

**DRAFT 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.

November 16, 2004

Pursuant to notice duly given, the Meeting of the Board of Directors of Electric Reliability Council of Texas, Inc. convened at approximately 10:20 a.m. on November 16, 2004.

Meeting Attendance:

Board Members:

Armentrout, Mark		Unaffiliated
Espinosa, Miguel		Unaffiliated
Greene, Mike	TXU Power	IOU; Board Chairman
Hayslip, Darrell	Calpine Corp.	Independent Generator
Kahn, Bob	Austin Energy	Municipal
Karnei, Clifton	Brazos Electric Power Cooperative	Cooperative
Manning, Bob	H-E-B Grocery Company	Consumer/Commercial – Board Vice Chairman
Pappas, Laurie	Office of Public Utility Counsel	OPUC Residential & Small Commercial Consumers; Proxy for Suzi McClellan
Parsley, Julie	Public Utility Commission of Texas	PUCT Chairman; Proxy for Paul Hudson
Payton, Tom	Occidental Chemical Corp.	Consumer/Industrial
Priestly, Vanus	Constellation New Energy	Segment Alternate, Independent REP
Schrader, Tom	ERCOT President and CEO	ERCOT
Stockstill, Dottie	Mirant Americas Energy Marketing	Independent Power Marketer

Staff and Guests:

Adriane Buford	Deloitte
B.J. Flowers	TXU Energy
Barbara Clemenhausen	Sempra Energy
Barry Smith	AEP
Betty Day	ERCOT Staff
Bill Bojorquez	ERCOT Staff
Bob Helton	ANP
Brad Belk	LCRA
Brian D. Bartos	ERCOT Staff
Bridget Headrick	PUCT
Cesar Seymour	Tractebel
Cheryl Moseley	ERCOT Staff
Cheryl Yager	ERCOT Staff
Chris Feenstra	Ernst & Young
Clayton Greer	Constellation
David Kasper	ERCOT Staff
David H. McMillan	Green Mountain Energy Co.

Diana Zake	ERCOT Staff
Dottie Roark	ERCOT Staff
Eddie Kolodzies	DFW Electrical Consumer Coalition
Eddy Reece	RCEC
Erin Bain	PUCT
Evan Rowe	PUCT
Garry Waters	Competitive Assets
Gary Eddins	Topaz Power Group
George Scott	Deloitte
Greg Ramon	Frontera (TECO Energy, Inc.)
Henry Vadie	Utility Choice Electric
Jack Suh	Deloitte
Jamille Ruebsahm	Deloitte
Jeremy Jackson	First Choice Power
Jeyant Tamby	ERCOT Staff
Jom Campbell	City Public Service
Jim Galvin	ERCOT Staff
Jim Harder	Garland Power and Light
John Clitherow	AREVA T&D
John Flory	NECC
John Houston	CenterPoint Energy
John Meyer	Reliant Energy
John Moore	
Kathie Schwerdtfeger	Deloitte
Kent Saathoff	ERCOT Staff
Kevin Gresham	Reliant Energy – PRS Chair
Kristy Ashley	Exelon
Lane Lanford	PUCT
Margaret Pemberton	ERCOT Vice President, General Counsel and Secretary
Mark Bruce	FPL Energy
Mark C. Davis	Brickfield Burchette Ritts & Stone, P.C.
Mark Dreyfus	Austin Energy
Mark Niehans	PwC
Mark Walker	ERCOT Staff
Mark Zion	Texas Public Power Association
Miguel A. Huerta	TXI
Mike Petterson	ERCOT Controller
Natalie Gott	AP
Ned Ross	FPL Energy
Neil Eddleman	TEAM
Nelson H. Nease	Brickfield Burchette Ritts & Stone, P.C.
Nick Fehrenback	City of Dallas
Nieves Lopez	ERCOT Staff
Pamela Dautel	ERCOT Staff
Parviz Adib	PUCT – Market Oversight Division
Pat Escobedo	CPS
Paul Wattles	ERCOT Staff
Paula Mueller	PUCT
Phillip Oldham	Andrews & Kurth
R. P. Verret	AEP
Randy Chapman	TLSC

Randy Jones	Calpine
Ray Giuliani	ERCOT Vice President and Chief of Market Operations
Ray King	Frontera
Read Comstock	Strategic Energy – TAC Chair
Richard Gruber	ERCOT Staff
Robert Penshorn	Deloitte
Sally I. Nelson	Consumer
Sam Jones	ERCOT Executive V.P. and Chief Operating Officer
Sandy Morris	LCRA
Sean Barry	PwC
Smith Day	Direct Energy, LP
Steve Bartley	CPS
Steve Grendel	ERCOT Staff
Sudeep Reddy	Dallas Morning News
Terri Eaton	Green Mountain Energy
Tom Standish	CenterPoint Energy
Valerie Anderson	GDS Associates, Inc.
Vanessa Spells	ERCOT Staff
Walt Shumate	Shumate & Associates
Wendell Bell	Texas Public Power Association

Announcements

Chairman Greene called the meeting to order and determined that a quorum was present and mentioned the proxies and segment alternates set forth above. Chairman Greene also welcomed Public Utility Commission of Texas (PUCT) Commissioner Julie Parsley to the meeting as Proxy for Chairman Hudson.

Approval of Minutes

Chairman Greene requested comments on and approval of the minutes of the October 2004 Board of Directors meeting with revisions recommended by Mr. Richard Gruber, ERCOT Director of Market Services, as shown in Exhibit A to these minutes. **Mr. Manning moved to approve the minutes as revised. Mr. Kahn seconded the motion. The motion passed by a unanimous voice vote with no abstentions.**

Special Committee Report

Chairman Greene invited Mr. Miguel Espinosa, unaffiliated Board member, to report on the activities of this committee. Mr. Espinosa reported that several audits have taken place, including two audits ordered by the PUCT. Mr. Espinosa explained that in financial terms, the audits are qualified and found several areas where ERCOT could improve. Mr. Espinosa noted that ERCOT management has already begun to implement many of the recommendations. Mr. Espinosa stated that the Board members support Mr. Schrader and the ERCOT team in these efforts.

(1) Report from Independent Auditors

Mr. Robert Penshorn of Deloitte & Touche (D&T) presented a summary of the results of the Risk Assessment and Internal Control review. The review looked at ERCOT as of August 1, 2004. D&T reviewed June 2003 through July 2004 and revealed various strengths and risks. Mr. Penshorn commended Tom Schrader, ERCOT President and CEO, for increasing the focus on accountability. D&T

found a lack of policies/procedures; but Mr. Penshorn stated that this finding is not surprising for a company that experienced tremendous growth like ERCOT. He proceeded by reviewing the various controls that D&T tested. Importantly, they found no inappropriate behavior by any current employees.

At this time, the report is an “interim” report because ERCOT and the PUCT have asked D&T to perform additional work. After the report is finalized, D&T will work with ERCOT to create a roadmap to address the various findings.

Mr. Schrader stated that ERCOT fully accepts and embraces the results of the audit and intends to address all the issues raised. He presented a response from management to explain the steps that have been undertaken already and the additional steps that will be taken in the future.

Mr. Vanus Priestly commended Mr. Schrader on his ability to implement the proposed roadmap from D&T. He asked for a timeline from Mr. Schrader. Mr. Schrader stated that ERCOT management would review the roadmap from D&T and intended to have a high-level plan in early December.

Ms. Laurie Pappas asked if ERCOT management intended to investigate the possibility of more instances of fraud. Mr. Schrader stated that D&T reported that they found no such instances, but ERCOT management continues to watch for misconduct. In furtherance of this effort, ERCOT has: (i) proposed providing additional resources to the internal auditor and (ii) implemented the EthicsPoint program allowing the reporting by employees, vendors or any member of the public of any instances of misconduct.

Chris Feenstra of Ernst & Young (E&Y) reported on the results of the E&Y Cyber-Security Assessment of ERCOT. They looked at wireless access points, host configuration, seven key web applications, security protection, vulnerabilities on work stations and the application development and implementation process. E&Y interviewed employees and conducted tests on various environments.

ERCOT’s cyber-security group no longer exists. That work is currently being done by the I.T. organization. E&Y found a number of good practices currently in place. The primary issue they found was the lack of a comprehensive cyber-security plan.

Mr. Feenstra stated that ERCOT has done a very good job of protecting itself against external threats but could improve in the way it protects against internal threats. The prior cyber-security organization was not effective in developing policies and procedures for cyber-security risks. E&Y recommends the creation of a separate security organization outside the I.T. group, the hiring of an experienced CISO and a bolstering of staffing in internal audit. They recommend a comprehensive risk assessment on critical assets. They recommend that the CISO report to a Chief Risk Officer or someone else not involved in day-to-day operations.

Mr. Schrader reiterated ERCOT management’s embracing of the results of the audit reports. He stated that he intends to create a security position which will report directly to Mr. Schrader until ERCOT hires a risk officer. He also stated that ERCOT has been focusing on re-staffing the cyber-security area since the departure of prior employees. Currently, ERCOT is using a well-respected cyber-security firm to take over those activities.

Commissioner Parsley stated that the PUCT appreciates ERCOT’s willingness to endure these audits, the employees’ openness in working with E&Y and management’s willingness to embrace the results. Mr. Armentrout stated that he has reviewed the reports and ERCOT management’s proposed response and he endorses them.

At that time, Mr. Schrader stated that ERCOT management accepts the reports as the current status of its business. Management intends to implement the required controls, some of which have already taken place. He stated that he regretfully accepted the resignation of ERCOT's CFO, who resigned because she believed it was in the company's best interest. ERCOT will hire a Risk Management Officer and a Chief Security Director, who will report to the Risk Management Officer. Management will develop a detailed action plan for each issue raised. ERCOT staff is reviewing each and every recommendation working on responses to them, and taking immediate action, where possible, on high-risk items. Each issue will have an "owner" and dates for milestones and completion. Finally, ERCOT will issue a Request for Proposal for an internal control management program, business process improvement program and a process for effectively implementing change.

Mr. Espinosa thanked D&T and E&Y for their work and recommendations. Chairman Greene invited questions from the audience. None were raised. Chairman Greene also thanked Mr. Espinosa for his willingness to serve as the Special Committee chairman and Mr. Armentrout for his willingness to assist in these efforts. Finally, Chairman Greene thanked Mr. Schrader for his hard work and desire to improve the organization. In conclusion, Chairman Greene stated that the Board of Directors intends, and has always intended, to take any steps necessary to improve the organization.

Finance & Audit Committee Report

Clifton Karnei, Chairman of the Finance & Audit (F&A) Committee reported on the following matters:

(1) 2005 ERCOT Budget Approval

Mr. Karnei reported on the status of the budget process. Work began in September and several public meetings have taken place.

Yesterday, the Committee met to discuss the company's debt policy. Ms. Cheryl Yager, ERCOT Treasurer, circulated information on ERCOT's financial policy. Mr. Karnei stated that ERCOT's current financial policy suffices at this time. He stated that the company remains in a state of flux due to uncertainty regarding whether the market design will change to a nodal market. If it does, a question remains regarding how to fund the redesign.

Mr. Karnei represented that the Committee recommends a ratio of 40% revenue and 60% debt for 2005 capital expenditures. He explained that ERCOT has sufficient borrowing capacity to meet its needs through 2019. He presented a graph demonstrating that the average life of the company's assets exceeds the average life of its debt. Approximately 77% of the debt is long-term debt in 2005. Finally, Mr. Karnei showed the effect that accelerating the reduction of debt would have on the ERCOT administration fee. To change the debt/revenue ratio to 30/70, the fee would change to \$0.48/MW; to change to a 0/100 ratio, the fee would change to \$0.51/MW.

Mr. Randy Chapman asked several questions about the budget process and debt requirements. Mr. Schrader stated that, contrary to Mr. Chapman's assertion, the proposed budget is not a "business as usual" budget. ERCOT management has looked long and hard at areas where it can reduce costs. Mr. Mike Petterson, ERCOT Controller, stated that ERCOT's current operating expenses (4th quarter 2004) are approximately \$0.44/MW, not the \$0.39/MW mentioned by Mr. Chapman.

Commissioner Parsley stated that the PUCT's concern about ERCOT's budget is whether ERCOT is funding items that should not be funded. Mr. Karnei stated that the Committee carefully

reviewed the items being funded by debt and determined that ERCOT does not fund operating expenses through debt; instead, it limits debt to capital projects. Mr. Hayslip stated that the ERCOT Board has worked under the assumption that the PUCT desires stability in the administration fee and if, instead, the PUCT wants ERCOT to accelerate retirement of the debt, ERCOT can do so by increasing the fee.

Ms. Pappas stated that OPUC participates in the fee case at the PUCT and, therefore, she will not participate in any vote on the budget today.

Mr. John Meyer of Reliant stated that he believes the assumption of \$35 million in capital expenses is probably appropriate for one year, but will need to be reconsidered for 2006 and 2007 if a new market design goes into effect.

At this time, Mr. Karnei made a presentation regarding the 2005 proposed budget. The F&A Committee recommends freezing the fee at \$0.44/MW and approving the budget proposed by ERCOT management (\$154.1 million in total spending; \$133.1 million in revenue). He stated that ERCOT expected to have \$196 million in debt at year-end 2004 and, instead, has \$176 million.

If ERCOT implements the Texas Nodal market design, as currently required by the PUCT, the committee estimates that implementation would cost \$500,000 in 2005 and \$40 million in each of the years 2006 and 2007.

Mr. Ray Giuliani, ERCOT's Chief of Market Operations, made a presentation to support his group's request for increased staff in 2005. Several of the positions requested relate to implementing PRRs; several others are for new functions (*e.g.* training). The training positions resulted from the results of the Market Participants survey.

Mr. Sam Jones, ERCOT Executive V.P. and Chief Operating Officer, made a presentation in support of his group's request for additional staff in 2005. Twenty-five of the positions represent contractor replacement. Some of those positions relate to additional support to the PUCT's Market Oversight Division.

Mr. Hayslip moved to approve the 2005 ERCOT budget as proposed by the F&A Committee. Mr. Karnei seconded the motion. At that time, Chairman Greene read a statement from Chairman Hudson (copy attached as *Exhibit B*) and invited discussion.

Mr. Armentrout wanted to clarify Chairman Hudson's representation that the proposed 2005 budget represents a 13% increase in expenditures over 2004. He stated that, when a company grows rapidly, like ERCOT, each quarter expenses exceed those of the previous quarter. Therefore, it is not appropriate to compare the expenses for 2005 against the average expense for 2004. The 2005 budget contains expenses that are flat versus the annualized expenses for the fourth quarter of 2004 as stated by Mr. Petterson earlier. The Board recessed for lunch.

The Board reconvened. **Mr. Hayslip withdrew his prior motion and moved that the Board table the budget discussion until next month in order to allow more discussions with the PUCT. Mr. Karnei seconded the motion to table the issue.** Mr. Armentrout asked that the Board consider the fact that ten PRRs and one PIP will not be implemented under the current budget proposal and, if the fee is reduced further, even fewer projects will take place. Specifically, these are PRRs 478, 359, 457, 408, 454, 521, 426, 311, 414 and 307 and PIP210.

Chairman Greene stated that the ERCOT Board wants to provide the PUCT all the information it needs to perform its oversight. Mr. Schrader stated that, because ERCOT is a non-profit corporation, any

excess revenue remains in the company (to reduce debt). Mr. Manning stated that it would be irresponsible for the Board of Directors to not pass a budget at this time. He stated further that, in his mind, the “safety net” of the budget is that any excess revenue goes toward debt reduction. He stated that Messrs. Jones and Giuliani made clear cases for the need for additional staff. He is concerned that current ERCOT Staff members are getting burned out.

The motion to table the budget passed by a unanimous voice vote with one recusal?? (Lauri Pappas).

(2) Accept Benefit Plans Audited Financial Statements

Mr. Karnei moved to accept the audited financial statements of the benefit plans. Mr. Manning seconded the motion. The Motion passed by unanimous voice vote with no abstentions.

Operations Update

Chairman Greene invited Sam Jones to report on the Reliability Council’s operations. Mr. Jones stated that, in August of this year, ERCOT recovered from a significant event (loss of generation) in seventeen minutes. NERC rules require recovery in fifteen minutes. As a result, ERCOT reported itself to the NERC. Mr. Jones requested an exemption from the NERC due to extenuating circumstances. The Resource subcommittee of NERC is considering the request. A question from the audience was raised regarding whether the original tripping of the generator related to an SPS. Mr. Jones said that the SPS trip resulted from an action taken by a maintenance technician that tripped a circuit breaker and the SPS had acted properly. Mr. Parviz Adib of the PUCT stated that the Market Oversight Division is investigating eleven QSEs who may have violated the Protocols and exacerbated the situation.

(1) Elm Creek Switching Station Project

Mr. Bill Bojorquez, ERCOT’s Director of Transmission Services, made a presentation regarding a project proposed by the South Region planning group. The proposal seeks to add a switching station containing eight 345 kV terminals, one autotransformer and two 138 kV circuits to support Load growth in the area. The switching station would be located at the intersection of Marion Hill Country and Marion Skyline. Cost of the project is estimated at \$16.5 million. The project would save between \$4 million and \$11 million per year in congestion costs. The project received broad support at the Regional Planning meeting in September and TAC voted in favor of the project on November 4, 2004.

Mr. Manning moved to approve the Elm Creek 345 kV Switching Station project. Mr. Kahn seconded the motion. Mr. Hayslip was not present for the vote. The motion passed by unanimous voice vote with no abstentions.

Market Operations Update

Mr. Ray Giuliani, ERCOT’s Chief of Market Operations, reported that ERCOT has processed almost eleven million transactions since market open. For August, September and October, Move-In, Move-Out (MIMO) rejections decreased by 54%. He also reported that Balancing Energy Service increased substantially in September and that OOMC and OOME Service deployments dropped dramatically in September.

Mr. Giuliani stated that ERCOT has completed True-up Settlements for 2003 and should catch up on 2004 settlements within a few weeks.

(1) **ADAM Timeline**

In March 2004, the Board approved an Auction Day-Ahead Market (ADAM) to be implemented by March 2005 or as soon as practicable. ERCOT went through the process of evaluating the implementation of the ADAM. Several vendors submitted proposals. The TNT economists questioned the need for this type of ADAM. As a result, no clear consensus was reached. TNT voted yesterday to implement an integrated model immediately upon TNT implementation. Ms. Stockstill stated that, in her opinion, this may not be the right time to consider this issue because several of the interested companies have expressed an interest in establishing a market on their own.

Chairman Greene asked Mr. Trip Doggett, TNT Independent Facilitator, to recap the process to date. **Ms. Stockstill moved to rescind the following resolution endorsed by the Board at its March 2004 meeting:**

“A day-ahead market shall be established in ERCOT through the implementation of the Auction Day-Ahead model by March 2005 or as soon as practicable and the implementation of a day-ahead market that includes the settlement of CRRs in both real-time and day-ahead timeframes, and is substantially similar to the currently proposed Enhanced Hybrid Day-Ahead model within 12 months or as soon as practicable following the implementation of the real-time nodal market.”

Mr. Karnei seconded the motion. Eight Board members voted in favor of the motion, three were opposed (Mr. Payton, Ms. Pappas, Mr. Schrader) and one abstained (Mr. Priestly). Chairman Greene invited discussion on the topic. Mr. Adib of the PUCT provided some comments on behalf of PUCT Staff. The Board postponed further discussion until the Executive Session.

(2) **Impacts of ADR – Data Correction Disputes**

Mr. Greene left the room, recusing himself from the discussion and vote on this issue. Mr. Giuliani made a presentation regarding the following issue:

Whether it is appropriate to deny Market Participant disputes and ADRs that are filed with unspecific allegations about the accuracy of data supplied to ERCOT by TDSPs and other Market Participants (as required by Sections 10 and 15 of the Protocols) as a placeholder expecting improved data subsequent to the True-Up Settlement related to the Operating Day.

Mr. Priestly recommended that this issue be sent to TAC for discussion. Mr. Manning asked what instructions the Board should give to TAC. Mr. Schrader expressed concern that some disputes remain open from 2001 and the Market Participants need some type of closure. **Mr. Priestly moved that this issue be sent to TAC for resolution. Mr. Hayslip seconded the motion. The motion passed by unanimous voice vote with Mike Greene recusing himself.**

Texas Nodal Team (TNT) Report

Chairman Greene invited Trip Doggett, the Independent Facilitator for the Texas Nodal project, to present the TNT Report.

Mr. Doggett reported that the TNT has continued its work on the cost benefit study. He also reported on the status of the Protocol development. Round Two began on November 1, 2004. Fourteen of the twenty-two sections will have gone through round two reviews by tomorrow.

He also reported on the status of the issues raised by the economists, the recommendations they have made and the results of the votes taken at the October 20, 2004 meeting.

Jim Galvin reported that TNT approved the Market Mitigation Concept Group's recommendation on the Competitive Test. At the implementation of the Nodal Market, competitive constraints will be the current Commercially Significant Constraints and their Closely Related Elements (CRE's). These elements will be determined under the current CSC process. Element Competitive Index calculations will be monitored prior to and after implementation of the Nodal Market.

(1) Revision of Texas Nodal Design Elements

Mr. Doggett asked the Board to agree to the following changes to the previously-approved design elements:

- (1) Addition of co-optimization of Ancillary Services and energy in the Day Ahead Market.
- (2) Lowering of the RUC allocation multiplier that limits the amount that QSEs may be charged when short.
- (3) Creation of a demand curve for a small quantity of Responsive Reserve Service.

Mr. Kahn moved to approve the proposed design. Mr. Hayslip seconded the motion. Mr. Payton was not present for the vote. The motion passed by unanimous voice vote with no abstentions.

TAC Report

Chairman Greene invited Mr. Read Comstock, TAC Chairman, to report on recent TAC activities.

(1) Protocol Revision Requests

The PRS met, discussed the issues and submitted Recommendation Reports to TAC regarding the PRRs described below. TAC considered the issues and voted to take action on the PRRs as described below.

- **PRR527 – Revision to Ancillary Service Performance Conditions (formerly “OOME Definition”)** – URGENT. Proposed effective date: December 1, 2004. No budget impact; no impact to ERCOT staffing; no significant impacts to ERCOT computer systems; no impact to ERCOT business functions; no impact to grid operations. This PRR modifies the Protocols to require ERCOT to issue a verbal Dispatch Instruction to the QSE to relieve the QSE from having to provide the Ancillary Service for the interval or retract the Resource-specific Dispatch Instruction if a unit-specific OOME or Balancing Energy Dispatch Instruction issued by ERCOT causes a QSE to be unable to provide Ancillary Services that it is obligated to provide. PRS approved urgent status for PRR527 through an email vote. At its July meeting, PRS voted to remand PRR527 to WMS for clarification. WMS discussed PRR527 at its August and September meetings. On 9/24/04, PRS agreed to table PRR527 until October to allow for additional review. At its October meeting, with all market segments present, PRS unanimously recommended approval of the PRR without abstentions. At its November meeting, TAC voted to recommend approval as submitted by PRS with 23 votes in favor and 5 votes opposing (from the consumer and independent REP segments), there were no abstentions. ERCOT Credit

staff and the CWG have reviewed PRR527 and do not believe that it requires changes to credit monitoring activity or the calculation of liability.

- **PRR532 – Recommended on Remand**

On October 19, the Board remanded PRR532 to TAC to address legal issues. TAC discussed the issues remanded by the Board and recommends approval as revised:

PRR532 – Implementation of Non-Transmission Alternatives to RMR. Proposed effective date: December 1, 2004. Impact to staffing resources is dependant on the number and type of MRA agreements negotiated; impacts to ERCOT systems will be evaluated on a per-contract basis; some impact to Legal, System Planning and Resources Planning functions; impacts to grid operations will be evaluated on a per-contract basis. This PRR revises the Protocols to allow ERCOT to implement non-transmission alternatives to Reliability Must-Run (“RMR”) Services to reduce uneconomic uplift. The PRR allows ERCOT to contract with a Resource Entity to provide reliability service in place of the RMR unit provided the offered Must Run Alternative (MRA) provides an acceptable solution to the reliability requirement and does so more cost effectively. PRS rejected a request for urgent status for PRR532 through an email vote. PRS voted to recommend approval of PRR532 with two opposing votes and four abstentions. The ERCOT CWG has reviewed PRR 532 and determined that implementation of this PRR does not impact the current methods that are used to calculate ERCOT Creditworthiness Requirements or the kind of activity that should be monitored. However, implementation of PRR 532 does have broader credit implications. *See* CWG Comments dated 9/28/04 for further detail. With all segments present, TAC unanimously approved urgent status for PRR532 to modify the PRR. With one member from the IOU segment opposing and all segments present, TAC voted to recommend approval of PRR532 as revised by CWG comments and TAC. At its October 19, 2004, meeting the Board considered approving the PRR, but ERCOT Staff raised a legal issue and other parties raised concerns about the lack of definition of the amount of benefit that must be shown to merit an MRA. The Board remanded the PRR to TAC to consider the legal issue and those concerns. On November 4, 2004, TAC voted to recommend approval of PRR532 as revised by comments from ERCOT Staff and TAC, which provided that the Board delegate authority to approve MRA contract to a subcommittee of the Board and that MRA service must provide at least a projected \$1 million annualized savings over the RMR alternative. All segments were present for the vote, there were no opposing votes and one member from the independent power marketer segment abstained.

Mr. Kahn moved to approve PRRs 532 and 527; Ms. Stockstill seconded the motion. The motion passed unanimously in favor on PRR532 and in favor of PRR527 with Mr. Payton opposing.

(2) **Appeal of TAC Rejection of PRR 546**

After discussion at the November 4, 2004, meeting, TAC rejected PRR 546.

PRR546 – PCR Treatment for Federal Hydropower Resources. No budgetary impact; no impact to ERCOT staffing; no impacts to ERCOT computer systems, minor changes to TCR calculation spreadsheet; no impact to ERCOT business functions; no impact to grid operations. This PRR would have revised Section 7.5.6 to provide that long-term power purchase agreements for federal hydropower are eligible for PCR treatment if a long-term allocation was in place prior to September 1, 1999. PRS approved urgent status for PRR546 through an email vote. At its October meeting, PRS recommended approval of the PRR with seven abstentions from the independent power marketers, investor owned utilities and consumer segments. No

participant present at the meeting voted against approval of the PRR. All segments were present for the vote. At its November meeting, TAC voted to reject PRR546 with 13 abstentions (independent REP, independent power marketer, and IOU segments), 2 opposing votes (IOU and consumer segments), and 13 affirmative votes (consumers, cooperatives, IOU and municipal segments). PUC Staff submitted comments to both PRS and TAC recommending rejection of PRR 546. ERCOT Credit staff and the CWG reviewed PRR546 and do not believe that it requires changes to credit monitoring activity or the calculation of liability. Tex-La submitted an appeal of TAC's decision to the Board.

Commissioner Parsley pointed out that PUCT staff's position on this matter did not reflect the Commissioners' position because they had not considered the issue.

Mr. Kahn moved to grant Tex-La's appeal; Mr. Karnei seconded the motion. Chairman Greene invited discussion. Mr. Adib of PUCT's Market Oversight Division stated the PUCT Staff's position regarding this issue. PUCT staff recommends denying the appeal. Mr. Mark Davis, on behalf of Tex-La, presented its position to the Board of Directors. Commissioner Parsley stated that she agrees with the positions espoused by Mr. Karnei and Ms. Pappas (in favor of granting the appeal). **Eight Board members voted in favor of the motion, one opposed (Mr. Payton) and three abstained (Mr. Hayslip, Ms. Stockstill and Mr. Priestly). The motion passed.**

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

<http://www.ercot.com/AboutERCOT/PublicDisclosure/ProtocolRev.htm>

(3) Closely Related Elements (CREs) Approval

TAC recommended that the CREs for 2005 remain the same as in 2004. **Mr. Armentrout moved that the Board approve the same CREs for 2005 as were set for 2004. Mr. Karnei seconded the motion. The motion passed by unanimous voice vote with no abstentions.**

(4) Report on Administration Fee Allocation Study

Mr. Comstock reported that, at the October 28, 2004 open meeting of the PUCT, the Commissioners discussed the fee allocation issue. PUCT Staff suggested that a Commission rule-making would be the best forum for working through the issues. PUCT Staff noted that obtaining better quality ERCOT cost data would be important in the development of a rule to evaluate these issues. ERCOT Staff has indicated its commitment to begin employee timekeeping according to the activities identified by TAC or the Commission to accumulate this data. As a result, some members of TAC believe that this activity by the TAC duplicates the efforts being undertaken at the PUCT. Mr. Comstock proposed possible alternatives: (1) Direct TAC to continue working to develop options for Fee allocation; (2) direct TAC to cease its activities on the issue of Fee allocation; or (3) select either (1) or (2) and direct ERCOT Staff to proceed with employee timekeeping.

Mr. Armentrout moved to direct TAC to cease all fee allocation methodology discussions and, if ERCOT implements a cost-tracking program, work with the PUCT to implement a system that would help the PUCT rule-making. Ms. Stockstill seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Human Resources & Governance Committee Report

Mr. Kahn, H.R. and Governance Committee Chair, stated that his Committee had no report this month.

Nominating Committee Report

Chairman Greene reported that the Board has hired an executive recruiting firm to assist in finding a replacement for David Baggett. Three candidates have been interviewed so far and the discussions have gone well.

Other Business

No other business was raised.

Adjournment

Chairman Greene adjourned the open portion of the meeting at approximately 4:35 p.m.

Executive Session

The Board met in Executive Session to discuss litigation matters, H.R. issues and contract matters.

The next Board meeting will take place on December 14, 2004 at the Austin Airport Hilton Hotel in Austin, Texas. The following meeting will be held on January 19, 2005 at the Lakeway Inn Conference Resort at 101 Lakeway Dr., Austin, Texas 78734.

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

EXHIBIT A

Texas Nodal Team (TNT) Report

Chairman Greene invited Trip Doggett, the Independent Facilitator for the Texas Nodal project, to present the TNT Report.

- Mr. Doggett reported on: (i) the cost/benefit study, (ii) TNT Protocols development, (iii) the economists' workshop (held September 16 and 17) and (iv) October 5th votes.

A discussion took place regarding several of the issues associated with the TNT's work.

At that time, Richard Gruber, ERCOT Director of Market Services, made a progress report regarding the work of the TNT, TAC, WMS, a market participant established vendor evaluation team and ERCOT Staff on the Board directed implementation of an Auction Day-Ahead Market, or ADAM..

Additional discussion took place, including comments by Parviz Adib of the PUCT, John Meyer of Reliant, and Clayton Greer of Constellation Power Source. The Board requested that Mr. Gruber return in November for another report regarding the available options evaluated, including cost estimates for each option.

Exhibit B

Statement of Chairman Paul Hudson at the ERCOT BOD Meeting - November 16th

At the outset, please allow me to apologize for not being in attendance today. It is my belief that ERCOT is at a critical juncture. Early this summer, I stated my concerns over both the direction and effectiveness of the organization. At that time, dialogue between ERCOT and the PUC was limited, the organization was in search of new leadership, and criminal investigations of certain employees had begun.

Six months later, circumstances are changing. Dialogue between the PUC and ERCOT has increased and the quality of the discourse continues to improve, new leadership has begun to address issues critical to the organization, and audit reports, though harsh in the light of day, will lead to concrete plans for the overall improvement of the organization.

This brings me to the 2005 budget. Throughout the past two months I have articulated concerns over the proposed increase in ERCOT staffing. What is presented as a "flat" fee for 2005 actually represents almost a 13% increase in spending for the organization from the current projected 2004 spending. The budget includes proposals to add 57 employees and assumes continued increases in salaries. Reductions in contracting and decreased loading factors are positive. However, I have left both budget presentations that I attended troubled by proposals that assume growth in staffing and an increase in spending yet lack the type of internal review of existing staff and functions that is critically necessary to any budget process.

I believe it is essential to give Tom the opportunity to put his own stamp on ERCOT. However, this budget must reflect many things. It must reflect not only Tom's vision for the organization, but also the expectations of the Legislature, the PUC and the ERCOT constituency. It is unclear how this budget, along with the justifications shown so far, contribute to the reformation of public confidence in ERCOT.

I believe that this budget *can* be part of that rebuilt public trust. However, to do so it must do more than account for the dollar changes from the prior year's expenses. It must also tackle the issues of current spending and staffing. ERCOT must explain, document, and justify not only changes, but also the baseline of the budget before I can accept it without further Commission review. Though I cannot speak for my colleagues on the Commission, nor for the members of the Legislature, I can tell you that I will ask my fellow commissioners to review the ERCOT budget as part of a fee case unless the board approves a budget that:

- 1) Fully details spending on capital projects and operations;
- 2) Fully details employee compensation, including an account of increases, bonus amounts, changes in compensation over the past four years, and benchmarks compensation to the market;
- 3) Fully details the justification for additional employees over the current number; and
- 4) Fully delineates what process the agency has undertaken to examine the current cost structure and organization.

While I want to provide Tom with the latitude he needs to reshape ERCOT according to his vision, I cannot provide that flexibility this year if I believe that doing so means that the PUC has neglected its oversight responsibility.