



Date: February 13, 2007
To: ERCOT Board of Directors
From: Clifton Karnei, Chairman of the Finance and Audit Committee
Subject: Approval of Maxwell Locke & Ritter, LLP as Auditor for 2006 – 2008 Retirement Benefit Plan Audit

Issue for the ERCOT Board of Directors

ERCOT Board of Director Meeting Date: February 20, 2007

Agenda Item No.: 7d

Issue:

ERCOT management seeks Board approval to select and negotiate terms of an agreement with the firm of Maxwell Locke & Ritter, LLP for the performance of an independent audit of the financials of ERCOT's retirement benefit plans, for the years 2006 – 2008. In October 2005, the Board approved PricewaterhouseCoopers LLP ("PwC") as the auditor to audit ERCOT financial statements (including the financial statements of ERCOT's retirement benefit plans) for a three-year period. However, as described in more detail below, ERCOT has discovered that it must quickly complete an audit of the Money Purchase Plan ("MPP"), which was terminated and combined with the 401(k) Savings Plan ("401(k)") in March 2006, in order to avoid accruing interest and penalties. Because of the urgent need to quickly complete this audit, PwC suggested that ERCOT use a different accounting firm for these audits. ERCOT competitively bid the final audit of the financials of the MPP, along with the audit of the financials of the newly combined 401(k), and has tentatively selected Maxwell Locke & Ritter, LLP.

Background/History:

Section 4.10(d) of the ERCOT Bylaws ("Bylaws") require the Board to approve the annual selection of a qualified public accounting firm ("Auditor") to audit the financial statements of ERCOT. Section 9.6 of the Bylaws establishes that at least annually, an audit of the financial statements of ERCOT shall be performed by the Auditor approved by the Board. The Auditor's opinion and the audited financial statements will be made available to all Members.

Sections 4.10 and 9.6 of the Bylaws do not distinguish between the financial statements of ERCOT and the financial statements of ERCOT's retirement benefit plans. In October 2005, following a competitive bid process and based on recommendation from ERCOT staff and the Finance and Audit Committee, ERCOT's Board of Directors selected PwC as the auditor of ERCOT's financial statements, including as well as the financial statements of ERCOT's retirement benefit plans. The selection was for a three year period covering audit years 2005 – 2007 (audit field work to be conducted in 2006 – 2008).

PwC completed the audit of the 2005 financials statement as planned and has commenced work on the audit of ERCOT's 2006 financial statements. Historically, the retirement benefit plan financial statement audit is executed in July or August. PwC was planning on completing audit



field work for the retirement benefit plans during this time.

However, in March 2006, ERCOT terminated its MPP and combined it with ERCOT's amended 401(k). Within six months following termination of the MPP, ERCOT was required to have a final financial statement audit for the plan. Unfortunately, this requirement was not recognized until after more than six months and the audit deadline had passed. Penalties and fines stemming from failure to timely complete financial statement audits of terminated plans can be assessed at rates up to \$1,100 per day.

To limit exposure to potential penalties and interest, ERCOT is attempting schedule the final financial statement audit of the terminated MPP as quickly as possible. For efficiency, ERCOT would like to have the same accounting firm do the 2006 financial statement audit of the 401(k). In addition, ERCOT would like to have the same accounting firm do the 2007 and 2008 financial statement audit of the 401(k) to provide continuity and reduce the annual price.

PwC committed to meet ERCOT's audit needs, but after considering salient factors including staff expertise, staff availability, and the price of the benefit plan audit engagements ERCOT management decided, with the approval of PwC, to competitively bid services to perform the final audit of ERCOT's terminated MPP as well as the 2006 – 2008 comparative financial statement audit of its amended 401(k). Maxwell Locke & Ritter, LLP was selected as the audit firm preferred by management as a result of the competitive process. The cost for both audits is estimated to be less than \$50,000. The 401(k) audits for 2007 and 2008 are estimated to be less than \$25,000 per year.

Key Factors Influencing Issue:

Key factors influencing the issue include the need expedite the benefit plan audits due to benefit plan administration compliance issues that expose ERCOT to risk of significant potential penalties and fines and the desire to engage a firm that through their audit team can help ensure future regulatory compliance.

Alternatives:

1. Approve the recommendation of the Finance and Audit Committee, as recommended 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:

The Finance and Audit Committee recommends that the Board authorize ERCOT management to negotiate with Maxwell Locke Ritter, LLP for the audit of the 2006 financial statements of ERCOT's MPP and 401(k) and 2007-2008 for the 401(k).



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 select Maxwell Locke & Ritter, LLP to conduct the final audit of its terminated Money Purchase Plan and the 2006 – 2008 financial statement audit of its 401(k) Savings Plan;

THEREFORE, be it RESOLVED that:

1. Maxwell Locke & Ritter, LLP is selected as the 2006 financial statement auditor of ERCOT’s 401(k) Savings Plan and its terminated Money Purchase Plan;
2. Maxwell Locke & Ritter, LLP is selected as the 2007 and 2008 financial statement auditor of ERCOT’s 401(k) Savings Plan;
3. ERCOT is hereby authorized and approved to negotiate terms and execute an engagement letter with Maxwell Locke & Ritter, LLP for the final financial statement audit of ERCOT’s terminated Money Purchase Plan and the 2006 financial statement audit for ERCOT’s 401(k) Savings Plan and the 2007 and 2008 financial statement audit for ERCOT’s 401(k) Savings Plan.