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Date: April 11, 2006
To: Board of Directors
From: Clifton Karnei, Finance and Audit Committee Chair
Subject: Amendment to Finance and Audit Committee Charter

Issue for the ERCOT Board of Directors

ERCOT Board of Director Meeting Date: April 18, 2006

Agenda Item No.: 10a

Issue:

Provide recommended guidelines for ERCOT's management team, members of the Finance and Audit Committee of the Board, and the ERCOT Board of Directors to use when engaging external auditors for services other than audit services.

Currently, the Finance and Audit Committee Charter includes a provision that the Committee shall approve the provision of all auditing and non-audit services by the independent auditor to the Company in advance of the provision of those services and shall also approve the fees for all non-audit services provided by the independent auditor.

The pre-approval requirements of Section 202 of The Sarbanes-Oxley Act of 2002 are less stringent than those included in the Finance and Audit Committee Charter and provide for de minimus exceptions as described below.

(1) IN GENERAL.

(A) AUDIT COMMITTEE ACTION. All auditing services (which may entail providing comfort letters in connection with securities underwritings or statutory audits required for insurance companies for purposes of State law) and non-audit services, other than as provided in subparagraph (B), provided to an issuer by the auditor of the issuer shall be pre-approved by the audit committee of the issuer.

(B) DE MINIMUS EXCEPTION. The pre-approval requirement under subparagraph (A) is waived with respect to the provision of non-audit services for an issuer, if:

- (i) the aggregate amount of all such non-audit services provided to the issuer constitutes not more than five (5) percent of the total amount of revenues paid by the issuer to its auditor during the fiscal year in which the non-audit services are provided;



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(ii) such services were not recognized by the issuer at the time of the engagement to be non-audit services; and

(iii) such services are promptly brought to the attention of the audit committee of the issuer and approved prior to the completion of the audit by the audit committee or by 1 or more members of the audit committee who are members of the board of directors to whom authority to grant such approvals has been delegated by the audit committee.

Background/History:

The F&A Committee considered this issue at its March 2006 meeting, and requested that ERCOT staff prepare a proposed amendment to the Finance and Audit Committee Charter allowing for the type of de minimus exception allowed for in The Sarbanes-Oxley Act. In summary, the members of the Finance and Audit Committee agreed with the recommendations of ERCOT staff that:

1. ERCOT should follow the requirements established in Section 202.
2. When necessary to request pre-approval from the Finance and Audit Committee for engagement of external auditors for “other services,” ERCOT staff should make the request using the standard decision template (with other essential supporting documentation) used for Board and Board Committee meetings.
3. Engagements for “other services” totaling less than \$5,000 should be communicated in writing to the members of the Finance and Audit Committee at the first meeting following the engagement for the “other services” at issue. This threshold amount is well below the de minimus exceptions provided for in Section 202.
4. Amend the Charter of the Finance and Audit Committee to allow for de minimus exceptions, consistent with point 3 (above) and the requirements of Section 202.

Key Factors Influencing Issue:

The key factors influencing the recommendation were the administrative efficiency of Committee business, the significance of potential financial and operational risk stemming from the proposed amendment to the Charter, and conformity of Committee responsibility to provisions of Section 202 of the Sarbanes Oxley Act.

Alternatives:

- (1) Approve proposed F&A Committee Charter amendment as recommended by the Committee;
- (2) reject the Committee’s recommendation; or



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(3) remand this issue to the Committee with instructions.

Conclusion/Recommendation:

The Chair requests the Committee recommend amendment of the F&A Charter to require that provision of non-audit services of less than or equal to \$5,000 by the independent auditor to the Company do not require pre-approval from the Committee but shall be communicated in writing to the members of the Committee at their first meeting following the engagement for the non-audit services at issue.



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

WHEREAS, the Board of Directors (the “Board”) of the Electric Reliability Council of Texas, Inc. (the “Company” or “ERCOT”) deem it desirable and in the best interest of the Company to amend the Finance and Audit Committee Charter to state that the provision of non-audit services of less than or equal to \$5,000 by the independent auditor to the Company do not require pre-approval from the Committee but shall be communicated in writing to the members of the Committee at their first meeting following the engagement for the non-audit services at issue.

BE IT RESOLVED that the Board hereby amends the first three points under the section heading “With respect to the independent auditors:” of the Finance and Audit Committee Charter to read,

1. Annually, the Committee shall recommend to the Board of Directors the selection and employment of the Company’s independent auditor. The Committee shall fulfill the oversight responsibility of the Board of Directors with respect to the independent auditors’ audit of the books and accounts of the Company and for the fiscal year for which it is appointed.
2. The Committee shall approve the provision of all auditing and non-audit services (in excess of \$5,000) by the independent auditor to the Company in advance of the provision of those services and shall also approve the fees for all non-audit services provided by the independent auditor.
3. Provision of non-audit services of less than or equal to \$5,000 by the independent auditor to the Company do not require pre-approval from the Committee but shall be communicated in writing to the members of the Committee at their first meeting following the engagement for the non-audit services at issue.