



Date: June 10, 2008
To: Board of Directors
From: Steve Byone, Vice President and Chief Financial Officer
Subject: Application of the 2007 Actual vs. Budget Revenue Requirement Variance

Issue for the ERCOT Board of Directors

ERCOT Board of Directors Meeting Date: June 17, 2008

Agenda Item No.: 10(a)

Issue:

At the June 17, 2008 meeting of the ERCOT Finance and Audit Committee, Committee members reviewed schedules of the 2007 revenue requirement variance and considered alternatives for the use of the funds made available by the favorable variance. It is expected that the Finance and Audit Committee will recommend the following action to the Board:

The Finance and Audit Committee recommends that the Board direct ERCOT staff to apply any favorable budget variances from the 2007 budget year to fund up to 40 percent of spending on the Met Center replacement initiative approved by the ERCOT Board of Directors in February 2008 and employ remaining favorable 2007 financial variance, if any, to reduce debt-funding of other 2008 projects.

Background/History:

ERCOT staff presented financial forecasts of its results of operations for fiscal 2007 to the Finance and Audit Committee and Board of Directors at various times throughout 2007. Each time, ERCOT indicated that a favorable revenue requirement variance was expected.

Based on audited financial information, ERCOT recorded income totaling approximately \$2.1 million in excess of revenue requirements for the year. The projected favorable budget variance is primarily the result of lower-than-budgeted operating expenses, higher-than-budgeted interest income, and higher-than-budgeted income relating to generation interconnection study fees.

The Committee considered several options regarding how to address the utilization of ERCOT's favorable financial variance, including (1) reducing the ERCOT System Administration Fee, (2) refunding of a portion of ERCOT System Administration Fee proceeds, (3) increasing 2008 project funding, or (4) either reducing ERCOT debt or reducing the debt-funded portion of 2008 capital project expenditures. The first two options would require approval of the Public Utility Commission of Texas (Commission).

After final discussion at the June 17, 2008 Committee meeting, it is anticipated that the Committee will arrive at the recommendation described above.



Key Factors Influencing Issue:

In recent years, the Finance and Audit Committee and the Commission have consistently directed or encouraged ERCOT to maintain 40 percent revenue-funding of all project expenditures.

When ERCOT's 2008 budget was prepared by management and subsequently approved by the ERCOT Board of Directors it included many projects, each of which was planned to be funded 40 percent from current year revenue and 60 percent from borrowed money. However, the 2008 budget did not include planned expenditures for the replacement of ERCOT's Met Center facility and relocation of all business conducted in that facility. As a result, when the ERCOT Board of Directors authorized the replacement of the Met Center facility, they authorized 100 percent debt funding of expenditures incurred in connection with the initiative during 2008. It was assumed expenditures incurred in 2009 and subsequent years would be factored into ERCOT's future budget submissions and would be funded with 40 percent revenue and 60 percent debt.

If the favorable financial variance realized in 2007 is used to revenue-fund a portion of expenditures incurred in 2008 relating to the replacement of the Met Center facility, ERCOT can more closely adhere to past direction from the Finance and Audit Committee and the Commission and, as a result, reduce interest costs and other operating expenses borne by ERCOT customers.

Alternatives:

1. Approve the recommendation of the Finance and Audit Committee, as received or as modified by the Board;
2. reject the recommendation of the Finance and Audit Committee;
3. remand this issue to the Committee with instructions; or
4. defer action until a later Board meeting.

Conclusion/Recommendation:

ERCOT Staff respectfully recommends that the Board adopt the recommendation of the Finance and Audit Committee.



ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
BOARD OF DIRECTORS RESOLUTION

WHEREAS, the Board of Directors (“Board”) of Electric Reliability Council of Texas, Inc. (“ERCOT”) deems it desirable and in the best interest of ERCOT to formalize its direction to ERCOT management with regard to favorable financial variance realized from its operations in 2007.

THEREFORE, be it RESOLVED that ERCOT is hereby directed to apply any favorable budget variances from the 2007 budget year to fund up to 40 percent of spending on the Met Center replacement initiative approved by the ERCOT Board of Directors in February 2008 and employ remaining favorable financial variance, if any, realized in 2007 to reduce debt-funding of other 2008 projects.

CORPORATE SECRETARY’S CERTIFICATE

I, Michael G. Grable, Corporate Secretary of ERCOT, do hereby certify that, at its May 20, 2008 meeting, the ERCOT Board of Directors passed a motion approving the above Resolution by a vote of _____.

IN WITNESS WHEREOF, I have hereunto set my hand this _____ day of _____, 2008.

Michael G. Grable
Corporate Secretary