ERCOT
Accounting Background - General Summary
January 2009

Every $1 ERCOT Spends

Operating expense

Capital expense

Expense = Expenditure - At ERCOT, the term "expense" is synonymous with the term "expenditure".
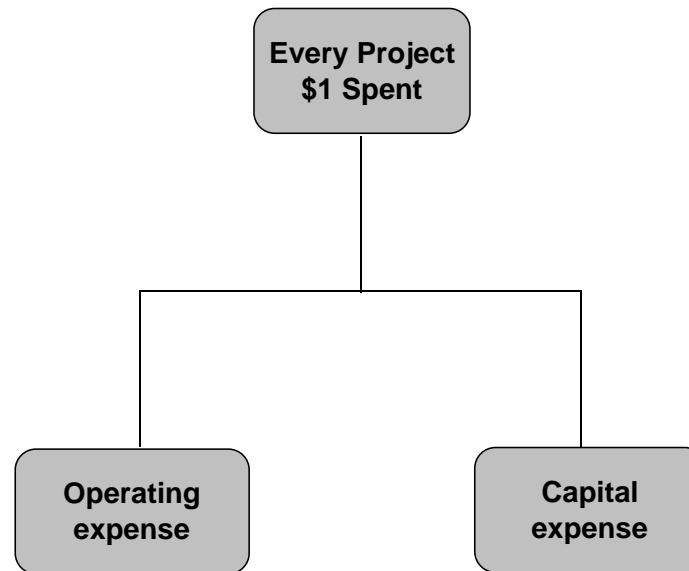
Accounting Rules Dictate - The decision regarding whether the dollar spent is categorized as an operating or capital expense / expenditure is based on accounting rules (e.g. SOP 98-1)

Operating Expense Characteristics -
* Primarily an income statement impact
* Benefit for less than one year
* SOP 98-1 requires most costs incurred during project "preliminary planning" and "post operation" to be classified as operating expenses.

Capital Expense Characteristics -
* Known as capital costs or capitalizable costs
* Primarily a balance sheet impact
* Benefit for more than one year
* Value of more than $1,000
* SOP 98-1 requires most costs incurred during project "development" to be classified as capital expenses.
* Interest costs must be included in capital expenses. The interest amount included is based on the level of other capital expenses and the company's cost of capital.

ERCOT
Accounting Background - SOP 98-1 Summary
January 2009

Activities for a Software Development Project Per SOP 98-1	*Categorization Per SOP 98-1*	*Accounting Treatment Per SOP 98-1*
Conceptual formulation of alternatives	Preliminary planning	Operating expense
Evaluation of alternatives	Preliminary planning	Operating expense
Determination of existence of needed technology (through an RFI, RFQ, RFP or other method)	Preliminary planning	Operating expense
Final selection of alternatives	Preliminary planning	Operating expense
Design of chosen path, including software configuration and software interface	Development	Capital expense
Coding	Development	Capital expense
Installation of hardware	Development	Capital expense
Testing including parallel processing phase	Development	Capital expense
Data conversion costs to develop or obtain software that allows for access of existing data by new system	Development	Capital expense
Other data conversion costs	Development	Operating expense
Training	Post operation	Operating expense
Application maintenance	Post operation	Operating expense
Ongoing support	Post operation	Operating expense

**Every Project
$1 Spent**

**Operating
expense**

**Capital
expense**

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Operating Expense Characteristics -
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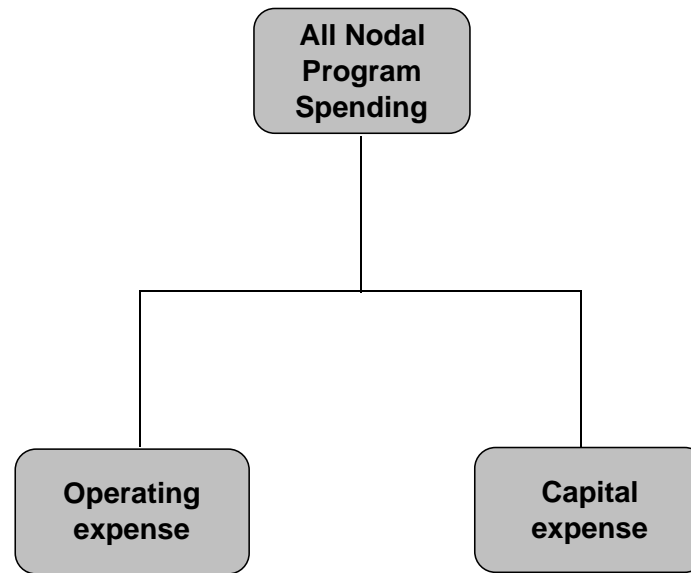**Most Projects have Both Expense Types -**
Most projects on ERCOT's Project Priority List have both operating and capital expenses.

Capital Expense Characteristics -
* Known as capital costs or capitalizable costs
* Primarily a balance sheet impact
* Benefit for more than one year
* Value of more than $1,000
* SOP 98-1 requires most costs incurred during project "development" to be classified as capital expenses.
* Interest costs must be included in capital expenses. The interest amount included is based on the level of other capital expenses and the company's cost of capital.

All Nodal Program Spending

Operating expense

Capital expense

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Accounting Rules Dictate - The decision regarding whether the dollar spent is categorized as an operating or capital expense / expenditure is based on accounting rules (e.g. SOP 98-1)

Operating Expense Characteristics -
* Primarily an income statement impact
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Capital Expense Characteristics -
* Known as capital costs or capitalizable costs
* Primarily a balance sheet impact
* Benefit for more than one year
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* SOP 98-1 requires most costs incurred during project "development" to be classified as capital expenses.
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Nodal Program has Both Expense Types -
Like most projects on ERCOT's Project Priority List, the Nodal Program has expenditures which must be categorized between operating and capital expenses.
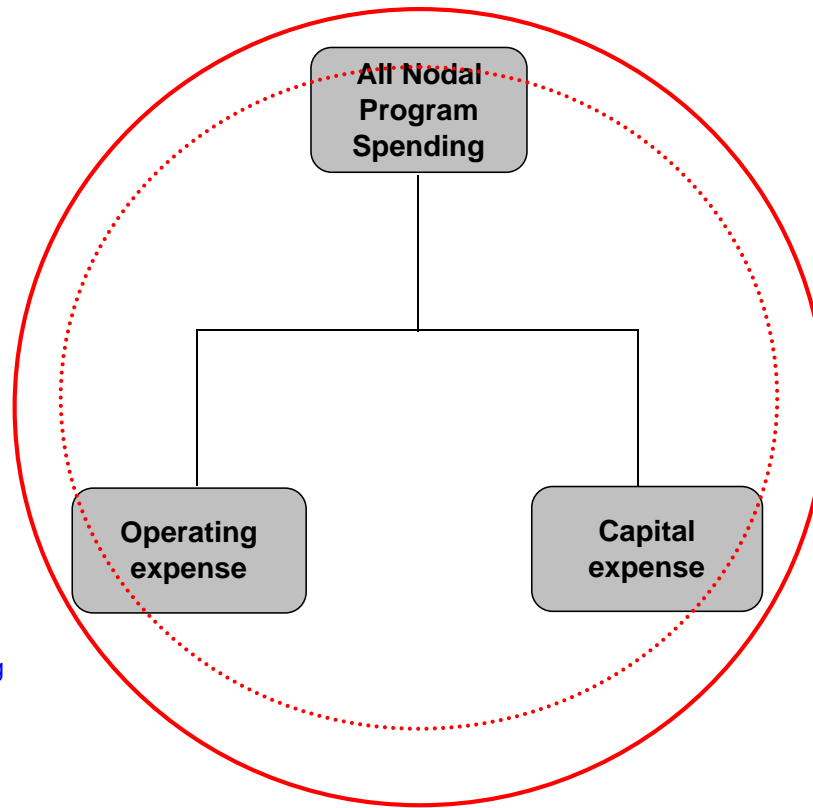
Cost Recovery - Nodal Program cost recovery through the Nodal Surcharge or other methodology is a business policy call not addressed or dictated by accounting rules.

In this case, cost recovery has been established through order of the Public Utility Commission of Texas.

Cost recovery includes the full cost of implementing the Nodal Program, excluding $39.7 million of "interdependent projects".

Operating Expense Characteristics -
* Primarily an income statement impact
* Benefit for less than one year
* SOP 98-1 requires most costs incurred during project "preliminary planning" and "post operation" to be classified as operating expenses.

All Nodal Program Spending

Operating expense

Capital expense

Expense = Expenditure - At ERCOT, the term "expense" is synonymous with the term "expenditure".

Accounting Rules Dictate - The decision regarding whether the dollar spent is categorized as an operating or capital expense / expenditure is based on accounting rules (e.g. SOP 98-1)

Capital Expense Characteristics -
* Known as capital costs or capitalizable costs
* Primarily a balance sheet impact
* Benefit for more than one year
* Value of more than $1,000
* SOP 98-1 requires most costs incurred during project "development" to be classified as capital expenses.
* Interest costs must be included in capital expenses. The interest amount included is based on the level of other capital expenses and the company's cost of capital.

Nodal Program has Both Expense Types -
Like most projects on ERCOT's Project Priority List, the Nodal Program has expenditures which must be categorized between operating and capital expenses.

ERCOT
Accounting Background - Nodal Table Actual
January 2009

	Nodal Program Expenditures (a)			
	Operating	Capital	Total	
Internal labor	17,055	30,833	47,888	
External labor	11,133	184,694	195,827	
Hardware / software	5,361	61,721	67,082	
Travel and other	6,573	695	7,268	
Finance charge	1,868	11,139	13,007	
Subtotal	41,990	289,082	331,072	
Less: Interdependent projects	na	na	39,700	
Subtotal	na	na	291,372	100%
Revenue-funded Nodal Program expenses (a)	na	na	80,214	28%
Debt-funded Nodal Program expenses (a)	na	na	211,158	72%
Depreciation expense (b)	na	na	25,237	

Notes:

(a) Preliminary and unaudited figures through December 31, 2008.

(b) Depreciation expense recorded on hardware, software, and other assets acquired or constructed as part of the Nodal Program that have been placed into service before December 31, 2008.