2004 and 2002-2005), annual distributions were payable in the year following completion of the cycle. In 2005, there was 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, 2005 and 2004, respectively, were $856,606 and $818,980. The short-term portion of such liability, included in Other Current Liabilities, at December 31, 2005 and 2004 was $118,725 and $545,709, respectively.

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, 2005 and 2004, respectively, the fair market value of securities held by the trust was $840,726 and $807,936. Options outstanding at December 31, 2005 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 have been exercised as of December 31, 2005.

Severance Pay Plan — In 2005, NYISO implemented changes to its organizational structure to more closely align with its corporate objectives and market participant expectations. As a result of these realignments, eleven employee positions were eliminated. These former employees were eligible to receive certain termination benefits under a Severance Pay Plan adopted by NYISO in 2005. Total severance costs resulting from these activities were $1,425,031, and are reflected in the Compensation and Related Benefits line item on the 2005 Statement of Activities. Of this total, $1,029,497 was paid to terminated employees during 2005, and the remaining $395,534 at December 31, 2005 is expected to be paid during 2006. As such, this balance is included with Other Current Liabilities on the 2005 Statement of Financial Position.

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 Albany, NY, expires in January 2006. Another lease agreement for property in Altamont, NY, expires in February 2006, and is expected to be extended on a month-to-month basis thereafter. The third lease agreement for property in Albany, NY expires in April 2008, but is cancelable after April 2006.

Rent expense related to these leases in 2005 and 2004 was as follows:

	2005	2004
Minimum lease payments	$1,020,990	$1,020,990
Additional lease payments	49,584	-
Total	$1,070,574	$1,020,990

The future minimum lease payments under these operating leases at December 31, 2005 are as follows:

2006	$ 302,582
Thereafter	-
Total	$ 302,582

On July 8, 2005, NYISO purchased an office building to relocate NYISO's alternate control center and to consolidate employees currently located in leased facilities. On this date, NYISO also executed an agreement to lease certain office space within the building to the previous owner of this building for a period of one year. The lessee may terminate the lease after ten months or may extend for two months. Rent paid includes $89,546 per month plus reimbursements for a percentage of operating, maintenance, real estate taxes and insurance costs. A security deposit of $281,521 was received at closing to be applied to the last two months' rent and expenses. In December 2005, the tenant gave notice to terminate the lease after ten months. On January 16, 2006, NYISO amended the lease terms to reduce the square footage rented and reduce rent and expense reimbursements by 9.8%. The minimum lease income recorded in 2005 was $517,056 plus additional rent income of $698,826. The future minimum lease income will be $341,526 in 2006, with the lease terminating in May 2006.

In connection with the purchase, management entered into a Payment in Lieu of Taxes ("PILOT") Agreement with the Rensselaer County Industrial Development Agency ("RCIDA") to achieve certain benefits. Per the terms of this agreement, NYISO will be required to make annual payments of approximately $175,000 for the first ten years. However, the agreement is cancelable at the discretion of NYISO.

10. WORKING CAPITAL RESERVE

At December 31, 2005 and 2004, the working capital reserve consisted of:

	2005	2004
Market participant contributions through Rate Schedule 1	$46,440,345	$46,440,345
Interest on market participant contributions	3,259,791	468,530
Total	$49,700,136	$46,908,875

11. DEFERRED REVENUE

Deferred revenue at December 31, 2005 and 2004 consisted of the following:

	2005	2004
Advance payments received on interconnection studies	$ 2,937,925	$ 130,203
Amounts collected for self-insurance reserve	1,290,096	1,210,000
Security deposit and advanced rent on building lease	428,993	-
Governance participation fees	375,400	368,000
Other deferred revenue	51,703	-
Total - current	$ 5,084,117	$ 1,708,203

12. REGULATORY LIABILITIES

At December 31, 2005 and 2004, respectively, NYISO recorded the following amounts as regulatory liabilities:

	2005	2004
Rate Schedule 1 load overcollections	$10,002,548	$ 2,043,108
Voltage support service (reactive power) market	3,679,480	-
Due to market participants for bad debt recovery	2,759,606	-
Funding for deferred charges	1,279,459	2,791,308
Rate Schedule 1 underspending	1,072,525	14,474
Timing differences on certain ratemaking recoveries	-	4,766,585
Total	18,793,618	9,615,475
Less: current portion	(17,514,159)	(2,057,582)
Long-term portion	$ 1,279,459	$ 7,557,893

NYISO recovers its operating expenses through a surcharge assessed to market participants via Rate Schedule 1 of the OATT and Services Tariff. To the extent that transactional volumes billed under Rate Schedule 1 exceed the amount expected when the Rate Schedule 1 surcharge is established, NYISO reflects a regulatory liability for the overcollection amounts. Additionally, to the extent that NYISO's spending does not exceed the annual Rate Schedule 1 revenue requirement, a regulatory liability is also established for the underspending amounts. The regulatory liabilities resulting from Rate Schedule 1 load overcollections and underspending at December 31, 2005 and 2004, respectively, will be applied toward long-term debt in 2006.

In order to maintain acceptable transmission voltages on the New York State transmission system, certain market participants within the New York Control Area produce or absorb voltage support service (reactive power). Payments to market participants supplying voltage support service and recoveries from other market participants are assessed via Rate Schedule 2 of the OATT and Services Tariff. Differences between the timing of recoveries and payments for voltage support service that result in overcollections are reflected as regulatory liabilities. At December 31, 2005 and 2004, respectively, NYISO recognized a regulatory liability of $3,679,480 and a regulatory asset of $672,865 (see Note 3) related to such timing differences.

During 2005, NYISO recovered $2,759,606 from claims entered in the Enron bankruptcy proceedings to recover amounts previously charged to market participants for bad debt losses on two Enron subsidiaries. This recovery amount will be refunded to market participants in 2006.

Certain amounts recovered under NYISO's ratemaking mechanisms are based on estimates. The difference between actual results and estimates that result in overcollections are reflected as regulatory liabilities due to market participants. Additionally, under NYISO's ratemaking structure, principal payments on long-term debt are recovered to fund the cost of acquiring certain property and equipment. Differences resulting between the timing of recoveries of such principal payments and the depreciation expense associated with such property and equipment also result in overcollections reflected as regulatory liabilities. At December 31, 2005 and 2004, respectively, NYISO has recognized an Other Noncurrent Asset of $11,397,988 (see Note 1) and a Regulatory Liability of $4,766,585 related to such timing differences.

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. This case has been stayed pending the outcome of related proceedings at the FERC and the D.C. Circuit Court of Appeals. While is not possible to predict the outcome of this matter with certainty, in the opinion of NYISO management, this proceeding will not have a material adverse effect on the financial position, results of operations or liquidity of NYISO.

14. 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, 2005 and 2004 (in $ billions). The increase in energy transactions from 2004 to 2005 is driven primarily by price rather than volume considerations.

	2005	2004
Energy	$ 9.6	$ 6.3
Installed Capacity	0.8	0.8
Transmission Congestion Contracts	0.3	0.2
Total	$10.7	$7.3