The Electric Reliability Council of Texas, Inc.

		POLICY NO. 2-____
FINANCIAL POLICY	**Effective Date:** June, 2002	**Revised:** June, 2002

PURPOSE

This financial policy is a framework from which ERCOT's financial integrity will be maintained while serving the long-term interests of market participants. ERCOT recognizes that maintaining financial integrity is critical to accomplishing its corporate goals and discharging ERCOT's primary responsibilities.

FINANCIAL OBJECTIVES

In seeking to fulfill its corporate objectives, ERCOT will maintain a high level of financial stability and will not compromise long-term financial integrity to achieve short-term benefits.

Strategic Financial Plan and Budget. Prior to or in conjunction with the submission of the annual Budget, the Chief Financial Officer will submit an update to the Strategic Financial Plan. Both the Strategic Financial Plan and the related Budget will be consistent with this financial policy. The Budget will be submitted to the Board within the timeframe contemplated by the flowchart attached as Exhibit A, which may be updated from time to time.

In developing the Strategic Financial Plan and Budget, ERCOT staff will work to ensure that the ratio of EBITDA to interest expense is not less than 1.25 to 1.00.

ERCOT will target a capital structure with an Equity Ratio that will allow it to maintain an investment grade debt rating with Moody's. If a rating below investment grade is received or expected to be received, staff will promptly recommend a plan for Board consideration to recover or maintain the targeted rating within 18 months.

Overall, the Strategic Financial Plan and the related Budget will seek to assure ERCOT's financial stability. They will be approved by the Board and will guide ERCOT's financial planning process.

Fees and Charges. ERCOT will assess fees consistent with the ERCOT Protocols. The fees and related rates will be set to recover the Board approved Operating and Maintenance Budget (excluding depreciation), Scheduled Debt Service (less any principal payments reasonably expected to be refinanced), and the portion of the Capital Budget that is to be financed with revenue. Fee adjustments, if necessary, will generally be developed and proposed in connection with ERCOT's annual Budget.

ERCOT's fees and charges are subject to approval by the Public Utility Commission of Texas.

Draft

ERCOT will use all reasonable means to operate within the approved Budget for the current year. In the event that unforeseen events occur (e.g. MWh's are significantly over or under projected levels, functionality is added or removed from ERCOT's control by the Board, etc) and as a result, ERCOT experiences or expects to experience in the next 12 month period more than a 25% variance from 1) its Capital Budget 2) its Operating and Maintenance Budget (excluding depreciation and amortization) or 3) its projected revenue stream, staff will promptly recommend a plan for Board consideration, which may include cost reductions or additions, fee increases or decreases, or other means to ensure that approved functions can be maintained, capital expended and expenses paid in the normal course of business.

Sources of Financing. ERCOT will use a combination of equity (revenue funding) and debt to finance capital additions. ERCOT may borrow for capital projects where it is appropriate to spread the cost of capital assets over their useful life.

The issuance of debt requires an affirmative vote of 67% of the Board.

Generally, ERCOT will structure debt issues such that the average maturity of the debt approximates the average life of the assets financed; however, debt issues may be structured with a longer or shorter average maturity if economically justified. ERCOT will use reasonable means to fund 80% of capital projects with debt issues during the startup phase of its operations. Once past the startup phase, ERCOT's target for utilizing debt issues to fund capital projects will be between 60% and 65%.

ERCOT may use variable-rate debt to provide flexibility in its overall financing program and to manage its overall interest rate exposure.

As appropriate, ERCOT will periodically evaluate mechanisms to restructure or refinance debt. ERCOT will continually evaluate alternatives to conventional financing to obtain the lowest overall cost of borrowing while still meeting the objectives of this financial policy.

Liquidity. ERCOT will seek to maintain adequate liquidity to meet its business needs. Liquidity is the combination of available a) cash on hand, b) cash equivalents / short term investments and c) undrawn borrowing capacity under credit facilities.

ERCOT's targeted minimum level of liquidity will factor in: 1) six months of forecasted Scheduled Debt Service, other than principal payments reasonably expected to be refinanced, 2) two months of average Cash Operating and Maintenance Expenses, net of projected administrative fee receipts, 3) two months of budgeted capital expenditures and 4) two months of estimated transmission congestion rights (TCRs) expected to be paid, net of projected TCR receipts during the same period.

Draft

If at any time ERCOT's liquidity is less than or is expected to be less than the targeted minimum level set forth in this policy, staff will promptly recommend a plan for Board consideration to achieve the liquidity target within 6 months.

Funds received in conjunction with TCR auctions may be utilized to fund ERCOT working capital and capital expenditure needs so long as liquidity is at or above the target levels. These funds may be utilized in place of borrowing under short term credit facilities to meet liquidity needs.

RESPONSIBILITIES

It is the responsibility of the Chief Executive Officer and the Chief Financial Officer to ensure that this policy is implemented and to recommend changes in the policy as needed.

FINANCIAL POLICY ADOPTION

ERCOT's financial policy will be adopted by resolution of the Board of Directors. The policy will be reviewed annually by the Finance and Audit Committee and any modifications made thereto must be approved by the Board of Directors.

DEFINITIONS

Budget – The budget consists of both the Capital Budget and the Operations and Maintenance Budget.

Capital Budget – The capital budget consists of the proposed capital expenditures to be made during ERCOT's Fiscal Year and should be substantially consistent with the Strategic Financial Plan when proposed. Any significant capital project not included in the approved capital budget will be presented to ERCOT's Board of Directors for approval.

Operations and Maintenance Budget - The operations and maintenance budget consists of operating costs expected to be incurred during ERCOT's Fiscal Year and should be substantially consistent with the Strategic Financial Plan when proposed.

Cash Operating and Maintenance Expenses – All reasonable and necessary costs and expenses (excluding non-cash items such as depreciation and amortization) incurred in the operation and maintenance of the ERCOT's facilities, equipment and systems.

EBITDA – Earnings (net change in unrestricted assets) before interest, taxes, depreciation or amortization.

Equity Ratio – The calculation is the ratio of unrestricted net assets (capital employed) divided by unrestricted net assets plus long-term debt.

Draft

Fiscal Year – ERCOT's fiscal year is January 1st through December 31st.

Scheduled Debt Service – All interest and mandatory principal payments on ERCOT's outstanding indebtedness (both long-term and short-term) over a 12-month period.

Strategic Financial Plan – The strategic financial plan will provide current financial information and a five-year projection, which addresses all sources of revenues, including any proposed fee adjustments. It will include projections of operating and maintenance expenses, capital expenditures, the funding sources of capital expenditures, and debt service requirements as well as the resulting capital structure.

EFFECTIVE: June __, 2002.

Draft

Exhibit A