

**MINUTES OF THE BOARD OF DIRECTORS MEETING OF
ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.**

Electric Reliability Council of Texas, Inc. Offices

Austin, Texas

10:00 a.m.

July 20, 2004

Pursuant to notice duly given, the Meeting of the Board of Directors of Electric Reliability Council of Texas, Inc. convened at approximately 10:15 a.m. on July 20, 2004.

Meeting Attendance:

Board members:

Armentrout, Mark		Unaffiliated
Baggett, David		Unaffiliated
Espinosa, Miguel		Unaffiliated
Greene, Mike	TXU Power	IOU; Board Chairman
Kahn, Bob	Austin Energy	Municipal
Hayslip, Darrell	Calpine Corp.	Independent Generator-Segment Alternate
Hudson, Paul	Public Utility Commission of Texas	PUCT Chairman
Karnei, Clifton	Brazos Electric Power Cooperative	Cooperative
Manning, Bob	H-E-B Grocery Company	Consumer/Commercial – Board Vice Chairman
McClellan, Suzi	Office of Public Utility Counsel	OPUC Residential & Small Commercial Consumers
Meyer, John	Reliant Resources, Inc.	Independent PM – Segment Alternate
Noel, Tom	Electric Reliability Council of Texas, Inc.	CEO
Payton, Tom	Occidental Chemical Corp.	Consumer/Industrial
Vadie, Henry	Utility Choice Electric	Independent REP – Proxy for David Veisesh

Staff and Guests:

Agatha DeLeon	PUC
B.J. Behroon	KEMA
Barry Smith	AEP
Barry Smitherman	PUCT Commissioner
Betty Day	ERCOT Staff
Bob Helton	ANP
Carrie Morgan	ERCOT Staff
Cheryl Moseley	ERCOT Staff
Clayton Greer	Constellation
Dave Turner	Gestalt LLC
David Kasper	ERCOT Staff
Denise Stokes	Competitive Assets
Diana Zake	ERCOT Staff
Evan Rowe	PUC
Garry Waters	Competitive Assets
Gary Stroud	ERCOT Staff

Heather Tindall	ERCOT Staff
Henry Durrwachter	TXU
Jeyant Tamby	ERCOT Staff
John Houston	CenterPoint Energy
John Moore	Consultant
Kent Saathoff	ERCOT Staff
Kevin Gresham	Reliant
Kevin Judice	ERCOT Staff
Kristy Ashley	Excelon
Lindsey Turns	ERCOT Staff
Margaret Pemberton	ERCOT Staff – VP, General Counsel and Corporate Secretary
Marialyn Barnard	CPS
Mark Dreyfus	Austin Energy
Mark Walker	ERCOT Staff
Maxine Buckles	ERCOT Staff – VP and CFO
Michael Petterson	ERCOT Staff
Neil Eddleman	TEAM
Nelson Nease	East Texas Cooperatives
Parviz Adib	PUCT Staff
Paul Wattles	ERCOT Staff
Randy Jones	Calpine
Ray Giuliani	ERCOT Staff – VP and Chief of Market Operations
Rich Creegan	Gestalt LLC
Richard Gruber	ERCOT Staff
Rob Connell	ERCOT Staff
Sam Jones	ERCOT Staff – Executive VP and COO
Sudeep Reddy	Dallas Morning News
Susan Vincent	ERCOT Staff
Terri Eaton	Green Mountain Energy
Tom Standish	CenterPoint Energy
Tommy Weathersbee	TXU Electric Delivery
Walt Shumate	Shumate & Associates
Wendell Bell	TPPA

Announcements

Chairman Greene called the meeting to order and determined that a quorum was present. He welcomed the Segment Alternates attending the meeting: Darrell Hayslip and John Meyer, who were serving as alternates for Barry Huddleston and Dottie Stockstill, respectively. He also welcomed Henry Vadie, Proxy for David Veiseh.

Approval of Minutes

Chairman Greene requested comments on and approval of the minutes of the June 2004 meeting. **Darrell Hayslip moved to approve the prior month's meeting minutes as circulated. Bob Manning seconded the motion. The motion passed by a unanimous voice vote with no abstentions.**

CEO Report

Tom Noel, President and CEO, reported that the Reliability Council passed the ten million retail

transaction mark as of this week. That number includes move-ins, move-outs, switches, *etc.* He also reported that testing of Texas SET 2.0 is complete and roll-out should take place on August 1, 2004. Mr. Noel reported further that the Reliability Council had no NERC violations in the first quarter of 2004 and remains fully compliant with 2003 planning standards. The Reliability Council received a complimentary letter from the NERC regarding its compliance with the 2003 planning standards. He also stated that the operations group is working to expand control room staff to assist in congestion management and RMR issues.

Mr. Noel mentioned an article in today's Austin American-Statesman which references concerns about contract processes and irregularities within various state agencies. The article sets forth the names of many state agencies, but makes no reference to the Reliability Council. Mr. Noel then briefly addressed some of the vendor irregularities currently facing the Reliability Council and stated that, from the beginning of the internal investigation, he decided to ensure that if wrongdoing was found, all information would be provided to the authorities so they could determine how to prosecute. The Reliability Council found these irregularities through its internal audit process and, once sufficient tangible evidence was obtained, requested that DPS investigate and prosecute.

In closing, Mr. Noel mentioned the many changes which have taken place in the industry since June 2002; *e.g.* members of the legislative committees, Commissioners at the PUCT and the maturation of the Reliability Council itself.

Operations Update

Chairman Greene invited Sam Jones, Executive Vice-President and Chief Operating Officer, to report on the Reliability Council's operations. At the beginning of the report, Chairman Hudson asked Mr. Jones if recent IT personnel changes and the roll-out of Texas SET 2.0 might affect operations and the reliability of the ERCOT System this Summer. Mr. Giuliani, Vice-President and Chief of Market Operations, stated that he believes that the thorough testing of Texas SET 2.0 should preclude any negative impact. Market Participants have tested many scripts and completed that testing early. That fact allows the Reliability Council to ensure that no problems will arise during the switch-over. Mr. Jones stated that he sees no threat to grid operations.

Mr. Jones also reported that the Reliability Council had renewed several RMR contracts this year, while determining that several previously designated RMR units are no longer needed. The Reliability Council continues to implement the exit strategies developed by staff. Recently, several TXU (1,471 MWs) and Garland (78 MWs) units were tendered for consideration for RMR service. The Reliability Council Staff performed a thorough study of the units and determined that the Reliability Council would need only one unit at Eagle Mountain (375 MW) for RMR service to facilitate construction/maintenance of the transmission system. The Reliability Council signed an RMR contract in July, covering a ten month period.

Mr. Jones stated that recent Load growth in the ERCOT Region exceeded the rate in other NERC regions. In the summer of 2000, the Reliability Council had a very low reserve capacity that required deployment of interruptible Load resources. Over the next two years, capacity increased (by approximately 18,000 MWs) while Load remained flat to slightly lower. Beginning in 2003, Market Participants began to mothball some older units and, as a result, capacity dropped slightly, although the Reliability Council maintains approximately a 26-30% reserve margin. He also reported that Market Participants had installed over 700 miles of 345kV lines and 200 miles of 138 kV lines since 1998.

Even with the robust reserve margins, congestion still requires close monitoring. Yesterday, in the north-central Texas area, a great deal of generation needed for congestion control was not available due to

planned outages and emissions limitations. As a result, the Reliability Council interrupted service to approximately 100 MWs of Load for a brief time.

Mr. Jones mentioned that the Reliability Council had experienced a virus in its e-mail system yesterday. The virus had no affect on operations and has proven to be only a nuisance. Mr. Espinosa asked whether the current audit by CanAudit had anything to do with the matter. Mr. Jones stated that it did not. Mr. Armentrout reported that, after discussing the matter with Mr. Judice, he could confirm that the virus incident yesterday had nothing to do with CanAudit. The event appears, at this point, to not involve a hacker or an intrusion into the ERCOT e-mail system but rather appears to be a very common random internet attack.

Mr. Jones then assured the Board of Directors that the recent contract irregularities have had no impact on grid operations and do not appear to have threatened the Reliability Council's system security in any way. The power and market systems are not exposed to the internet at all and remain very well protected from intrusion. None of the former rouge employees worked in those areas. Chairman Greene also pointed that, although the Reliability Council oversees operation of the grid in Texas, it does not physically control any device on the grid. The local TDSPs actually operate the transmission lines and the Resource Entities control Generation Resources. The Reliability Council sends instructions to those entities as the ERCOT control area operator.

Finally, Mr. Jones briefly discussed the Reliability Council's EECPP (Emergency Electric Curtailment Plan) which the Reliability Council implements in certain emergency situations. He stated that the Reliability Council last implemented the EECPP in February 2003 during the ice storm which hit most of Texas and which led to widespread gas curtailments. Mr. Meyer stated that the EECPP is akin to what the system utilities have used for many years to get through emergency conditions. Mr. Karnei asked if the Reliability Council was studying the impact of long-term gas curtailments on generation. Kent Saathoff, Director of System Operations, stated that TAC had referred this matter to the Reliability and Operations Subcommittee (ROS).

Market Operations Update

Ray Giuliani, Vice-President and Chief of Market Operations, reported on retail and wholesale activity in the ERCOT Region. Mr. Giuliani reiterated Mr. Noel's report that the Reliability Council had processed more than ten million retail transactions and stated further that each of those transactions involves several Texas SET transactions. Additionally, he stated that this number does not include wholesale transactions. The Reliability Council oversees 5.9 million ESI IDs (and each ESI ID equates to approximately one meter). By comparison, PJM has only approximately 180 meter points in its system.

Mr. Giuliani reported that, as of May 31, 2004, approximately 18% of residential Load, 50% of small non-residential Load and 64% of large non-residential Load had migrated away from the Affiliated REP. Presumably, customers would not switch to other providers unless the customer saw an economic benefit and, therefore, we can deduce that deregulation has led to cost savings for many of the ultimate end users of electricity in the State of Texas.

Mr. Giuliani presented a detailed report of the wholesale/reliability services. He stated that Balancing Energy Up comprised only 3.7% of the market dollars through May 31, 2004, and Balancing Energy Down comprised only 3.1% of the market dollars through May 31, 2004.

In closing, Mr. Giuliani assured the Board of Directors that none of the recent vendor irregularities have had any impact on market operations and the reliability of the settlement system.

Financial Report

Maxine Buckles, Vice-President and Chief Financial Officer, reported on the Reliability Council's financial matters. Revenue (approximately \$61 million) has closely tracked the budget forecast. Operating expenses and capital expenses have been lower than budget. She reported that the Reliability Council's headcount is less than the budgeted amount (460 in budget and 409 actual employees). Operating expenses have totaled \$55.2 million (including depreciation). Ms. Buckles stated that the Reliability Council currently has 43 capital projects underway.

Ms. Buckles also reported that internal audits of consultants and contractors continue. The Reliability Council has enhanced several internal controls. Currently, the cyber security group reports to the General Counsel. The COO and CMO are sharing the functions of the CIO. The Reliability Council has strengthened its ethics agreements and the confidentiality and conflict of interest language in its contracts. Background checks are required for all contract workers and employees. The Reliability Council has also hired a contract administrator to coordinate activities between the H.R. department and Legal department.

Ms. Buckles reported that the 2005 budget process has begun. A public meeting on the budget is scheduled for September, and finally, the TCE bankruptcy Reorganization Plan began on July 1, 2004 and the Reliability Council had received approximately \$500,000 from TCE on July 2, 2004 which will be applied to previous short payments.

Several Board members and guests asked questions about the information provided by Ms. Buckles, including the budget process, headcount and other issues. Mr. Neil Eddleman raised a question regarding how the Reliability Council will ensure that projects relating to the retail market will be implemented in the upcoming budget. In response, Mr. Gresham, Chairman of PRS, stated that the TAC assigns a priority level to every project before it sends the project to the Board for approval. The Reliability Council then attempts to implement as many of those projects as it can while staying within the confines of the budget.

In response to questions by Chairman Greene, Ms. Buckles stated that the Reliability Council does not directly bill any electricity consumers in the State. The Reliability Council's fees are paid by QSEs in the ERCOT Region; the fee is part of the cost of all electricity purchased/sold in the State. Ms. Buckles also stated that, on a typical bill of \$100 for an electricity user, the ERCOT fee would represent approximately forty-four cents.

Chairman Greene stated that, if the rogue employees are convicted of wrongdoing, the Reliability Council will take whatever steps are available to it to recover the money involved. Additionally, the Reliability Council has insurance coverage regarding criminal activity. Ms. Pemberton, the Reliability Council's General Counsel, stated that the Reliability Council has filed a claim with its insurance carrier.

In conclusion, Chairman Greene stated that the contract irregularities will not impact grid security or market security and should ultimately have no financial impact on the power market in the State of Texas.

After lunch, Chairman Greene welcomed PUCT Commissioner Barry Smitherman to the meeting. At that time, Chairman Hudson announced the beginning of an Open Meeting of the PUCT.

Finance and Audit Committee Report

David Baggett, Chairman of the Finance and Audit Committee, reported that the committee had

asked the Finance Dept. to provide a forecast of expenses versus revenue through the end of the year. The results of that work indicated that revenue will probably exceed expenses by approximately \$10 million for the year.

Mr. Baggett also stated that a total of nineteen EthicsPoint items have come in through the new reporting mechanism. Not all of those issues are truly ethics matters; several represent other specific employee concerns.

TAC Report

Ms. Beth Garza, TAC Chairman, reported on the following recent TAC activities:

(1) Retail Market Guide Revisions

- **RMGRR 2004-006** – This RMGRR relates to the change control process and the Disconnect/Reconnect process.
- **RMGRR 2004-007** – This RMGRR relates to how Critical Care customers are handled in the disconnect process.

(2) System Change Requests

Ms. Garza reported that the following System Change Requests were approved:

- SCR734 -- Continuous Service Agreement Report for Competitive Retailers
- SCR735 -- Responsive Reserve Service Calculation for Hydro Units in Synchronous Condenser Mode

(3) Day Ahead Energy Market

Ms. Garza reported that TAC approved the development and issuance of an RFP, by the ERCOT staff with input from Market Participants, to solicit third-party provision of credit and an auction engine for the Auction Day-Ahead Energy Market. TAC has instructed the WMS to establish a team that includes PUCT, Market Participants from all Segments and ERCOT Staff to develop an evaluation and selection criteria. TAC instructed the team to produce a recommendation of selection to the ERCOT Board of Directors, if necessary.

(4) Protocol Revision Requests

- **PRR479 - IDR Optional Removal Threshold - Urgent.** *Proposed effective date: revisions to Section 18.6.1 item (4)(b) can be implemented upon approval by the ERCOT Board; changes to Section 18.6.2 and the new 18.6.7 will take effect upon system implementation. Some computer system impact to develop a new query and report; the incremental staffing impacts can be absorbed with the addition of an already-budgeted FTE; new ERCOT business function; no impact to grid operations.* This PRR would allow the removal of an IDR meter for settlement under certain conditions when Load drops below a minimum threshold. This PRR also allows IDRs installed by NOIEs for only Load aggregation purposes to be exempt from use in retail customer settlement purposes and allow the NOIE to remove IDRs used for NOIE Load aggregation within one hundred and twenty (120) days after the NOIE fully implements Customer Choice. TAC remanded this PRR to PRS in March 2004 with instructions to remand it to RMS and direct consideration of the issues discussed at TAC relative to existing and move-in

IDR customers. The Profile Working Group considered PRR479 and proposed revisions ultimately approved by RMS at its June 10, 2004 meeting. PRS, through a roll call vote, approved PRR479 as recommended by the PWG and as amended by comments submitted by Nueces Electric Cooperative and discussion at PRS - 71.4% in favor and 28.6% opposed.

TAC then voted to approve urgent status for the PRR. After considerable discussion, TAC voted to approve PRR479 as modified by TAC. ERCOT Credit staff and the Credit Working Group (CWG) have reviewed PRR479 and do not believe that it requires changes to credit monitoring activity or the calculation of liability.

- **PRR501 - A/S Revision to Down Balancing Requirement.** *Proposed effective date: upon updating required documentation (likely within one month after ERCOT Board approval). No ERCOT computer systems impacts; no long-term staffing impacts; business functions and staffing are impacted in short-term by need to update "ERCOT Methodologies for Determining Ancillary Services Requirements" (impacts fall within 2004 Budget amounts); no control room impact; there is a slight increase in the risk of running out of Down Balancing that may result in an increased need to dispatch units off-line during night periods.* This PRR revises the Down Balancing Requirement to account for Regulation Down obligations. TAC remanded PRR501 to PRS at its June 3, 2004 meeting. PRS unanimously approved recommendation of PRR501 as revised by ERCOT comments. TAC voted unanimously to recommend approval of PRR501 as submitted by PRS. ERCOT Credit staff and the CWG have reviewed PRR501 and do not believe that it requires changes to credit monitoring activity or the calculation of liability.
- **PRR514 - Twelve Month Window for Non-IDR Scaling.** Proposed effective date: upon system implementation. No staffing impacts; insignificant impact to Lodestar system; no long-term impacts to ERCOT business functions; no impacts to grid operations. PRR514 would change the timeframe used in data aggregation for estimating non-IDR meter reads when data for an Operating Day is not present in ERCOT systems. The PRS voted to recommend approval of PRR514 as revised by PRS. TAC voted unanimously to recommend approval of PRR514 as submitted by PRS. ERCOT Credit staff and the CWG have reviewed PRR514 and do not believe that it requires changes to credit monitoring activity or the calculation of liability.
- **PRR515 - Disclosure of Local Congestion.** Proposed effective date: upon system implementation. Minimal impact to ERCOT staffing upon implementation; some impact to ERCOT systems; minimal impacts on ERCOT business function; no impact to grid operations. PRR515 provides for the disclosure of information on each Resource receiving an OOMC Dispatch Instruction or an OOME Dispatch Instruction, and the transmission studies performed by ERCOT Staff that lead to OOMC, OOME or RMR deployments. This PRR also provides for disclosure of the contingency and/or overloaded element(s) causing the Local Congestion (OOMC, OOME, and RMR) dispatch instructions as soon as possible. PRS voted to recommend approval of PRR515 as revised by ERCOT Comments and PRS. TAC voted unanimously to recommend approval of PRR515 as submitted by PRS. ERCOT Credit staff and the CWG have reviewed PRR515 and do not believe that it requires changes to credit monitoring activity or the calculation of liability.

After some discussion, **Mr. Karnei moved to approve all the PRRs as submitted. Mr. Baggett seconded the motion. The motion passed by unanimous voice vote with no abstentions.**

All PRRs and supporting materials appear on the following ERCOT web page:

Texas Nodal Team (TNT) Report

Chairman Greene invited Trip Doggett, one of the Independent Facilitators for the Texas Nodal project, to present the TNT Report. He began with an update regarding the cost/benefit study. The development of the model has gone slower than expected. As a result, the review process will have to be shortened to maintain the September 22, 2004 milestone to preview the results. The TNT will distribute a new schedule shortly. Chairman Hudson stated that the PUCT is interested in getting as much information as possible to determine whether the nodal approach will benefit the market. Commissioner Smitherman echoed those comments.

Next, Mr. Doggett reviewed the status of Protocol development for the nodal market. The process has taken longer than originally anticipated. As a result, it looks like the end of the first round review will occur near the end of August.

Finally, the TNT is asking the Board of Directors to establish a committee to review the Competitive Test mentioned in the Market Mitigation Whitepaper. The TNT has recommended that the Board establish a committee similar to the Market Mitigation Concept Group (MMCG). Mr. Noel asked if the MMCG could simply undertake the project. Jim Galvin replied that the MMCG has no voting structure.

Mr. Kahn moved to approve the creation of a committee of the TNT to evaluate the Competitive Test and report the committee's recommendations to the TNT for a vote and, subsequently, present to the Board of Directors for vote. Mr. Payton proposed an amendment to the motion to expand the MMCG to include representatives from all segments and then serve as the TNT committee reviewing the Competitive Test and the MMCG. Mr. Kahn agreed to the amendment of his motion consistent with Mr. Payton's comments. Mr. Armentrout seconded the motion, as amended. The motion carried by a unanimous voice vote with no abstentions.

Update of the Special Committee of the Board

Miguel Espinosa, Chairman of the Special Committee, reported that this committee had a public meeting yesterday to take comment from and provide information to any interested parties. The Committee reported that the RFP (for a Management/Internal Controls Audit) and RFI (for and Internal IT Security Assessment) have been sent out for audits of internal controls—both were ordered by the PUCT. A system has been put into place (EthicsPoint) to allow employees and others to file reports regarding internal issues or concerns. The Reliability Council's internal auditor continues his work. PricewaterhouseCoopers has two on-going audits: (i) the SAS 70 audit and (ii) the annual audit of the Reliability Council's systems. Additionally, CanAudit has been conducting an audit of the Reliability Council's security systems. The DPS continues its investigation. We do not know the scope of that investigation. The Committee has received documents setting forth the Reliability Council's internal procedures and will review them and make recommendations.

Human Resources & Governance Committee Report

Mr. Kahn, Chairman of the H.R. & Governance Committee, stated that he had nothing to report this month.

Other Business

Chairman Greene thanked Mr. Noel for his efforts over the last few years in guiding the Reliability Council through market start-up. In conclusion, Chairman Greene commended the Board on its work through the recent challenges the Reliability Council has faced and also thanked the employees of the Reliability Council for continuing to work hard and do their jobs well. Mr. Espinosa stated that the Board should take some action to officially recognize the employees of the Reliability Council for their professionalism and continued good work. Mr. Noel stated that he would convey those feelings to the staff at this week's lunch and learn and Chairman Greene agreed to convey these sentiments to the employees this Thursday.

Executive Session

The Board met in Executive Session until approximately 4:00 p.m. to discuss litigation matters. Chairman Hudson asked that the record reflect that he would participate in the Executive Session, but Commissioner Smitherman would not participate.

Adjournment

Chairman Greene adjourned the meeting at approximately 4:00 p.m. **The next Board meeting will take place on August 17, 2004 at the Reliability Council's Metro Center office in Austin, Texas. The following meeting will be held on September 21, 2004 at the Reliability Council's Met Center office in Austin, Texas.**

Board materials and presentations from the meeting are available on ERCOT's website at:
<http://www.ercot.com/calendar/2004calendar/2004boardmaterials.htm>

Margaret Uhlig Pemberton, Corporate Secretary