



ERCOT Finance & Audit Committee Meeting

7620 Metro Center Drive, Austin, Texas
Met Center, Conference Room 206
May 16, 2007; 7:30am – 10:00am*

Agenda Item #	Description/Purpose/Action Required	Presenter	Time
	Call to order	C. Karnei	7:30 a.m.
1.	Adjourn to Executive Session		
	• Approval of Internal Audit department charter	B. Wullenjohn	7:30 a.m.
	• Internal Audit Department status report	B. Wullenjohn	7:35 a.m.
	• Update on Internal Audit 2007 goals	B. Wullenjohn	7:45 a.m.
	• EthicsPoint update	S. Maslon	7:50 a.m.
	• Security assessment update	J. Brenton	7:55 a.m.
	Reconvene to General Session		8:05 a.m.
2.	Approval of minutes (Vote) (04/18/07) (Vote) (05/04/07)	C. Karnei	8:05 a.m.
3.	Finance & Audit Committee Charter (Vote)	S. Vincent	8:10 a.m.
4.	Approval of Credit Work Group Charter (Vote)	C. Yager	8:25 a.m.
5.	Update on Credit Review RFP	C. Yager	8:30 a.m.
6.	Authority for additional debt financing (Vote)	C. Yager	8:45 a.m.
7.	Review results of and vote on acceptance of benefit plan financial audit (Vote)	L. Porter	8:50 a.m.
8.	Briefing on preliminary 2008 budget schedule and assumptions	M. Petterson	9:00 a.m.
9.	Update on Texas Regional Entity 2008 budget	L. Grimm	9:10 a.m.
10.	Update on Nodal surcharge filing	S. Byone	9:25 a.m.
11.	Committee briefs (Q & A only)	All	9:35 a.m.
12.	Future agenda items	S. Byone	9:40 a.m.
	Adjourn		9:45 a.m.

*** Background material is enclosed or will be distributed prior to meeting.*

All times shown in the agenda are approximate.

The next Finance & Audit Committee Meeting will be held Tuesday, June 19, 2007, at ERCOT, 7620 Metro Center Drive, Austin, Texas 78744, in Room 168.

(vote)

Draft MINUTES OF THE ERCOT FINANCE & AUDIT COMMITTEE MEETING

Austin Airport Hilton

7:30 A.M.

April 18, 2007

Pursuant to notice duly given, the meeting of the Electric Reliability Council of Texas, Inc. Finance & Audit Committee convened at 7:30 A.M. on **April 18, 2007**. The Meeting was called to order by **Clifton Karnei** who ascertained that a quorum was present.

Meeting Attendance

Committee members:

Clifton Karnei, Chair	Brazos Electric Cooperative	Cooperative	Present
Miguel Espinosa, Vice Chair	Unaffiliated Board Member	Unaffiliated Board Member	Present
Nick Fehrenbach	City of Dallas	Consumer	Present
R. Scott Gahn	Just Energy	Ind. Retail Electric Provider	Present
Michehl Gent	Unaffiliated Board Member	Unaffiliated Board Member	Present
Tom Standish	Centerpoint Energy	Investor-Owned Utility	Present
William Taylor	Calpine Corporation	Ind. Generator	Present
Dan Wilkerson	Bryan Texas Utilities	Municipal	Present

ERCOT staff and guests present:

Barry, Sean	PricewaterhouseCoopers (PwC)
Bartley, Steve	CPS Energy
Byone, Steve	ERCOT
Campbell, Cassandra	ERCOT
Davies, Morgan	Calpine
Day, Betty	ERCOT
Fournier, Marguerite	Competitive Assets
Grimm, Larry	ERCOT
Hancock, Misti	ERCOT
Kolodzies, Eddie	Customized Energy Solutions
Maslon, Sharon	ERCOT
McElfresh, Brandon	ERCOT
Moseley, Cheryl	ERCOT
Petterson, Mike	ERCOT
Simpson, Lori	Constellation
Stolle, Brent	PricewaterhouseCoopers (PwC)
Thomas, Robert	Green Mountain
TroxteLL, David	ERCOT
Twiggs, Thane Thomas	Direct Energy
Vincent, Susan	ERCOT
Yager, Cheryl	ERCOT
Westbrook, Susan	ERCOT

Wullenjohn, William	ERCOT
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Executive Session

At 7:30 AM, the Committee meeting was adjourned and the Committee went into Executive Session until approximately 8:20 AM, when the Committee returned to Open Session.

Approval of Previous Minutes

Dan Wilkerson moved to approve the minutes for the previous meeting held on March 21, 2006. Miguel Espinosa seconded the motion. The motion passed unanimously.

Review Finance and Audit Committee Charter

The Committee briefly discussed the proposed modifications to the Finance & Audit Committee Charter which were included in the materials. Because of the late hour and because the Committee needed time to consider a number of modifications proposed by the Director of Internal Audit, the Committee delayed further discussion of the Charter until the May meeting. William Taylor and Clifton Karnei requested that all proposed modifications be included in a consolidated one-color redline compared to the currently approved Charter.

Review of Credit Workshop Minutes

Nick Fehrenbach moved to approve the minutes from the Credit Workshop held on March 5, 2007; Tom Standish seconded the motion. The motion passed unanimously.

Review Credit Workgroup Charter

Morgan Davies gave an overview of the proposed modifications to the Credit Workgroup (“CWG”) Charter. Clifton Karnei noted that the CWG administration and governance procedures had been modified to make them more consistent with other ERCOT committees, and he asked the Committee members for comments to the proposed changes. Nick Fehrenbach discussed his concerns regarding: (1) the voting qualification requirement (he believes that the qualification should instead be for a quorum); (2) lack of proxy restriction prohibiting voting in multiple segments; and (3) qualification for membership. The Committee requested that the selection of the Chair and Vice Chair be changed to occur at the same time as the other Committees. The Committee will continue its discussion of the Charter at the May Committee meeting.

Confirmation of CWG Chair and Vice Chair

Cheryl Yager informed the Committee that the Credit Work Group had nominated Morgan Davies with Calpine as CWG Chair and Amanda List with Strategic Energy as CWG Vice Chair.

Michel Gent made a motion to approve the recommendation of the CWG and approve Morgan Davies as Chair of the Credit Workgroup and, subject to approval of the revisions to the CWG Charter, Amanda List as Vice Chair of the CWG; Scott Gahn seconded the motion. The motion passed unanimously.

CWG Report on ERCOT Credit Matters

Morgan Davies provided the Committee with a report of ERCOT credit matters and the matters being addressed by the Credit Working Group (“CWG”), including creditworthiness standards, potential credit insurance, and the review of PRRs and NPRRs for credit issues.

Mr. Davies also reviewed the intended scope of the planned request for proposal for a third party credit assessment (RFP), which was included in the materials, and discussed the need to determine the amount of acceptable risk and balance this with the need to maintain access to the ERCOT market. Clifton Karnei noted that the RFP scope must include modeling of the “perfect storm” of credit losses. The Committee discussed the RFP scope in detail. Scott Gahn noted that the Committee did not want a mere repeat of the Black & Veatch study that was done several years ago, but they wanted new information. Ms. Yager confirmed that staff already had the previous study and that the RFP was intended to obtain new information. The Committee authorized ERCOT staff to issue the RFP, and Ms. Yager confirmed that staff intended to issue the RFP by the end of April.

Financial Audit Review

Mike Petterson summarized the results of the annual 2006 financial statement audit by PricewaterhouseCoopers (“PwC”). Sean Barry confirmed that the audit was complete and that PwC had issued an unqualified (“clean”) opinion. Mr. Barry confirmed that 2006 financial results were favorable, with revenues up and operating expenses down and unrestricted net deficit moving toward zero.

Brent Stolle overviewed the details of the audit report, noting that several audit adjustments were identified during the audit. These adjustments included, in the fixed asset area: (1) \$2.2 million reconciling issue relating to fixed assets (increasing assets); (2) \$1.7 million software impairment (decreasing assets); \$1.3 million missed accruals (increased system under development assets).

Mr. Stolle also informed the Committee that PwC had reviewed management’s conclusions regarding the post retirement health benefits which item was discussed with the Committee in the March Committee meeting. Management determined that post retirement health care benefit plan (FAS 106) obligations were deemed not material for 2005. In addition, based upon ERISA counsel advice, PwC concurred with management and determined that these benefits were terminated as of July 2006, and as a result, no liability for ERCOT existed on December 31, 2006.

Mr. Barry informed the Committee that during the last year, the requirements for external auditor evaluation of internal controls of private companies have become more stringent and call for reporting on internal control issues in the same manner as public companies, even though the auditing for private companies is different from public companies. Mr. Barry explained that the PwC had determined one “material weakness” and two “significant deficiencies” relating to the audit adjustments presented by Mr. Stolle in its review of ERCOT’s internal controls. He explained that as a general rule, all audit adjustments are categorized as either material weaknesses, significant deficiencies, or control deficiencies. Mr. Barry explained that the material weakness related to the audit adjustment in the fixed asset area and the significant deficiencies related to the accrual and software impairment audit adjustments. Mr. Barry noted that ERCOT staff had identified the impairment issue, which was quite positive. Mr. Barry told the Committee that ERCOT had made significant internal control improvements in 2006 but audit adjustments clearly indicate more improvement is needed. He noted that staff had put additional processes in place to correct these issues and management’s responses were included in the report. William Taylor asked what improved processes had been put into place for 2006. Mr. Byone discussed management’s intended review of all supporting processes, people and technology to ensure the right focus throughout the company. Dan Wilkerson asked Mr. Byone if he was getting support on internal controls from the other business areas of the company, and Mr. Byone confirmed that he was. Mr. Wilkerson asked if PwC had looked at the processes for paying in a timely manner. Mr. Barry confirmed that this was not included, and Mr. Wilkerson questioned whether this should be added. Mr. Karnei noted that the Committee

was concerned that two of the issues were repeated from the previous year, and he stated that the Committee did not want to see issues in these areas for 2007.

Miguel Espinosa moved to accept the PwC audit of ERCOT's 2006 financial statements; Dan Wilkerson seconded the motion. The motion passed unanimously.

Debt financing and Liability Management

The Committee reviewed the financing options presented by staff, including (a) bank debt with interest rate swaps and (b) senior notes by private placement. The Committee discussed the recommendations in detail. Mr. Karnei stated that the Committee needed to see the estimated pricing and costs for the options before deciding upon the method of financing. Ms. Yager told the Committee that the costs and pricing were comparable, but that if the Committee wanted to see the pricing and costs at a point in time (understanding that pricing would change each day), an executive session could be scheduled. William Taylor requested that staff schedule a special Committee meeting before the May Board meeting, so the Committee could determine its recommendation. Mr. Gahn requested that the information include the cost to pay down the variable rate interest with a swap. Mr. Karnei noted that the Committee also wanted to see the balance sheet impacts of the options. The Committee asked that a special meeting be scheduled in the next three weeks, to discuss the financing options in further detail.

Preview of Proposed Texas Regional Entity Budget and Timeline

Larry Grimm previewed the first draft of the Texas Regional Entity ("TRE") 2008 budget and timeline with the Committee. The Committee discussed the budget briefly and requested that they discuss when more information was available. Mr. Grimm confirmed that FERC was expected to make a determination on the proposed Delegation Agreement on April 19th. The Committee agreed that the TRE Workshop, to allow market participant input on the budget, should be scheduled for May 17, 2007 at 9 A.M. Mr. Karnei and Mr. Wilkerson asked that the TRE budget be discussed at the special Committee meeting to be scheduled on the financing options.

Review of Investment Funds Held at ERCOT

Cheryl Yager confirmed that the yield on investment of funds held at ERCOT had stayed in a consistent range to the previous month and was within the benchmark parameters.

Adjournment

At 10:00 A.M., the meeting was adjourned. The next Committee meeting will be held on the morning of Wed. May 17, 2007.

Susan Vincent, Secretary

Draft MINUTES OF THE ERCOT FINANCE & AUDIT COMMITTEE MEETING

Austin Met Center

9:00 A.M.

May 4, 2007

Pursuant to notice duly given, the meeting of the Electric Reliability Council of Texas, Inc. Finance & Audit Committee convened at **9:00 A.M.** on **May 4, 2007**. The Meeting was called to order by **Clifton Karnei** who ascertained that a quorum was present.

Meeting Attendance

Committee members:

Clifton Karnei, Chair	Brazos Electric Cooperative	Cooperative	Present via telephone
Miguel Espinosa, Vice Chair	Unaffiliated Board Member	Unaffiliated Board Member	Present
Nick Fehrenbach	City of Dallas	Consumer	Present via telephone
R. Scott Gahn	Just Energy	Ind. Retail Electric Provider	Present via telephone
Michehl Gent	Unaffiliated Board Member	Unaffiliated Board Member	Present via telephone
Tom Standish	Centerpoint Energy	Investor-Owned Utility	Present via telephone
William Taylor	Calpine Corporation	Ind. Generator	Present via telephone
Dan Wilkerson	Bryan Texas Utilities	Municipal	Present via telephone

ERCOT staff and guests present:

Byone, Steve	ERCOT
Capezzuti, Nancy	ERCOT
Doolin, Estrellita	ERCOT
Grimm, Larry	ERCOT
Hancock, Misti	ERCOT
Harris, Mike	ERCOT
Jones, Sam	ERCOT
Petterson, Mike	ERCOT
Thorne, James	ERCOT
Vincent, Susan	ERCOT
Westbrook, Susan	ERCOT
Wullenjohn, Bill	ERCOT (via telephone)
Yager, Cheryl	ERCOT

Other Board Members and Segment Alternates:

Andrew Dalton	Valero Energy Corporation	Industrial Consumers	Present
Robert Thomas	Green Mountain Energy	Ind. Retail Electric Provider	Present via telephone
Jean Ryall	Constellation Energy Commodities Group	Ind. Power Marketers	Present via telephone

Executive Session

At 9:02 AM, the Committee meeting was adjourned and the Committee went into Executive Session until approximately 10:00 AM, when the Committee returned to Open Session.

Debt Financing and Liability Management

Clifton Karnei overviewed the financing options for (a) costs related to the Texas Nodal Market Implementation Program (TNMIP) which are not funded with the Nodal Surcharge through the development period, (b) capital expenditures from base operations not concurrently funded with the System Administration Fee, and (c) working capital needs, which the Committee had discussed in detail at the previous meeting and in Executive Session. Cheryl Yager explained that this debt will be in addition to the Senior Notes, which have an outstanding balance of approximately \$96 million.

Miguel Espinosa moved to authorize (a) debt financing of up to \$300 million, in addition to the 2002 Senior Notes, using bank debt which would pay off and replace the existing Term Note and Revolver, and (b) interest rate derivative products of up to \$130 million of the new debt; Dan Wilkerson seconded the motion. The motion was approved by a vote of seven to one, with the one opposing vote by Nick Fehrenbach.

2008 Texas Regional Entity Budget

Larry Grimm presented an overview of the proposed 2008 Texas Regional Entity (“TRE”) Budget and staffing plan. He explained that while there are still many unknowns with respect to the TRE, the proposed budget is based on FERC and NERC requirements for the “Delegated” or “statutory” activities (proposing and enforcement of the NERC Reliability Standards), and is set forth in categories dictated by NERC. Mr. Grimm explained that the budget also includes the costs for the “non-statutory” activities, since TRE would also perform ERCOT Protocols compliance functions. The Committee members extensively discussed the level of staffing and whether certain positions should be filled with full-time employees or contractors, particularly in the short run. There was also discussion regarding which administrative functions needed to be filled by TRE as well as ERCOT. Mr. Espinosa and Mr. Karnei voiced general concern about the ability to functionally separate the TRE from ERCOT, acknowledging that Commissioner Parsley and the PUC wanted to retain the TRE functions within ERCOT, and asked that the full Board discuss this in detail at the next meeting. The Committee discussed whether the Board should have separate meetings for TRE matters, in order to have a clearer separation for the TRE division and the Board’s fiduciary duties. James Thorne agreed to add a discussion about TRE staffing and governance issues to the agenda for the next Executive Session of the Board of Directors.

Mr. Grimm also reviewed the budget development schedule and highlighted the following items:

- 5/16/07 Finance & Audit Committee/Board – Preliminary Budget Presentation and Final Business Plan Review
- 5/17/07 Public Workshop/Open Meeting – Business Plan and Proposed Budget Presentation
- 5/28/07 Finance & Audit Committee Special Meeting – Budget Review and Recommendation (if necessary)
- 6/1/07 NERC – Final Business Plan and Budget (Draft) due to NERC (Statutory and Non-Statutory Functions)
- 6/19/07 Board – Final Budget Approval
- 7/12/07 NERC – Final Board Approved Budget Due

In response to a question from Mr. Karnei, Susan Vincent confirmed that the Workshop was already on the ERCOT web site calendar and a notice regarding the Workshop would be distributed at least seven days prior to the meeting. She also told the Committee that she would also inform the TAC members about the Workshop during the May 4th TAC meeting.

Review Finance and Audit Committee Charter

The Committee considered several proposed changes to the Finance & Audit Committee Charter. Because of the late hour and time needed to consider a modifications proposed William Taylor, the Committee delayed further discussion of the Charter until the May 16, 2007 meeting.

Adjournment

At 11:15 A.M., the meeting was adjourned. The next Committee meeting will be held on the morning of Wednesday May 16, 2007.

Susan Vincent, Secretary

3. F&A Charter – Credit language options

Susan Vincent

3. F&A Charter – Credit language options

Susan Vincent

Option 1

Purpose

- Review and make recommendations to the Board of Directors regarding credit standards, procedures, governance, ERCOT Protocols and other market rules which impact credit risk, with the goal of maintaining the financial stability of the ERCOT market and minimizing credit losses, consistent with prudent credit practices

Duties and Responsibilities

- ***With respect to maintaining the financial stability of the ERCOT market and minimizing credit losses, consistent with prudent credit practices, the Committee shall make recommendations to the Board of Directors regarding:***
 - The adoption and maintenance of a credit standard that defines the goals for the market with respect to financial stability;
 - The adoption and maintenance of credit procedures that provide an appropriate system of checks and balances to help ensure compliance with ERCOT's credit standard, credit procedures, and credit-related Protocols and market rules;
 - The establishment of creditworthiness requirements, methods of evaluating credit exposure and credit risk mitigation strategies which adequately address financial stability goals;
 - Credit implications of all proposed changes to market rules;
 - Other recommended steps for maintaining financial stability of the ERCOT market.

Option 2

Duties and Responsibilities

- The Committee shall review the Company's credit policies to consider:
 - **Appropriateness of credit practices and creditworthiness standards established for market participants**
 - **Compliance with existing creditworthiness standards by market participants**
 - **Compliance with credit-related Protocols and market rules and**
 - **Development of appropriate methods to evaluate and mitigate credit risk**
- The Committee's review shall consider the recommendations of Staff and the Credit Work Group and the decisions of the appropriate stakeholder groups, including the Technical Advisory Committee.
- Following each such review, the Committee may, in its discretion, recommend to the Board of Directors any proposed changes to the previously approved credit policies."



**THE ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
FINANCE & AUDIT COMMITTEE CHARTER**

Purpose

The Finance and Audit committee of the Board of Directors of ERCOT shall:

1. Oversee the Company's budget process and adherence to budget.
2. Provide recommendations to the Board of Directors for establishing levels of financing and in setting the Company's fees, including its administrative fee;
3. Review and make recommendations to the Board of Directors regarding investment and financial standards for the Company;
4. Review and make recommendations to the Board of Directors regarding credit standards, procedures, governance, ERCOT Protocols and other market rules which impact credit risk, with the goal of maintaining the financial stability of the ERCOT market and minimizing credit losses, consistent with prudent credit practices;
5. Ensure that the Company's financial statements are timely, audited by qualified accountants who are independent;
6. Assist the Board of Directors in fulfilling its oversight responsibility with respect to the Company's maintenance of an effective internal audit function;
7. Establish and maintain procedures for the receipt (including anonymous submission), retention and treatment of complaints regarding accounting, internal controls, and auditing;
8. Perform such other duties and responsibilities enumerated in and consistent with this Charter.

The Committee's function is one of oversight, recognizing that the Company's management is responsible for preparing the Company's financial statements, and the independent auditor is responsible for auditing those statements. In adopting this Charter, the Board of Directors acknowledges that the Committee members are not employees of the Company and are not providing any expert or special assurance as to the Company's financial statements or any professional certification as to the external auditor's work or auditing standards. Each member of the Committee shall be entitled to rely on the integrity of staff and external auditors to provide accurate, complete financial and other information to the Committee, absent actual knowledge to the contrary.

While the Committee has the responsibilities, duties and powers set forth in this Charter, it shall be the responsibility and duty of the Company's management and independent auditor, and not the responsibility or duty of the Committee, to plan or conduct audits, to make any determination that the Company's financial statements are complete, accurate and in accordance with generally accepted accounting principles, and to assure compliance with laws, regulations and the Company's ethics policies. It is the responsibility of the Committee to conduct investigations and resolve disagreements regarding financial reporting, if any, between management and the independent auditor.

The Committee shall provide assistance to the Board in fulfilling its oversight responsibility relating to the Company's financial statements and the financial reporting process, the systems of internal accounting and financial controls, the annual independent audit of the Company's financial statements and the legal compliance and ethics programs as established by management and the Board. In so doing, it is the responsibility of the Committee to maintain

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free and open communication between the Committee and the Company's independent auditors, internal accounting personnel and management.

Membership

The Finance and Audit Committee of the Board of Directors of ERCOT (the "Committee") shall be comprised of at least five Board members, at least three of which are from market Segments and two or more of which must be Independent Board members of ERCOT (the "Company"). Each Member must be able to read and understand fundamental financial statements, including the balance sheet, income statement and cash flow statement. At least one Member must have past employment experience in finance or accounting, requisite professional certification in accounting or any other comparable experience or background which ensures the individual's financial sophistication, including a past or current position as a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities.

The board members shall decide from among themselves who shall participate in the Committee. The term shall be for one year.

The Chair of the Committee shall be selected through a majority vote of the Committee members. The Committee Chair shall not be the Chief Executive Officer of the Company and shall have accounting or related financial management expertise.

The Committee may request that any officers or employees of ERCOT, or any other person, whose advice and counsel are sought by the Committee, attend any meeting of the Committee to provide such pertinent information as the Committee requests.

Board members (other than Committee members) including Board member alternates may attend and participate in all Committee meetings but may not participate in Committee voting.

Non-Committee members may attend Committee meetings at the discretion of the Committee. The Committee may exclude any persons who are not Directors, the Segment Alternate or the Director's Designated Representative from any meeting or portion of any Committee meeting that the Committee determines, in its discretion, needs to be held in closed session to discuss personnel issues, confidential legal matters, negotiations or other business of the Committee involving confidential information.

Qualifications

Each member of the Committee shall also meet any experience requirements as may be established from time to time by the Board of Directors. The Board of Directors shall endeavor to appoint at least one member to the committee who is a financial expert as such term may be defined from time to time by the Board of Directors, the accounting industry or other regulatory authorities.

Authority

In discharging its oversight role, the Committee is empowered to investigate any matter brought to its attention with full access to all books, records, facilities and personnel of the Company and the power to retain outside counsel or other experts for this purpose. All employees are directed to cooperate as requested by the Committee or any of its Members for Committee purposes.

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The Committee may request any officer or employee of the Company, the Company's outside counsel or the Company's independent auditor to attend a meeting of the Committee or to meet with any Member or any consultants to the Committee.

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The Director of Internal Audit is the Chief Audit Executive at ERCOT. The Company's Chief Audit Executive shall report directly to the Committee. For administrative purposes, the Chief Audit Executive shall report to the Chief Executive Officer. The Committee shall approve an Annual Internal Audit Plan prepared by the Chief Audit Executive. The Chief Audit Executive shall (1) manage the execution of the Annual Internal Audit Plan, (2) conduct investigations at the direction of the Chair and the Committee, and (3) make periodic reports to the Committee at regularly scheduled Committee meetings and as otherwise directed by the Chair and the Committee.

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The Committee may appoint workgroups or task forces to investigate issues defined by the Committee. Members of such workgroups or task forces need not be Directors. Such workgroups or task forces shall have no authority to bind the Committee or the Company.

Structure

The presence of at least half of the members of the Committee shall constitute a quorum. At any meeting at which a quorum exists, the act of a majority of the members present at a meeting shall be the act of the Committee. For the purposes of voting, members who recuse themselves from voting on an issue shall not be counted as present for that vote.

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The Chair, in consultation with the Chief Financial Officer, shall develop the agenda, the frequency, and length of meetings and shall have unlimited access to management and information for purposes of carrying out functions of the Committee. The Chair shall establish such other rules, as may from time to time be necessary and proper for the conduct of the Committee.

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Duties and Responsibilities

The following shall be the prominent recurring duties and responsibilities of the Committee in carrying out its oversight functions. The duties and responsibilities are set forth below as a guide to the Committee with the understanding that the Committee may alter or supplement them as appropriate under the circumstances to the extent permitted by applicable law, and by the Company's Articles of Incorporation and Bylaws:

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With respect to budget oversight and financing:

1. Annually, on a schedule to be established by the Board of Directors, the Committee shall review staff's proposed budget for the following year, including proposed staffing levels, proposed capital expenditures, and other proposed expenditures.
2. The Committee shall review the staff's estimate of revenues to support all proposed expenditures, including staff's recommendations for fee levels for the following year.
3. The Committee shall review the staff's recommendation of the amount and type of financing that may be needed to support the proposed budget, including the staff's proposed financial performance measures (e.g. ratios).
4. Following the Committee's review of the above items, the Committee shall recommend to the Board of Directors a staffing level, a proposed budget, proposed fees, and proposed financial performance measures for the following year.

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With respect to maintaining investment and financial guidelines for the Company, the Committee shall:

- 1. Establish standards by which the Company will investment funds and maintain its financial health/strength and review these standards at least annually, recommending updates to the Board of Directors as needed.

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With respect to maintaining the financial stability of the ERCOT market and minimizing credit losses, consistent with prudent credit practices, the Committee shall make recommendations to the Board of Directors regarding:

- 1. The adoption and maintenance of a credit standard that defines the goals for the market with respect to financial stability;
- 2. The adoption and maintenance of credit procedures that provide an appropriate system of checks and balances to help ensure compliance with ERCOT's credit standard, credit procedures, and credit-related Protocols and market rules;
- 3. The establishment of creditworthiness requirements, methods of evaluating credit exposure and credit risk mitigation strategies which adequately address financial stability goals;
- 4. Credit implications of all proposed changes to market rules;
- 5. Other recommended steps for maintaining financial stability of the ERCOT market.

With respect to the independent auditors:

- 1. Annually, the Committee shall recommend to the Board of Directors the selection and engagement 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 the first meeting following the engagement for the non-audit services at issue.
- 4. In connection with the Committee's approval of non-audit services, the Committee shall consider whether the independent auditor's performance of any non-audit services is compatible with the external auditor's independence.
- 5. At least annually, the Committee shall obtain and review a report by the independent auditor describing:
 - a. the independent auditor's internal quality control procedures;
 - b. all relationships between the independent auditor and the Company, in order to assess the auditor's independence
- 6. The Committee shall also review any report by the independent auditor describing:
 - a. significant accounting policies and practices used by the Company;
 - b. alternative treatments of financial information as required to be discussed by the independent auditors with the Committee; and
 - c. any other material written communication between the independent auditors firm and the Company's management.
- 7. Establish the Company's hiring policies for employees who are former employees of the Company's independent auditors

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With respect to the Company's financial statements:

1. The Committee shall discuss the annual audited financial statements with management and the independent auditor, including the Company's disclosures.
2. The Committee shall review disclosures made to the Committee by the Company's CEO and CFO about any significant deficiencies in the design or operation of the internal controls or material weaknesses therein and any fraud involving management or other employees who have a significant role in the Company's internal controls.
3. In connection with its review of the Company's financial statements, the Committee shall review and discuss with the independent auditor the matters relating to the conduct of the audit as they may be modified or supplemented, including, but not limited to, significant judgments, significant estimates, critical accounting policies, and unadjusted differences.
4. Review major changes to the Company's auditing and accounting principles and practices as suggested by the independent auditor, internal auditors or management.
5. Review with management and the independent auditor any correspondence with regulators or governmental agencies and any employee complaints or published reports that raise material issues regarding the Company's financial statements or accounting policies.
6. Review with management and the independent auditor the effect of regulatory and accounting initiatives as well as off-balance sheet structures on the Company's financial statements.
7. Review any and all press stories that relate to the Company's accounting and disclosure, require that management or the auditor explain any negative comments and determine whether these comments necessitate a change in the accounting structure of the Company.
8. Based on its review and discussions with management, the Chief Audit Executive and the independent auditor, the Committee shall provide a recommendation to the Board of Directors whether the Company's financial statements should be accepted.

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With respect to periodic reviews and reports:

1. Periodically, the committee shall meet separately with senior management, the Chief Audit Executive and the independent auditors.
2. The Committee shall review with the independent auditor any audit problems or difficulties and management's response to them.
3. The Committee shall review the Company's policies with respect to risk assessment and risk management.
4. The Committee shall review a summary of the Company's dealings with any financial institutions that are also market participants.
5. The Committee shall communicate to the Board of Directors the matters discussed at each meeting of the Committee, including any issues with respect to the quality or integrity of the Company's financial statements, the performance and independence of the Company's independent auditors or the performance of the internal audit function.
6. The Committee shall review and assess the adequacy of this Charter annually and recommend any proposed changes to the Board of Directors.

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With respect to Internal Audit:

1. The Committee shall review with management and the Chief Audit Executive the charter, activities, staffing, and organizational structure of the internal audit function.
2. The Committee shall have final authority to review and approve the Annual Internal Audit Plan and all major changes to the Plan.

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3. The Committee shall review, considering the recommendations of the independent auditors and the Chief Financial Officer, the scope of the Internal Audit Plan and the plan of work to be done by the Company's Internal Audit Department, and the results of such work.
4. The Committee shall review the significant reports to management prepared by the Internal Audit Department and management's responses.
5. The Committee shall ensure there are no unjustified restrictions or limitations, and review and concur in the appointment, replacement, or dismissal of the Chief Audit Executive.
6. The Committee shall, at least once per year, review the performance of the Chief Audit Executive and concur with the annual compensation and salary adjustment.
7. The Committee shall review the adequacy and effectiveness of the internal audit function, including compliance with The Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.
8. The Committee shall, on a regular basis, meet separately with the Chief Audit Executive in executive session to discuss any matters that the committee or Internal Audit believes should be discussed privately.

With respect to the other matters:

1. The Committee shall inquire of management and the independent auditors about significant risks or exposures to the Company and the ERCOT market and assess the steps management has taken to minimize such risks.
2. The Committee shall establish procedures for:
 - a. The receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters; and
 - b. The confidential, anonymous submission by the Company's employees of concerns regarding accounting or auditing matters.
3. The Committee shall establish the Company's hiring policies for employees who are former employees of the Company's independent auditor's.
4. The Committee shall meet at least biannually with the independent auditor and the chief financial officer in separate executive sessions.

Meetings

The Committee shall meet at least once during each fiscal quarter, and as many additional times as the Committee shall deem necessary or appropriate.

Minutes

The Committee shall designate a secretary, who may be a Committee Member or employee of ERCOT, who shall prepare or cause to be prepared the minutes of each meeting and file such minutes with the corporate records of the Company. The secretary shall send, or cause to be sent, copies of such minutes to each of the Members.

Evaluation

The Committee shall undertake an annual evaluation assessing its performance and, in light of this, consider changes in its membership, charter or procedures. The Committee

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shall report to the Board the results of its evaluation, including recommended charter, membership and other changes, if any.

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4. Approval of Credit Work Group Charter (Vote)

Cheryl Yager

- ❖ **Review final draft of Credit Work Group Charter**
- ❖ **Vote to approve the Credit Work Group Charter**



Electric Reliability Council of Texas, Inc.

ERCOT Credit Work Group Charter

I. Purpose and Authority

The Electric Reliability Council of Texas, Inc. (ERCOT) Board of Directors (Board) established the ERCOT Credit Work Group (CWG) as a group of credit professionals to help ensure that appropriate procedures are implemented to mitigate credit risk in the ERCOT Region in a manner that is fair and equitable to all Market Participants.¹

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The CWG will review all sections of the ERCOT Protocols that impact creditworthiness requirements or collateral calculation and provide recommendations to the Finance and Audit Committee of the Board, with a copy to the Chair and Vice Chair of the TAC. The CWG will provide comments to the TAC subcommittees when PRRs, NPRRs or other actions have credit implications.

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II. Reporting Relationships

- The CWG reports to the Finance and Audit Committee of the Board.

III. ERCOT Credit Work Group Functions

The functions of the CWG include, but are not limited to:

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- Providing input to PRRs and NPRRs that impact credit in accordance with this Charter and Board approved credit policies
- Providing input to the ERCOT Creditworthiness Standards

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¹ Capitalized terms used in this document shall have the meanings ascribed to them in the ERCOT Protocols unless otherwise noted.

In addition, the CWG may, from time-to-time, make recommendations to existing or proposed systems, projects, plans, Protocols and policies and procedures of ERCOT impacting credit issues.

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The CWG shall not engage in any activities that conflict with or violate ERCOT Protocols or the ERCOT Ethics Agreement.

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The CWG shall at all times comply with the Antitrust Guidelines for Members of ERCOT Committees, Subcommittees and Working Groups.

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The CWG shall not have direct responsibility or authority over ERCOT Staff. Although the CWG will recommend courses of action, the responsibility for implementation of policies or procedures shall rest with ERCOT Staff.

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In carrying out its responsibilities, the CWG shall be guided by industry best practices.

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¶
The CWG will meet at least quarterly to review credit policy. In addition, they will meet as needed to address issues as they arise or Protocol revisions as they are proposed or needed. All meetings will be posted on the ERCOT website and are open for interested parties to attend and participate in discussions.¶

IV. Credit Work Group Administration

Each Corporate Member of ERCOT may designate one employee that meets the Qualifications Guidelines for Credit Work Group Membership as a voting member to participate in the activities and attend meetings of the CWG. The Consumer representatives on the ERCOT Board may each designate one person, that meets the Qualifications Guidelines for Credit Work Group Membership, as a voting member to participate in the activities and attend meetings of the CWG.

¶
Each Market Participant may but is not required to have one designated voting member on the CWG. The Market Participant may appoint an alternate for the designated voting member. Any member of the CWG must meet the qualifications as identified on the attached Qualifications Guidelines for Credit Work Group Membership. The Finance and Audit Committee will review the requirements for membership in the CWG annually.¶

All designations of CWG members must be sent to ERCOT's Credit Manager.

¶
Each member of the Committee shall have one vote.¶

The Chair and Vice-Chair of the CWG shall be elected annually by the CWG membership and confirmed by vote of the Finance and Audit Committee.

¶
While the CWG will provide a recommendation based on the majority view of the CWG to the appropriate committee, any dissenting party shall have the right to present its view to the same committee if they choose to do so. ¶

The CWG Chair shall report at least semi-annually to the Finance and Audit committee regarding the state of credit policy within the ERCOT Region. In addition, the CWG Chair shall notify the Finance and Audit Committee Chair of significant credit issues as they arise.

¶
All votes shall be made at the time of the meeting by a representative of the member's company or by proxy by another member. If the vote is going to be made by proxy, the member must ensure that the appropriate ERCOT staff has received the proxy by electronic w[...] [1]

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In order to discharge its responsibilities, the CWG may form temporary or ad hoc task forces. The CWG Chair, with CWG approval, shall appoint the chair for each task force for a term of one year or the duration of the task force which ever is less. Each task force chair may serve in that role for no more than two consecutive one year terms. The CWG shall direct these task forces and make assignments as necessary.

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All task forces are responsible for reporting planned activities/projects and results to the CWG for review. All task force actions are subject to CWG review.

V. Meetings

A. Quorum

In order to take action, a quorum must be present. At least one CWG member from four of the seven market Segments listed below must be present at a meeting to constitute a quorum: Independent REPs (and Aggregators), Independent Generators, Independent Power Marketers, Municipals, Cooperatives, Investor Owned Utilities, and Consumers.

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Each CWG member or CWG member's company represented on CWG may designate, in writing, an Alternate Member or proxy who may attend meetings and vote on the member's behalf. Alternate Members must be employees of same company as the CWG member designating them or may be agents with a contractual obligation to represent the interest of the Company designating them. Proxies shall not be counted toward establishing a quorum at a CWG meeting. If a CWG member wishes to designate an Alternate Member or proxy, the CWG member must send to ERCOT notification of the designation of such Alternative Member or proxy in advance of any meeting and the designation shall be valid for the time period designated by the CWG Member.

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B. Meeting Schedule and Notification

The CWG shall meet at least quarterly to review credit policy. In addition, the CWG shall meet as needed to address issues as they arise such as PRRs or NPRRs as they are proposed or needed. Meeting notices and agendas shall be sent to the CWG distribution list and posted on the ERCOT website at least one (1) week prior to the CWG meeting unless an emergency condition requires shorter notice. Meeting notices for emergency meetings shall be sent to the distribution list and posted on the

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ERCOT website and shall clearly identify the condition requiring the shorter notice. Except in cases of emergency, all agenda items requiring a vote of CWG must be published at least one week prior to the meeting at which the vote will take place. In the case of an emergency, all agenda items requiring a vote of CWG shall be published as soon as possible prior to the meeting at which the vote will take place and the need for the emergency vote shall be clearly identified. All CWG meetings may be attended by any interested observer.

C. Voting

Votes: At all meetings, each Segment shall have one (1) vote. CWG members present at the meeting and participating in the vote shall receive an equal fraction of its Segment's vote.

Abstentions: In the event that a CWG member abstains from a vote, the Segment vote shall be allocated equally among the members casting a vote.

Voting: In matters determined by the CWG Chair to require a vote of CWG or when any CWG member requests a vote on an issue, each CWG member shall have one (1) vote except that a CWG member holding a valid proxy for another member shall have one (1) vote plus one vote for each proxy held. A motion passes when (A) a majority of the aggregate of the fractional Segment votes are: (i) affirmative, and (ii) a minimum total of three (3) and (B) a minimum of 67% of voting individuals meet Qualification guidelines.

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Any dissenting party shall have the right to present its position to the Finance and Audit Committee if such dissenting party chooses to do so.

E-mail voting: An e-mail vote is permitted provided a Notification is distributed to the CWG distribution list. An e-mail vote is subject to the same Notification requirements as other votes unless it is procedural only or has been designated as an urgent vote. A Notification must include a detailed description of the issue or proposition on which the vote will occur. A request for an e-mail vote shall be initiated only by the CWG Chair. A quorum of CWG members must participate in the e-mail vote. Participation requires casting a vote or abstaining. Votes shall be submitted to ERCOT for tallying by the close of two (2) Business Days after ERCOT staff circulates the Notification of the vote. Votes are tallied

in the same manner as a regular meeting. The final tally shall be distributed to the CWG distribution list and posted on the ERCOT MIS.

D. Conduct of Meetings

The CWG Chair, or Vice-Chair in the Chair's absence shall preside at all meetings and is responsible for preparation of agendas. In the absence of the CWG Chair or Vice-Chair, another CWG member shall preside at the meeting. The CWG members shall be guided by Robert's Rules of Order in the conduct of CWG meetings. ERCOT staff shall be responsible for recording minutes of CWG meetings and distributing and posting on the MIS the minutes and other communications to all CWG members and any other parties who express an interest in receiving such information. ERCOT staff shall endeavor to distribute and post the minutes of each meeting within seven days after the date on which the meeting took place. Generally, at the beginning of a CWG meeting, the minutes of the prior meeting shall be reviewed and approved by CWG.

CWG members and Alternate Members must meet the qualifications as identified on the attached Qualifications Guidelines for Credit Work Group Membership. The Finance and Audit Committee shall review the requirements for membership in the CWG annually.

This Charter shall be reviewed and ratified at least annually by the Finance and Audit Committee.

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Additional Questions on the ERCOT Credit Work Group

For additional questions on ERCOT's Credit Work Group and creditworthiness requirements, please contact the ERCOT Credit Manager, Vanessa Spells at (512) 225-7014 or by email at vspells@ercot.com.

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Qualification Guidelines for Credit Work Group Membership

Other than a CWG member appointed by a Consumer Board member, each CWG member must be an employee of a Corporate Member of ERCOT (as defined in the ERCOT By-Laws) in good standing. All CWG members and alternate members representing a Corporate Member must be actively engaged in or responsible for the credit activities of such Corporate Member.

All CWG members and alternate members must have experience in at least one or more of the following fields:

- Risk management (preferably credit risk management)
- Credit management and analysis
- Development and/or execution of credit risk policies and procedures
- Establishment and control of credit limits and terms
- Finance and/or loan administration
- Credit ratings analysis
- Commercial credit analysis
- Financial analysis

CWG members are encouraged to be active participants on the CWG.

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The Chairman of the CWG will be nominated annually by the membership of the CWG and confirmed by vote of the Finance and Audit Committee.

The CWG will meet at least quarterly to review credit policy. In addition, they will meet as needed to address issues as they arise or Protocol revisions as they are proposed or needed. All meetings will be posted on the ERCOT website and are open for interested parties to attend and participate in discussions.

Each Market Participant may but is not required to have one designated voting member on the CWG. The Market Participant may appoint an alternate for the designated voting member. Any member of the CWG must meet the qualifications as identified on the attached Qualifications Guidelines for Credit Work Group Membership. The Finance and Audit Committee will review the requirements for membership in the CWG annually.

Each member of the Committee shall have one vote.

While the CWG will provide a recommendation based on the majority view of the CWG to the appropriate committee, any dissenting party shall have the right to present its view to the same committee if they choose to do so.

All votes shall be made at the time of the meeting by a representative of the member's company or by proxy by another member. If the vote is going to be made by proxy, the member must ensure that the appropriate ERCOT staff has received the proxy by electronic written communication prior to the meeting.

The Chairman of the CWG will report at least semi-annually to the Finance and Audit committee as to the state of credit policy within ERCOT. In addition the Chairman of the CWG will notify the Chairman of the Finance and Audit Committee of significant issues as they arise.

5. Update on Credit Review RFP

Cheryl Yager

- ❖ Timeline
- ❖ Selection criteria
- ❖ F&A input

❖ Timeline

- ✓ April 30 – RFP released
- ✓ May 4 – Notice of Intent to Bid received
 - ✓ Received notice from 9 entities of their intent to bid
- ✓ May 11 – Clarifying questions received from bidders
- May 16 – ERCOT response to questions due
- May 22 – Proposals due
- May 28 & 29 – Presentations by selected Vendors
- June 12 – F&A materials mailed
- **June 19 – Review results with F&A and finalize vendor selection**
- June 25 – Bidder selected

❖ Selection criteria

1. Ability to meet scope of RFP
2. Quality of bid
3. Bidder's previous record of performance, service, and references
4. Ability of bidder to render value-added services
5. Delivery schedule
6. Price
7. Warranty (if applicable)
8. Terms and conditions
9. Bidder's financial condition

❖ F&A Input

- Selection criteria
- Analysis for June F&A meeting
 - ERCOT staff will present a summary of bidder capabilities and pricing along with ERCOT's recommendation in executive session
 - Any specific information F&A members want?
 - Will a special meeting be needed?

6. Authority for additional debt financing (Vote) Cheryl Yager

❖ **Review Board template and resolution**

(from Board packet, agenda item 15 (c))

❖ **Vote to recommend approval of resolution to BOD**



Date: May 8, 2007
To: Board of Directors
From: Steve Byone, Vice President and Chief Financial Officer
Subject: Authority for Additional Debt Financing

Issue for the ERCOT Board of Directors

ERCOT Board of Director Meeting Date: May 16, 2007

Agenda Item No.:

Issue:

The Electric Reliability Council of Texas, Inc. (ERCOT) requires authorization from the ERCOT Board of Directors (the Board) to negotiate and execute the documents necessary to obtain debt financing of up to \$300 million.

This financing will be in addition to the 2002 Senior Notes (which have an outstanding balance as of May 16, 2007 of approximately \$96 million) and any TCR borrowings (which are primarily used for short-term intra-year working capital needs), but will pay off and replace the current term loan and revolving credit facility. The authorization requested herein will bring total authorized ERCOT debt financing to \$396,000,000, excluding any TCR borrowing.

ERCOT staff anticipates that the Finance & Audit Committee will recommend that the requested financing be obtained through a new term loan and revolving credit facility, and, in order to ensure that un-hedged, variable rate debt is not more than 40% of total debt outstanding, in accordance with the Financial Standard, will include entering into interest rate derivative products of up to \$130 million.

ERCOT currently has a term loan, with an outstanding balance of approximately \$25,000,000 (Term Loan), and a revolving credit facility, with an authorized amount of \$125,000,000 (Revolver). These facilities are not expected to be adequate to accommodate ERCOT's financing needs through the next two years. The requested new financing will pay off and replace these facilities.

In addition to paying off the Revolver and Term Loan, the requested financing will provide additional borrowing capacity to fund, on market terms and interest rates: (a) costs related to the Texas Nodal Market Implementation Program (TNMIP) which are not funded with the Nodal Surcharge through the development period, (b) capital expenditures from base operations not concurrently funded with the System Administration Fee, and (c) working capital needs.

The proposed authorized debt will include:

Term Loan (new)	\$ 225,000
Revolver (new)	<u>75,000</u>
Proposed new borrowing capacity	300,000



Senior Notes (balance as of May 16, 2007)	<u>96,000</u>
Total proposed authorized debt	\$ 396,000

Background/History:

In 2005, ERCOT was charged with implementing a multi-year effort undertaken by the Public Utility Commission of Texas (PUCT) and ERCOT stakeholders to re-design the Texas Electric Market, through the TNMIP. The estimated cost of TNMIP is currently \$248.9 million, including interest costs. ERCOT is currently collecting \$0.0663 per MWh under an interim Nodal Surcharge approved by the PUCT for implementation on an interim basis effective October 1, 2006. Based on the current estimated cost of \$248.9 million, ERCOT has filed for a permanent Nodal Surcharge of \$0.127 to be effective June 1, 2007. If approved, ERCOT estimates that this fee will fund approximately 32% of TNMIP costs through the development period. The remaining 68% of TNMIP costs is to be financed with debt. To date, the debt which has been incurred by ERCOT to finance TNMIP costs has been financed under existing credit facilities.

As ERCOT evaluated its financing needs in the Fall of 2006, it issued an RFP for Debt Financing to fund TNMIP costs as well as the debt portion of capital expenditures from base operations. The RFP was sent to five financial institutions: 2 banks, 2 Private Placement sources and National Cooperative Services Corporation (NCSC), at least one of which has a related entity that is a market participant. All affected financial institutions were made aware of the confidentiality and notice requirements ERCOT has regarding financial institutions that operate in the ERCOT market. As ERCOT considered the financing options below, it evaluated the options from the RFP responses considering cost and flexibility to meet ERCOT's needs.

At December 31, 2006, ERCOT had short term borrowings (which excludes Senior Notes and the Term Loan) of \$47 million under the Revolver. By December 31, 2007, ERCOT expects to require outstanding debt under the Revolver or new facilities of approximately \$165 million (assuming no TCR borrowings and excluding the current \$25 million Term Loan) and by December 31, 2008, ERCOT expects outstanding debt under the new facilities to be approximately \$195 million. This is based on estimated debt funding of TNMIP costs of approximately \$109 million and debt funding of capital expenditures from base operations of approximately \$39 million in 2007 and 2008. In addition, ERCOT is required per the Financial Standard to maintain a base level of availability under facilities to meet liquidity needs. Through 2008, this is expected to be up to an additional \$40 million. In summary, the \$300 million requested is to fund:

- | | |
|--|----------------|
| 1. Expected outstanding debt through December 31, 2008
(approx \$151 million of which will be from TNMIP) | \$ 195 million |
| 2. Refinance existing Term Loan
(at same terms, but to simplify the structure) | \$ 25 million |
| 3. Provide for liquidity needs at end of 2008 | \$ 40 million |
| 4. Provide for contingencies or to be used in 2009 | \$ 40 million |



New borrowing capacity required

\$ 300 million

Finally, the Financial Standard requires that “in no event will ERCOT allow un-hedged, variable rate debt to be more than 40% of total debt outstanding”. This requirement mandates that a portion of the new debt issued must be fixed rate debt. To the extent variable rate bank debt is used to meet liquidity needs, interest rate swap(s) will need to be used to meet this requirement.

ERCOT staff considered various financing alternatives before settling on two primary financing strategies stemming from the results of the RFP:

Option 1 - Expanded or new bank facility with interest rate swap(s)

- Desire to incorporate a second bank to broaden access to bank market
- Total bank debt of up to \$300 million
 - \$225 million term loan
 - Includes refinancing existing \$25 million Term Loan
 - At least annual payments through November, 2012
 - Allow for prepayments without penalty
 - \$75 million revolving credit facility
 - Pay off outstanding balance under current \$125 million Revolver
 - Extend from current maturity in 2010 through 2012
- Up to \$130 million in interest rate swap(s)
 - To be executed through bidding process
 - Fairness opinion to be obtained
 - Will have income statement and balance sheet implications through 2012 with possible variability of \$7,000,000 or more

Option 2 – Private placement

- Up to \$175 million of senior notes under terms similar to existing 2002 Senior Notes
 - Fund approximately \$60-80 million at close and remainder as delayed draw by March 2008
 - Fixed annual pay down schedule to approximate expected revenues at slight discount
- \$25 million Term Loan – retain and payout
- \$75 to \$100 million Revolver
 - Reduce from \$125 million after final draw under new senior notes



Summary Comparison of Alternatives

	<u>Bank Debt w/ Swaps</u>	<u>Private Placement</u>
Pricing	Comparable	Comparable
Flexibility of terms	More flexible	Less flexible
Flexibility in obtaining amendments	More flexible / more timely	Less flexible / more formal process
Prepayment penalty	No penalty on bank debt Potential gain or loss on swap(s)	Yes, if negative No gain if positive
Ease of execution	Easier	Harder
Fix rate debt	Must execute interest rate swaps to "fix" the debt rate.	Straightforward
FAS 133 accounting valuations	Yes, must use FAS 133 accounting. May have valuation swings of \$3 - \$5 million over life of debt.	No

ERCOT staff reviewed both options in detail with the Finance and Audit Committee at a special meeting on May 4, 2007. After full discussion of the options, and variations thereof, the Finance and Audit Committee indicated a preference for Option 1 based on its competitive pricing and flexible structure. The Finance and Audit Committee will review the attached resolution at its May 16, 2007 meeting and is expected to formally vote on a recommendation at that time.

Key Factors Influencing Issue:

- Need to fund TNMIP costs not funded with the Nodal Surcharge during development
- Need to fund capital expenditures from base operations not funded with the System Administration Fee
- Need for additional financing to fund timing imbalances between revenue and expenses (working capital)

Alternatives:

- Increase Nodal Surcharge to fully fund TNMIP on a pay-as-you-go basis
- Increase System Administration Fee to fully fund capital expenditures on a pay-as-you-go basis



- Increase System Administrative Fee to build cash reserves sufficient to fund imbalances between cash income and expenses and fund Interest Reserve.
- Reduce spending for capital projects or other budgetary items
- Execute Private Placement or other financing alternates
- Execute expanded or new bank facility with interest rate swap(s)

Conclusion/Recommendation:

ERCOT staff recommends that the BOD authorize ERCOT to negotiate and execute the documents necessary to (a) obtain debt financing of up to \$300 million (in addition to the 2002 Senior Notes and TCR borrowings) and (b) enter into interest rate derivative products of up to \$130,000,000. The requested financing will replace existing revolving and term loan facilities and provide additional borrowing capacity to fund (a) costs related to the TNMIP which are not funded with the Nodal Surcharge during development, (b) capital expenditures from base operations not funded with the System Administration Fee, and (c) working capital needs, all on market terms and interest rates.



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 increase ERCOT' borrowing capacity and negotiate and enter into a new advancing term loan facility with banks for up to \$225,000,000 in principal amount, possibly through a syndicated arrangement, with a term of up to five and one-half years, to be repaid in at least annual installments, at market terms and rates (Term Loan);

WHEREAS, the ERCOT Board deems it desirable and in the best interest of ERCOT, to negotiate and enter into a revolving credit facility with banks for up to \$75,000,000 in principal amount, possibly through a syndicated arrangement, with a term of up to five and one-half years, at market terms and rates, for liquidity purposes (Revolver);

WHEREAS, the Term Loan and Revolver would pay and replace the term loan and revolving credit facility that ERCOT currently has in place, but would be in addition to the outstanding balance of the 2002 Senior Notes;

WHEREAS, the ERCOT Board deems it desirable and in the best interest of ERCOT to obtain fixed rate interest on up to \$130,000,000 of the floating rate \$225,00,000 Term Loan authorized herein;

And WHEREAS the ERCOT Board deems it desirable and in the best interest of ERCOT to negotiate and enter into interest rate derivative products (Interest Rate Agreements) with swap provider(s) for up to \$130,000,000;

THEREFORE, be it RESOLVED that:

1. The Term Loan, Revolver and Interest Rate Agreements described above are hereby authorized and approved in each and every respect;
2. ERCOT may enter into the Term Loan, Revolver and Interest Rate Agreements and that the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, and General Counsel/Corporate Secretary of ERCOT (Authorized Officers) are each hereby severally authorized to determine and approve the terms, conditions, and consideration of such transactions and to execute and deliver, in the name and on behalf of ERCOT, loan and other documentation evidencing and governing the Term Loan, Revolver or Interest Rate Agreements, including without limitation, a commitment letter, fee letter, credit agreement(s), all related promissory notes, all other related loan documentation and all interest rate hedging, swap or other related interest rate derivative documentation, all substantially in form and substance as shall be approved by the officer executing and delivering the same, such approval to be evidenced conclusively by such execution and delivery;



3. The obligations incurred upon such execution and delivery by ERCOT of the loan and other documentation evidencing and governing the Term Loan and Revolver shall be in all respects binding and enforceable obligations of ERCOT;
4. The obligations incurred upon such execution and delivery by ERCOT of the interest rate hedging, swap or other interest rate derivative documentation evidencing and governing the Interest Rate Agreements shall be in all respects binding and enforceable obligations of ERCOT;
5. The ERCOT Board severally designates, authorizes, and empowers each of the Authorized Officers (acting together or individually) to perform or cause to be performed, in the name of ERCOT, all acts and deeds, to pay or cause to be paid, on behalf of ERCOT, all related costs and expenses and to make, execute, and deliver, or cause to be executed and delivered, all such other agreements, consents, approvals, orders, applications, requests, demands, directions, certificates, undertakings, supplements, instruments, documents, further assurances, or other communications of any kind, with or without the corporate seal of ERCOT or otherwise, on behalf of ERCOT or otherwise as he or she may deem necessary, appropriate, or advisable to comply with the intent of the foregoing resolutions or to comply with the requirements of the instruments approved and authorized by the foregoing resolutions, including but not limited to, the loan and other documents evidencing and governing the Term Loan, Revolver or Interest Rate Agreements, and any other certificate, instrument, or document related thereto;
6. All acts and things whether heretofore or hereafter done or performed by any Authorized Officer of ERCOT which are in conformity with the intent and purposes of these resolutions, including but not limited to the execution and delivery of any and all agreements, amendments, supplements, instruments, documents or filings as may from time to time be required, such additional or specific authorizations shall be and the same are hereby in all respects ratified, confirmed, and approved, and adopted as acts by ERCOT; and
7. The Secretary of ERCOT is hereby authorized and empowered to certify to the passage of the foregoing resolutions with or without the seal of ERCOT or otherwise.

- ERCOT's Money Purchase Plan was terminated on March 31, 2007
- Terminated benefit plans are required to undergo a final financial statement audit
- Maxwell, Locke & Ritter, LLP was approved by the Board in February 2007 to perform the final audit of the terminated Money Purchase Plan
- Audit work has been completed and ERCOT has received the desired financial audit opinion
- Seeking Board of Director acceptance of the audit report on May 16, 2007
- Audit report is expected to be distributed to members of F&A Committee May 11, 2007
- Vote

□ Funding

■ Nodal Program

- Costs fully recovered through the Texas Nodal Surcharge and will not be presented in the 2008 budget proposal
- Inclusion Exception - Zonal/Nodal Interdependent projects funded through the System Administration Fee (if approved as filed by ERCOT)

■ Regional Entity

- Statutory functions funded through NERC assessment
- ERCOT compliance functions (non-statutory/Protocol compliance) funded through System Administration Fee
- No change in regional entity organizational structure

■ Market Monitoring

- No change in service anticipated
- Continue to fund through System Administration Fee

□ Expenditures

- Compensation and Staffing
 - Incorporate conclusions from PUCT workforce study (if available)
 - No change in employee benefit plans anticipated
 - Cost fluctuations to be shared between employer and employee
 - Incorporate merit and promotion funding consistent with market practices
 - Adjust for Contra labor to Nodal and Zonal projects
- Hardware/Software maintenance and support - no significant increases anticipated
- Expense Categories – include inflationary adjustment where appropriate

□ Project Funding

- Funding ratio restored - 60% debt / 40% revenue
- Identify and prioritize projects through TAC & F&A
- 2008 revenue requirement includes specific funding for only those projects that are expected to be through the planning phase by December 31, 2007
- Remaining projects are on a “candidate list” and will be considered for implementation after planning is complete
- Include Zonal/Nodal Interdependent projects funded through System Administration Fee (if approved by PUCT)

□ Nodal Program

- All hardware and software necessary to ensure the Nodal market is operational is funded via the Nodal Surcharge
 - Exception: \$37M Zonal/Nodal Interdependent projects
- Personnel resources and staff training required to operate Nodal market are acquired and conducted according to the Nodal Program plan and are funded via the Nodal Surcharge

2008 Budget Development Schedule

Monday, Apr. 23	Executive Committee - 2008 Strategic Planning & Budget Discussion
Monday, May 7	Executive Committee - 2008 Strategic Planning & Budgeting Assumptions
Wednesday, May 16	Board Agenda - Strategic Planning & Budgeting Assumptions <i>(briefing & request for public comment)</i>
Thursday, May 31	Budget Kick-off Meeting Instructions & Templates Distributed
Tuesday, June 5	PUCT Staff - Assumption & Timeline Discussion
Monday, June 18 - Wednesday, June 20	Departmental Submittals reviewed by Divisional VPs
Tuesday, June 19	Finance & Audit Committee Agenda - Budget/PPL Status Update
Wednesday, June 20	Submit Departmental Budget Request
Wednesday, June 20 - Friday, June 22	Calculate & Compile DRAFT Categorical Budget (Budget staff)
Monday, June 25 - Friday, June 29	Preliminary Budget Review by Office-- VP/Director/Manager CFO Review Meetings Budget Revisions (as necessary)
Monday, July 2	Executive Committee - 2008 Preliminary Budget Review (Company/Divisional levels)
Tuesday, July 3 - Friday, July 6	Departmental Adjustments Based on Executive Review
Monday, July 9	Executive Committee - 2008 Budget Final Review
Tuesday, July 10	Begin Testimony Preparation
Tuesday, July 17	Finance & Audit Committee Agenda - Preliminary Budget/PPL Presentation <i>(Courtesy copy to all Board members)</i>
Tuesday, July 17	Public Meeting - Preliminary 2008 Budget Presentation <i>(in conjunction w/Finance & Audit Committee Meeting)</i>
Wednesday, July 18 - Tuesday, July 31	PUCT Staff Review
Thursday, Aug. 2	Finance & Audit Committee Special Meeting - 2008 Budget Review (if necessary)
Friday, Aug. 17	Testimony - 1st Draft Due
Tuesday, Aug. 21	Board Agenda - Finance & Audit Committee 2008 Budget Recommendation and Board Review
Friday, Sept. 7	Testimony Finalized
Tuesday, Sept. 18	Board Agenda - 2008 Budget Approval/Vote
Wednesday, Sept. 19 - Thursday, Sept. 27	Review PUCT Fee Filing
Friday, Sept. 28	PUCT Fee Filing

NOTE
 (1) Schedule assumes PUCT Fee Filing will be required

2008 Budget Development Schedule

Date	Action
Wednesday, Apr. 18	Finance & Audit Committee - Preliminary Budget & Business Plan Discussion
Friday, May 4	Finance & Audit Committee - Special Meeting
Friday, May 11	NERC - First Draft - Preliminary Business Plan and Budget Due (Statutory Functions)
Wednesday, May 16	Finance & Audit Committee/Board - Preliminary Budget Presentation and Final Business Plan Review
Thursday, May 17	Open Meeting - Business Plan and Proposed Budget Presentation
Monday, May 28	Finance & Audit Committee Special Meeting - Budget Review and Recommendation (if necessary)
Friday, Jun. 1	NERC - Final Business Plan and Budget (Draft) due to NERC (Statutory and Non-Statutory Functions)
Thursday, Jun. 19	Board - Final Budget Approval
Thursday, July 12	NERC - Final Board Approved Budget Due

9. Regional Entity Update

Larry Grimm

Statement of Activities 2008 Budget	Total	Statutory Total	Non-Statutory Total
Funding			
ERO Funding	3,178,280	3,178,280	-
Membership Dues	-	-	-
Testing Fees	-	-	-
Services & Software	-	-	-
Workshops	70,000	70,000	-
Interest	-	-	-
Miscellaneous	985,568	-	985,568
Total Funding	4,233,849	3,248,280	985,568
Expenses			
Personnel Expenses			
Salaries	2,242,783	1,682,087	560,696
Payroll Taxes	186,151	139,613	46,538
Benefits	269,134	201,850	67,283
Retirement Costs	262,406	196,804	65,601
Total Personnel Expenses	2,960,474	2,220,355	740,118
Meeting Expenses			
Meetings	73,240	73,240	-
Travel	97,135	93,235	3,900
Conference Calls	1,000	1,000	-
Total Meeting Expenses	171,375	167,475	3,900
Operating Expenses			
Contracts & Consultants	89,000	89,000	-
Office Rent	271,000	203,000	68,000
Office Costs	20,000	17,450	2,550
Professional Services	338,000	256,000	82,000
Computer Purchase & Maint.	-	-	-
Depreciation	-	-	-
Miscellaneous/ Contingency	384,000	295,000	89,000
Total Operating Expenses	1,102,000	860,450	241,550
Total Expenses	4,233,849	3,248,280	985,568

9. Regional Entity Update

Larry Grimm

Statement of Activities 2008 Budget	Functions in Delegation Agreement										
	Statutory Total	Reliability Standards	Compliance & Organization Registration & Certification	Reliability Readiness Audit & Improvement	Reliability Assessment & Performance Analysis	Training & Education	Situational Awareness & Infrastructure Security	General Administrative	Legal & Regulatory	Information Technology	Accounting & Finance
Funding											
ERO Funding	3,178,280	167,668	655,626	58,345	811,514	73,503	46,925	779,024	308,281	124,735	152,659
Membership Dues	-	-	-	-	-	-	-	-	-	-	-
Testing Fees	-	-	-	-	-	-	-	-	-	-	-
Services & Software	-	-	-	-	-	-	-	-	-	-	-
Workshops	70,000	-	-	-	-	70,000	-	-	-	-	-
Interest	-	-	-	-	-	-	-	-	-	-	-
System Administration Fee	-	-	-	-	-	-	-	-	-	-	-
Total Funding	3,248,280	167,668	655,626	58,345	811,514	143,503	46,925	779,024	308,281	124,735	152,659
Expenses											
Personnel Expenses											
Salaries	1,682,087	108,605	447,330	32,368	523,106	38,154	32,368	176,207	163,811	85,670	74,469
Payroll Taxes	139,613	9,014	37,128	2,687	43,418	3,167	2,687	14,625	13,596	7,111	6,181
Benefits	201,850	13,033	53,680	3,884	62,773	4,578	3,884	21,145	19,657	10,280	8,936
Retirement Costs	196,804	12,707	52,338	3,787	61,203	4,464	3,787	20,616	19,166	10,023	8,713
Total Personnel Expenses	2,220,355	143,358	590,476	42,725	690,499	50,363	42,725	232,594	216,231	113,085	98,299
Meeting Expenses											
Meetings	73,240	810	810	-	810	70,000	-	-	810	-	-
Travel	93,235	8,500	4,340	10,620	46,205	10,140	200	6,480	2,740	150	3,860
Conference Calls	1,000	-	-	-	-	-	-	1,000	-	-	-
Total Meeting Expenses	167,475	9,310	5,150	10,620	47,015	80,140	200	7,480	3,550	150	3,860
Operating Expenses											
Contracts & Consultants	89,000	-	-	-	-	-	-	89,000	-	-	-
Office Rent	203,000	-	-	-	-	-	-	203,000	-	-	-
Office Costs	17,450	-	-	-	-	-	-	15,950	500	500	500
Professional Services	256,000	-	-	-	-	-	-	160,000	60,000	-	36,000
Computer Purchase & Maint.	-	-	-	-	-	-	-	-	-	-	-
Depreciation	-	-	-	-	-	-	-	-	-	-	-
Miscellaneous/Contingency	295,000	15,000	60,000	5,000	74,000	13,000	4,000	71,000	28,000	11,000	14,000
Total Operating Expenses	860,450	15,000	60,000	5,000	74,000	13,000	4,000	538,950	88,500	11,500	50,500
Total Expenses	3,248,280	167,668	655,626	58,345	811,514	143,503	46,925	779,024	308,281	124,735	152,659

9. Regional Entity Update

Larry Grimm

Statement of Activities 2008 Budget	Non-Statutory Total	Protocol & Operating Compliance	General Administrative	Legal & Regulatory	Information Technology	Accounting & Finance
Funding						
ERO Funding	-	-	-	-	-	-
Membership Dues	-	-	-	-	-	-
Testing Fees	-	-	-	-	-	-
Services & Software	-	-	-	-	-	-
Workshops	-	-	-	-	-	-
Interest	-	-	-	-	-	-
System Administration Fee	985,568	575,549	221,081	99,277	41,845	47,816
Total Funding	985,568	575,549	221,081	99,277	41,845	47,816
Expenses						
Personnel Expenses						
Salaries	560,696	393,977	58,736	54,604	28,557	24,823
Payroll Taxes	46,538	32,700	4,875	4,532	2,370	2,060
Benefits	67,283	47,277	7,048	6,552	3,427	2,979
Retirement Costs	65,601	46,095	6,872	6,389	3,341	2,904
Total Personnel Expenses	740,118	520,049	77,531	72,077	37,695	32,766
Meeting Expenses						
Meetings	-	-	-	-	-	-
Travel	3,900	3,500	-	200	150	50
Conference Calls	-	-	-	-	-	-
Total Meeting Expenses	3,900	3,500	-	200	150	50
Operating Expenses						
Contracts & Consultants	-	-	-	-	-	-
Office Rent	68,000	-	68,000	-	-	-
Office Costs	2,550	-	2,550	-	-	-
Professional Services	82,000	-	53,000	18,000	-	11,000
Computer Purchase & Maint.	-	-	-	-	-	-
Depreciation	-	-	-	-	-	-
Miscellaneous/Contingency	89,000	52,000	20,000	9,000	4,000	4,000
Total Operating Expenses	241,550	52,000	143,550	27,000	4,000	15,000
Total Expenses	985,568	575,549	221,081	99,277	41,845	47,816

Texas Regional Entity 2008 Budget Update

May 16, 2007

Considerations

- Regional Entities must comply with ERO Rules of Procedure as applicable to functions delegated to the RE by NERC.
 - Compliance Enforcement
 - Reliability Standards Development
 - Organization Registration and Certification
 - Reliability Readiness Evaluation and Improvement
 - Reliability Assessment and Performance Analysis
 - Training and Education
 - Situation Awareness and Infrastructure Security
- A Regional Entity must meet FERC and NERC requirements and maintain good standing as a Regional Entity.
 - NERC shall provide alternative means and resources for implementing NERC functions in the event a Regional Entity does not comply with the rules of procedure and the obligations of the delegation agreement

Key Factors

- ❑ Program requires significant issue tracking, reporting, and follow-up; compliance with rigid and strict timelines and deadlines; extensive communication and interaction with NERC and Registered Entities; up-to-date and accurate web site postings; and complete and detailed documentation.
- ❑ Includes compliance monitoring and enforcement of ERCOT Protocols and Operating Guides as a parallel process to the NERC Program. The Texas RE must follow PUCT-approved ERCOT Compliance Process.
- ❑ Texas RE does not utilize contractors or industry volunteers/experts to assist with Compliance and Readiness Audits.

Overview

- ❑ 169 Registered Entities – 206 functions
- ❑ Additional entities to be registered as PSEs and LSEs
- ❑ 83 FERC-approved NERC Reliability Standards: ~344 requirements & ~393 sub-requirements [excludes Critical Infrastructure Protection (CIP) Standards not yet approved by FERC]
 - Many Reliability Standards apply to multiple Registered Entities
- ❑ Compliance Audits will significantly increase in scope
 - Up to now, the scope of Compliance Audits has included only those standards in the current year's NERC Implementation Plan (those standards selected to be actively monitored during each year)
 - Going forward, the scope of compliance audits will include all of the standards included in the current year and previous three years' NERC Implementation Plans
- ❑ Self-certifications conducted annually on Registered Entities not audited, including spot checks
- ❑ Event investigations

2007 → 2008 Budget Comparisons

- Clearer and improved direction provided by NERC on completing budget docs – as a result, direct line item comparison between 2007 & 2008 budgets is difficult
- Total budget
 - 2007 - \$5,514,219
 - 2008 - \$4,233,849 (23.2% decrease)
- Personnel Costs – Increase by \$270,639 (~10% increase)
 - Average 4% salary increase for existing employees funded for 9 months
 - Proposes 3 new FTEs
 - Texas RE utilizes ERCOT pay grades
- Capital projects – \$1,396,825 in 2007 – (\$0 in 2008)
- Travel – Increase by \$13,916 (16.1% increase)
- Contingency included in 2008 – \$384,000

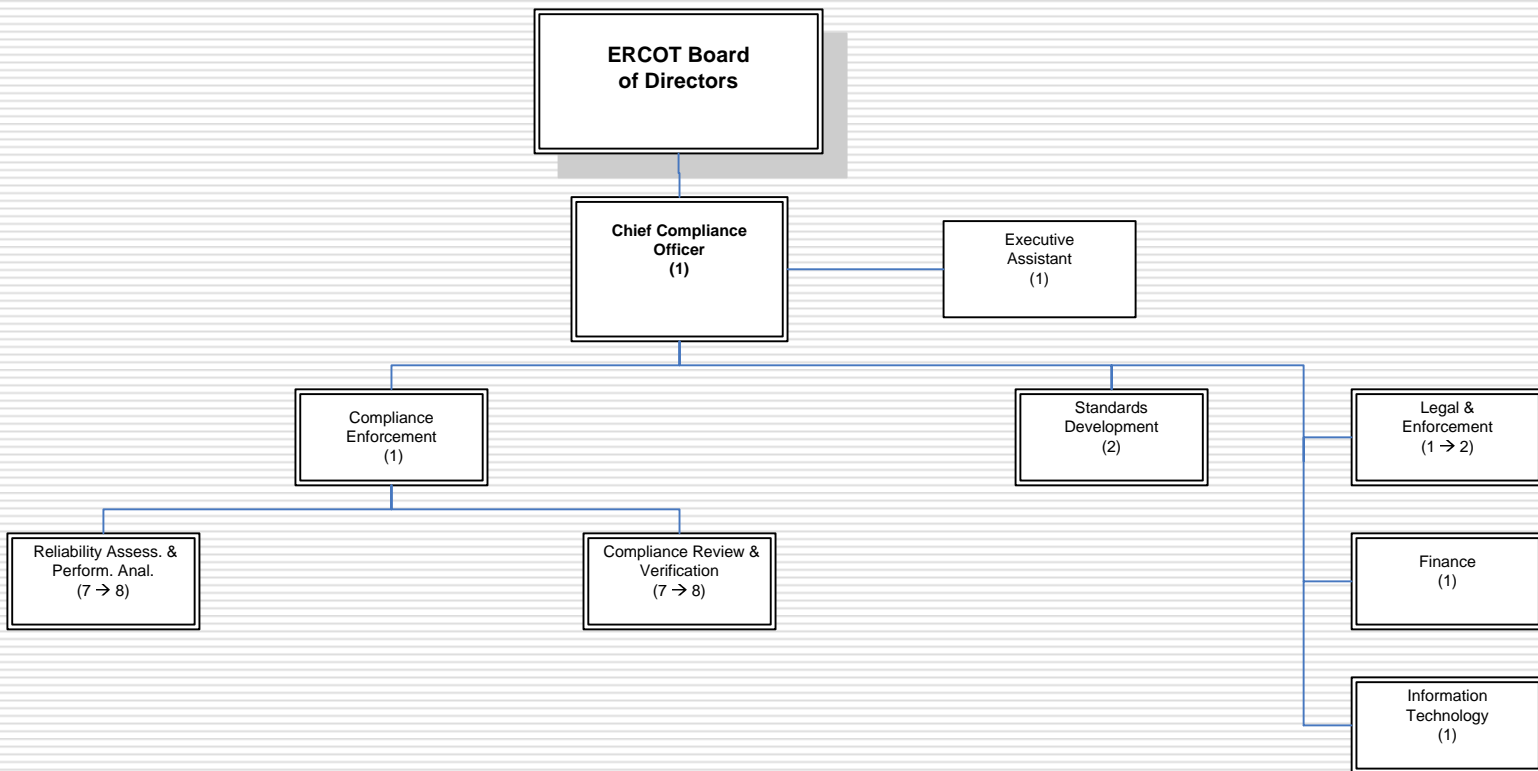
Proposed 2008 Staffing Additions

- ❑ Texas RE currently proposing to increase staff from 22 to 25 in 2008
- ❑ Sr. Compliance Engineer – Provide high level technical support to review and interpret information and data received in the course of conducting compliance activities
- ❑ Records Coordinator – Manage high volume of documents that will be created, received, used, stored, or maintained in the course of compliance activity
- ❑ Sr. Paralegal – Monitors and notifies appropriate Texas RE personnel of PUCT, FERC, legislative, and other governmental matters; performs research and file management of governmental and regulatory matters for the Texas RE; and assists with preparation of ERCOT Board packet

2007 Texas RE Budget Variances

- 2007 Budget developed assuming structural separation of Texas RE
 - Personnel expenses – Projected to be ~\$598,000 under budget
 - Anticipated “go-live” date for the ERO and Regional Entities was January 2007
 - 13 of 22 positions filled to date
 - Computer purchase & maintenance – Projected to be ~\$900,000 under budget
 - Capital projects re-evaluated resulting in cancellations
 - No initial computer equipment costs – IT equipment provided through ERCOT
 - Furniture & equipment – Projected to be ~\$575,000 under budget
 - Depreciation originally included – will not be utilized because it is a non-cash expense
 - Office costs – Projected to be ~\$61,000 under budget
 - Budget assumed complete autonomy – cost of leased space, office equipment, telephone, internet, etc. less
- Total projected under budget for 2007 ~\$2,134,000
 - Unspent 2007 budget will be applied to the 2008 budget

Texas Regional Entity Organization (2007 → 2008)



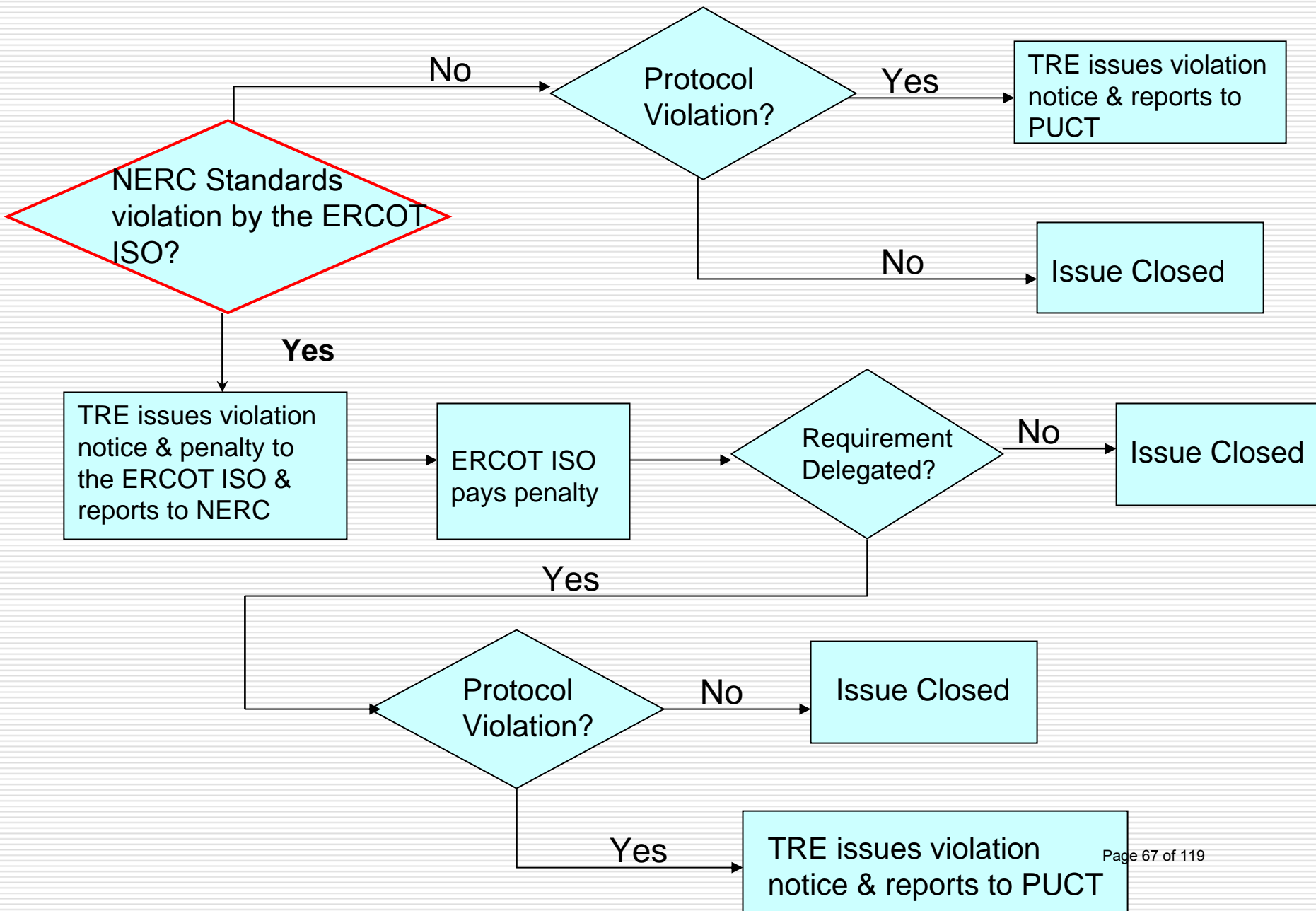
Personnel Analysis

Total FTEs by Program Area	2007	2008	Change
Operational Programs			
Reliability Standards Program	2	2	0
Compliance Enforcement and Organization and Certification Program	7	8	1
Reliability Readiness Audits and Improvement Program	.5	.5	0
Training, Education, and Personnel Certification Program	.5	.5	0
Reliability Assessment and Performance Analysis Program	6.5	7.5	1
Situational Awareness and Infrastructure Security Program	.5	.5	0
Operational Programs Total FTEs	17	19	2
Administrative Program			
Members Forums	0	0	0
General and Administrative	2	2	0
Information Technology	1	1	0
Legal and Regulatory	1	2	1
Human Resources	0	0	0
Finance and Accounting	1	1	0
Administrative Programs Total FTEs	5	6	1
Total FTEs	22	25	3

2008 Texas RE Budget Development Schedule

Date	Action
Wednesday, Apr. 18	Finance & Audit Committee - Preliminary Budget & Business Plan Discussion
Friday, May 4	Finance & Audit Committee - Special Meeting
Friday, May 11	NERC - First Draft - Preliminary Business Plan and Budget Due (Statutory Functions)
Wednesday, May 16	Finance & Audit Committee/Board - Preliminary Budget Presentation and Final Business Plan Review
Thursday, May 17	Open Meeting - Business Plan and Proposed Budget Presentation
Monday, May 28	Finance & Audit Committee Special Meeting - Budget Review and Recommendation (if necessary)
Friday, Jun. 1	NERC - Final Business Plan and Budget (Draft) due to NERC (Statutory and Non-Statutory Functions)
Thursday, Jun. 19	Board - Final Budget Approval
Thursday, July 12	NERC - Final Board Approved Budget Due

NERC Standards Violation- Delegated Requirements



2008 Proposed Budget

Statement of Activities 2008 Budget	Total	Statutory Total	Non-Statutory Total
Funding			
ERO Funding	3,178,280	3,178,280	-
Membership Dues	-	-	-
Testing Fees	-	-	-
Services & Software	-	-	-
Workshops	70,000	70,000	-
Interest	-	-	-
Miscellaneous	985,568	-	985,568
Total Funding	4,233,849	3,248,280	985,568
Expenses			
Personnel Expenses			
Salaries	2,242,783	1,682,087	560,696
Payroll Taxes	186,151	139,613	46,538
Benefits	269,134	201,850	67,283
Retirement Costs	262,406	196,804	65,601
Total Personnel Expenses	2,960,474	2,220,355	740,118
Meeting Expenses			
Meetings	73,240	73,240	-
Travel	97,135	93,235	3,900
Conference Calls	1,000	1,000	-
Total Meeting Expenses	171,375	167,475	3,900
Operating Expenses			
Contracts & Consultants	89,000	89,000	-
Office Rent	271,000	203,000	68,000
Office Costs	20,000	17,450	2,550
Professional Services	338,000	256,000	82,000
Computer Purchase & Maint.	-	-	-
Depreciation	-	-	-
Miscellaneous/ Contingency	384,000	295,000	89,000
Total Operating Expenses	1,102,000	860,450	241,550
Total Expenses	4,233,849	3,248,280	985,568

2008 Proposed Budget

Statement of Activities 2008 Budget	Functions in Delegation Agreement										
	Statutory Total	Reliability Standards	Compliance & Organization Registration & Certification	Reliability Readiness Audit & Improvement	Reliability Assessment & Performance Analysis	Training & Education	Situational Awareness & Infrastructure Security	General Administrative	Legal & Regulatory	Information & Technology	Accounting & Finance
Funding											
ERO Funding	3,178,280	167,668	655,626	58,345	811,514	73,503	46,925	779,024	308,281	124,735	152,659
Membership Dues	-	-	-	-	-	-	-	-	-	-	-
Testing Fees	-	-	-	-	-	-	-	-	-	-	-
Services & Software	-	-	-	-	-	-	-	-	-	-	-
Workshops	70,000	-	-	-	-	70,000	-	-	-	-	-
Interest	-	-	-	-	-	-	-	-	-	-	-
System Administration Fee	-	-	-	-	-	-	-	-	-	-	-
Total Funding	3,248,280	167,668	655,626	58,345	811,514	143,503	46,925	779,024	308,281	124,735	152,659
Expenses											
Personnel Expenses											
Salaries	1,682,087	108,605	447,330	32,368	523,106	38,154	32,368	176,207	163,811	85,670	74,469
Payroll Taxes	139,613	9,014	37,128	2,687	43,418	3,167	2,687	14,625	13,596	7,111	6,181
Benefits	201,850	13,033	53,680	3,884	62,773	4,578	3,884	21,145	19,657	10,280	8,936
Retirement Costs	196,804	12,707	52,338	3,787	61,203	4,464	3,787	20,616	19,166	10,023	8,713
Total Personnel Expenses	2,220,355	143,358	590,476	42,725	690,499	50,363	42,725	232,594	216,231	113,085	98,299
Meeting Expenses											
Meetings	73,240	810	810	-	810	70,000	-	-	810	-	-
Travel	93,235	8,500	4,340	10,620	46,205	10,140	200	6,480	2,740	150	3,860
Conference Calls	1,000	-	-	-	-	-	-	1,000	-	-	-
Total Meeting Expenses	167,475	9,310	5,150	10,620	47,015	80,140	200	7,480	3,550	150	3,860
Operating Expenses											
Contracts & Consultants	89,000	-	-	-	-	-	-	89,000	-	-	-
Office Rent	203,000	-	-	-	-	-	-	203,000	-	-	-
Office Costs	17,450	-	-	-	-	-	-	15,950	500	500	500
Professional Services	256,000	-	-	-	-	-	-	160,000	60,000	-	36,000
Computer Purchase & Maint.	-	-	-	-	-	-	-	-	-	-	-
Depreciation	-	-	-	-	-	-	-	-	-	-	-
Miscellaneous/Contingency	295,000	15,000	60,000	5,000	74,000	13,000	4,000	71,000	28,000	11,000	14,000
Total Operating Expenses	860,450	15,000	60,000	5,000	74,000	13,000	4,000	538,950	88,500	11,500	50,500
Total Expenses	3,248,280	167,668	655,626	58,345	811,514	143,503	46,925	779,024	308,281	124,735	152,659

2008 Proposed Budget

Statement of Activities 2008 Budget	Non-Statutory Total	Protocol & Operating Compliance	General Administrative	Legal & Regulatory	Information Technology	Accounting & Finance
Funding						
ERO Funding	-	-	-	-	-	-
Membership Dues	-	-	-	-	-	-
Testing Fees	-	-	-	-	-	-
Services & Software	-	-	-	-	-	-
Workshops	-	-	-	-	-	-
Interest	-	-	-	-	-	-
System Administration Fee	985,568	575,549	221,081	99,277	41,845	47,816
Total Funding	985,568	575,549	221,081	99,277	41,845	47,816
Expenses						
Personnel Expenses						
Salaries	560,696	393,977	58,736	54,604	28,557	24,823
Payroll Taxes	46,538	32,700	4,875	4,532	2,370	2,060
Benefits	67,283	47,277	7,048	6,552	3,427	2,979
Retirement Costs	65,601	46,095	6,872	6,389	3,341	2,904
Total Personnel Expenses	740,118	520,049	77,531	72,077	37,695	32,766
Meeting Expenses						
Meetings	-	-	-	-	-	-
Travel	3,900	3,500	-	200	150	50
Conference Calls	-	-	-	-	-	-
Total Meeting Expenses	3,900	3,500	-	200	150	50
Operating Expenses						
Contracts & Consultants	-	-	-	-	-	-
Office Rent	68,000	-	68,000	-	-	-
Office Costs	2,550	-	2,550	-	-	-
Professional Services	82,000	-	53,000	18,000	-	11,000
Computer Purchase & Maint.	-	-	-	-	-	-
Depreciation	-	-	-	-	-	-
Miscellaneous/Contingency	89,000	52,000	20,000	9,000	4,000	4,000
Total Operating Expenses	241,550	52,000	143,550	27,000	4,000	15,000
Total Expenses	985,568	575,549	221,081	99,277	41,845	47,816

Texas Regional Entity (RE)
2008 Business Plan and Budget

Draft 1
May 8, 2007

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Introduction

Total Texas RE Resources (in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	22.0	22.0	25.0
Total Direct Funding	1,890,205		1,883,582
Total Indirect Funding	2,980,550		1,364,698
Total Funding	4,870,755		3,248,280

The Federal Power Act (FPA) and FERC Regulations establish requirements for the formation of an Electric Reliability Organization (ERO). The ERO's primary mandate is to develop, implement, and verify compliance to a uniform set of standards designed to ensure and, over time, enhance the ongoing reliability of the bulk power system. The voluntary system of standards will be replaced with a mandatory system that a single ERO will administer, under the oversight of the Federal Energy Regulatory Commission (FERC) in the United States.

The Federal Power Act and FERC's regulations recognize the role of regional entities in monitoring and enforcing compliance within the regional area, along with strong ERO oversight. Regional entities will perform many of the activities necessary to support NERC's statutory obligations as the ERO. NERC has proposed detailed requirements for the Regional Compliance Programs in its rules of procedure. NERC and the regional entities are modifying their existing programs and procedures to meet these requirements.

Under the new system of mandatory reliability standards, regional entities will, after entering into a FERC-approved delegation agreement, fulfill certain functions currently performed by the Regional Reliability Councils. In anticipation of meeting the criteria in the Federal Power Act for becoming a regional entity, an independent reliability entity is being established in ERCOT to develop and enforce reliability standards within the ERCOT Region. As proposed, the new entity, the Texas Regional Entity (RE), will consist of the following functional areas:

- Compliance
- Reliability Standards
- Legal/Regulatory/Enforcement
- Corporate Operations

The Texas RE must maintain clear independence and not be unduly influenced by the owners, operators, and users of the bulk power system being monitored. The Texas RE will be functionally unbundled from the ERCOT ISO and will report to the ERCOT Board of Directors for administrative purposes. All possible compliance actions for violations of NERC and ERCOT-Specific Standards and ERCOT reliability-based Protocols and Operating Guides requirements will be referred to the Public Utility Commission of Texas (PUCT) for action as follows:

- Possible compliance actions for violation of a NERC or ERCOT-Specific Standard – The PUCT will review the report from Texas RE Compliance, decide whether some form of sanction is appropriate, hear any additional information and arguments pertaining to the reported violation, and issue a recommended decision. The Texas RE Chief Compliance Officer (CCO) will then make a final decision with respect to enforcement, and the issue will be forwarded to the ERO and FERC. Due process will be provided to any entity that is reported to have violated a standard, in accordance with requirements developed by FERC or NERC.
- Possible compliance actions for violation of an ERCOT reliability-based Protocol or Operating Guide requirement – The PUCT will review the report from Texas RE Compliance, decide whether some form of sanction is appropriate, hear any additional information and arguments pertaining to the reported violation, and render a final decision. Due process will be provided to any entity that is reported to have violated a standard, in accordance with requirements of State law.

The ERO and Texas RE Compliance shall determine and may levy monetary penalties and non-monetary sanctions and remedial actions against owners, operators and users of the bulk power system for violations of the requirements of NERC and ERCOT-Specific Reliability Standards. NERC has developed processes and principles for determining penalties, sanctions, and remedial actions. Adjustment factors can be used to allow some degree of discretion and flexibility needed to address each violation on its merits.

The Texas RE will follow these key principles in carrying out its delegated functions:

Regional Entity Resources – The Texas RE shall have sufficient resources to meet delegated compliance enforcement responsibilities, including the necessary professional staff, to manage and implement the Texas RE Compliance Monitoring and Enforcement Program (CMEP).

Regional Entity Staff Independence – Texas RE Staff must maintain clear independence from the ERCOT ISO and all ERCOT Market Participants that are expected to comply with the reliability standards and will not be unduly influenced by the owners, operators, and users of the bulk power system being monitored. The independence of the Texas RE staff is a critical element to ensure that the CMEP is carried out in a fair and consistent manner. The Texas PUCT will monitor the independence of the Texas RE from the ERCOT ISO and stakeholder operations.

Regional Entity CMEP Content – All approved reliability standards shall be included in the Texas RE CMEP for all owners, operators, and users within the defined boundaries of the Texas RE.

Compliance Audits – The Texas RE will maintain a program of proactive enforcement audits. Each owner, operator, and user of the bulk power system responsible for complying with NERC and applicable regional reliability standards shall be audited by the Texas RE in carrying out the CMEP.

Processes – All regional programs must contain processes for data reporting, auditing, assessing, penalizing and sanctioning violators, and mitigating non-compliance.

In accordance with Section 215(b) of the FPA, FERC has certified NERC as the ERO. The functions of the ERO are to develop and adopt reliability standards for the bulk power systems and to file such reliability standards, and any modifications to such standards, with FERC for approval; to enforce approved reliability standards by imposing a penalty on an owner, operator, or user of the bulk power system for violation of an approved reliability standard if the ERO finds, after notice and opportunity for hearing, that the owner, operator, or user of the bulk power system has violated a reliability standard; and to conduct periodic assessments of the reliability and adequacy of the bulk power systems in North America. The FERC Rule also requires the ERO to have “an audit program that provides for rigorous audits of compliance with reliability standards by users, owners and operators of the bulk power system” and to report its assessments of the reliability and adequacy of the bulk power system to FERC and the Secretary of Energy on a periodic basis. As the ERO, NERC will perform all of the above described functions.

To facilitate the ERO’s performance of the responsibilities described in the preceding paragraph, the FERC Rule requires each owner, operator, and user of the bulk power system within the continental United States to register with the ERO in accordance with the rules of the ERO. In addition, the ERO may, with approval of FERC, enter into agreements with regional entities by which the ERO delegates its authority to the regional entity to develop, propose, and enforce reliability standards for specific geographic regions. In its ruling issued on April 19, 2007, the FERC accepted the Texas RE Delegation Agreement.

Communication

The Texas RE will communicate with the industry, regulators, and other stakeholders by application of protocols that will be developed for each program area. This is a key element in the direction to continue building cooperative relationships with all segments of the industry through consistent messages. A notable example is the close working relationship the Texas RE will continue to have with ERCOT Stakeholder Groups such as the Technical Advisory Committee and the Reliability and Operations Subcommittee and its working groups to assure understanding of where activities can be mutually beneficial.

The Texas RE will continue to enhance its website with increased attention to ease of use and user preferences. More timely information that can be more easily found will ultimately improve not only the efficiency of operations, it will provide an improved platform for providing critical information to the industry and the public.

Finally, the established links between the regional entities and NERC must continue to thrive and improve. Not only will 2008 be the first full year for enforcement activities by NERC as the ERO in the United States, it will be the first full year of operation in the context of approved delegation agreements with Regional Entities. The 2008 plan calls for continued efforts to assist the regional entities in carrying out their delegated compliance enforcement, registration, and certification activities.

Actions following Certification/Recognition as the Regional Entity

The Texas RE will conduct the activities described in the following sections within the boundaries of the ERCOT Region. The Texas RE will excel in the execution of the plans laid out by each program area in 2008 through organized scheduling and tracking of activities within the program areas. As an example, a key milestone in the initiation of ERO and Texas RE activities is the completion of a compliance registry for all users, owners, and operators of the

bulk power system in the United States. Registration and certification of the organizations responsible for complying with the standards will be an ongoing activity requiring accurate tracking and record keeping. In addition, 2008 will represent the first full year for the compliance monitoring and enforcement program with mandatory compliance to approved reliability standards including the delegated regional compliance enforcement programs. Vital elements of this program are tracking the mitigation of identified violations of standards and the management of enforcement action appeals.

Section A — 2008 Business Plan

Reliability Standards Program

Reliability Standards Program Resources (in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	2.0	2.0	2.0
Total Direct Funding	288,757		167,669
Total Indirect Funding	350,653		143,652
Total Funding	639,410		311,321

Background

The Texas RE may develop, through its own processes, separate Standards that go beyond, add detail to, or implement NERC Reliability Standards; obtain a Regional Variance; or that cover matters not addressed in NERC Reliability Standards. Regional Criteria may be developed and exist in ERCOT Protocols, Operating Guides, and/or Procedures separately from NERC Reliability Standards, or may be proposed as NERC Reliability Standards. Regional Criteria that exist separately from NERC Reliability Standards shall not be inconsistent with or less stringent than NERC Reliability Standards.

ERCOT-Specific Standards shall provide for as much uniformity as possible with reliability standards across the interconnected bulk power system of the North American continent. An ERCOT-Specific Standard shall be more stringent than a continent-wide reliability standard, including a regional difference that addresses matters that the continent-wide reliability standard does not, or shall be a regional difference necessitated by a physical difference in the bulk power system. An ERCOT-Specific Standard that satisfies the statutory and regulatory criteria for approval of proposed North American reliability standards, and that is more stringent than a continent-wide reliability standard, would generally be acceptable.

Standards Process

The Texas RE Reliability Standards Development Process will be overseen by a Reliability Standards Committee (RSC) whose purpose is to see that all stakeholder interests are fairly represented in the development of regional reliability standards. The RSC will be a broad-based, representative committee consisting of representatives from each of the seven ERCOT Market Participant segments. Participation is open to any person or entity with an interest in the reliability of the ERCOT Bulk Power System.

Among other responsibilities, the RSC will review each proposal for development of a new regional reliability standard, or modification of an existing regional reliability standard, to determine if the proposal should be pursued. If it so determined, the RSC will forward to the ERCOT Reliability and Operations Subcommittee (ROS) to appoint a reliability standard drafting team that has the necessary technical expertise, competencies, and diversity of views needed to develop the proposed standard. Development of each regional reliability standard will include at least one time period for receipt of public comment before the proposed standard is

submitted for an approval vote. For the purpose of adopting each proposed reliability standard, a separate “ballot pool” will be established comprised of ERCOT Member Representatives from the seven Market Participant Segments that have an interest in voting on that particular standard. After receiving an affirmative vote by the ballot pool, a regional reliability standard will be submitted to ERCOT’s Board for approval. Finally, if approved by the Board, the regional reliability standard will be forwarded to NERC for approval and filed with FERC for its approval. Once FERC approves a standard and the effective date reached, compliance with the standard is legally binding on all applicable owners, operators, and users of the ERCOT Bulk Power System.

The Texas RE Reliability Standards Development Process is designed to build and verify consensus for each Regional Standard. The open, inclusive, balanced, and transparent process ensures that the resulting standards are just, reasonable, and nondiscriminatory. Participation by industry experts and compliance personnel ensures that the standards are technically sound, unambiguous, and measurable.

The Texas RE Reliability Standards Group will be responsible for coordinating and facilitating all aspects of the regional reliability standards development process. Staff will be actively involved in the NERC Reliability Standards Program, participate on Standards Drafting Teams and participate on NERC Readiness Audits. The Reliability Standards Group will review each reliability standard and notify impacted entities of any new requirements as well as communicate all reliability standards-related information to stakeholders. The group will also be responsible for reviewing all proposed ERCOT Protocol and Operating Guides Revisions to ensure there are no conflicts with Regional-Specific and NERC Reliability Standards, and coordinating the Texas RE review of all proposed Protocol and Operating Guides Revisions. Staff will also identify any possible training needed by responsible entity personnel to promote understanding and compliance with the new or revised reliability standards.

Transition to the Texas Regional Entity

On March 15, 2007 FERC approved 83 reliability standards that were proposed by the ERO. Until implementation and enforcement of mandatory reliability standards begins, ERCOT Compliance will continue to actively monitor compliance with a subset of the reliability standards now approved by FERC. The mandatory reliability standards approved by FERC apply to users, owners and operators of the bulk power system designated by NERC through its compliance registry procedures. While the approved reliability standards are immediately enforceable, FERC’s Final Rule directs the ERO and the future regional entities to focus resources on the most serious violations during an initial period through December 31, 2007. Enforcement discretion will also be used with regard to all applicable users, owners, and operators of the bulk power system, and not just to those new to the reliability scheme. This approach will help allow the Texas RE to ensure that the compliance monitoring and enforcement processes work as intended and all entities have time to implement the new processes. ERCOT Compliance will also continue to make changes to and refine its organization registration list to help ensure that compliance monitoring and enforcement applies to the correct entities.

Following the approval of the delegation agreement between NERC and the Texas RE, ERCOT Board approval of ERCOT Bylaws changes will be sought to address the formation of the Texas RE. Additional staff will also be added, in accordance with the approved Texas RE Budget which will allow the Texas RE to be ready to implement and enforce reliability standards.

Standards Program Goals and Objectives

The goals of the Regional Reliability Standards Program for 2008 are to:

- Meet all FERC and NERC directives with regard to regional reliability standards development and procedures.
- Work closely with the ERO and ERCOT Market Participants to develop separate regional reliability standards that go beyond, add detail to, or implement NERC Reliability Standards; obtain a Regional Variance; or otherwise address issues that are not addressed in NERC Reliability Standards.
- Develop regional reliability standards such that they achieve their reliability objective without causing undue restrictions or adverse impacts on competitive electricity markets.
- Ensure consistency and quality of regional reliability standards.
- Communicate with stakeholders and regulators regarding standards development – both NERC and regional reliability standards.
- Streamline and improve the Texas RE Reliability Standards Development Process and associated tools.
- Ensure the topics addressed by the regional reliability standards keep pace with changing industry needs
- Develop and revise standards directed by FERC and NERC.
- Be actively involved in the NERC Reliability Standards Program and participate on Standards Drafting Teams.
- Administer and facilitate a comprehensive program to develop new regional reliability standards and improve existing regional standards that meet the quality characteristics in the Texas RE Standards Development Process.
- Coordinate the Texas RE review of all proposed ERCOT Protocol and Operating Guides Revisions to ensure there are no conflicts with region-specific and NERC Reliability Standards.
- Actively participate on the NERC Regional Reliability Standards Working Group.
- Complete development of remaining regional “fill-in-the-blank” standards.
- Ensure Texas RE Standards Development Process is aligned to meet agreed-upon expectations.
- Revise standards development rules and procedures in response to FERC directives.
- Evaluate alternatives and improvements that ensure consensus is being achieved in an efficient manner.
- Evaluate and improve ballot performance (quorums and balance).
- Formalize a feedback loop for continuous improvement.
- Improve drafting team guidelines.
- Develop standards program communications that educate and inform stakeholders and support the Texas RE Standards Development Program objectives.

Compliance Enforcement and Organization Registration and Certification Program

Compliance Monitoring and Enforcement and Organization Registration and Certification Program Resources			
(in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	6.0	7.0	8.0
Total Direct Funding	1,180,655		655,626
Total Indirect Funding	1,051,959		574,610
Total Funding	2,232,614		1,230,236

Background

The purpose of the Texas RE Compliance Monitoring and Enforcement Program (CMEP) is to maintain the reliability of the ERCOT Bulk Power System. NERC oversees each Region's Compliance Program and each region is responsible for reviewing the compliance of its members with NERC and regional reliability standards and requirements. Going forward, this will be accomplished by:

- Monitoring and enforcing compliance with the NERC and regional reliability standards and requirements for all entities within ERCOT, including the ERCOT ISO.
- Reporting all violations of all standards, including regional standards, to NERC.
- Maintaining processes for data gathering, reporting, investigating, auditing, assessing, penalizing and sanctioning violators, and mitigating non-compliance.
- Performing the compliance and enforcement functions of the NERC CMEP by exercising the authority delegated to the Texas RE by NERC in its delegation agreement.

There are eight sources of an alleged violation, according to the Compliance Monitoring and Enforcement Program: self report, self certification, audit report, investigation, exception report, spot check, complaint, or a data submittal.

Monitoring, auditing, investigating, and enforcing compliance with reliability standards by owners, operators, and users of the bulk power system, like the development and adoption of the regional reliability standards, is at the core of the Texas RE's mission. Through a rigorous program of monitoring, audits, and investigations; mitigation activities; and the imposition of penalties and sanctions for non-compliance with reliability standards, the Texas RE will strive to maintain a high level of reliable operation of the ERCOT Bulk Power System by its owners, operators, and users. Ensuring the reliable operation of the bulk power system will benefit all owners, operators, and users of the ERCOT Bulk Power System and, ultimately, all users and consumers of electric power in the ERCOT Region which will provide a broad-based benefit to the public and will be in the public interest.

2008 is the first full year the Compliance Monitoring and Enforcement Program will be responsible for mandatory compliance to approved reliability standards, including the delegated

regional compliance enforcement programs. Texas RE Staff will work closely with NERC Staff to achieve maximum efficiency. Compliance data collection, analysis, and reporting to the regulatory authorities will be enhanced based on the regulators requests and data collection, analysis, and reporting tools developed.

Registration and, in some cases, certification of the organizations responsible for complying with the standards will be an ongoing activity.

Texas RE Compliance Staff also supports the development of compliance administration elements. This undertaking requires a significant amount of work and coordination with the standards program and Regional Entities to review and update the compliance administration elements of all standards. NERC and Regional Entity Staff will develop effective compliance violation security levels, data retention requirements, and monitoring methods that work in concert with the requirements and measures within the standards.

The Texas RE plans to implement a Compliance Data Management System that will be used by the Texas RE beginning in late 2007 and into 2008. The Compliance Data Management System contains a module to collect compliance information from Registered Entities.

Compliance Review and Verification

The Texas RE must maintain clear independence and not be unduly influenced by the owners, operators, and users of the bulk power system being monitored. One of two proposed sections in the Texas RE Compliance Area will be the Compliance Review and Verification Group which will focus on the following:

- Selectively monitor system operations and extract data at various intervals to meet reporting requirements and assess performance and compliance with NERC and ERCOT-Specific Standards.
- Periodic data submittal review and analysis
- Data and document management
- Compliance issue management and tracking
- Compliance procedure development and management
- Impact assessment of new/revised NERC Standards on ERCOT Protocol and Operating Guides requirements.
- Maintain entity/organization registration and contact information (see below for additional detail)
- Address issues as a result of self-reporting, exception reporting, and complaints (incident report)
- Compliance reporting to the PUCT, NERC, and stakeholders
- Audit training
- Capital project development, tracking, and oversight of projects in support of the Texas RE to fulfill its delegated functions

Compliance Review and Verification will also have the following objectives:

- Maintain working relationships between NERC and the Texas RE in order to achieve maximum effectiveness and consistency of monitoring, reporting, enforcement actions, and appeals.

- Assure timely mitigation of all violations of standards and requirements.
- Assess the effectiveness of enforcement actions in mitigating violations of standards.
- Enhance processes, databases, and reporting tools to allow for seamless, uniform reporting of alleged and confirmed violations of standards, proposed penalty and sanction actions, and disposition of all violations.
- Report all alleged violations of standards and penalties and sanctions applied to compliance violations to NERC and the appropriate governmental authorities through established processes.
- Report quarterly all confirmed violations of NERC or approved regional standards for which investigatory, decisional, and appeal processes have been completed, including the identity of the organizations involved in these violations.
- Track the mitigation of identified violations of standards.

Organization Registration and Certification Objectives

Organization registration identifies those entities that are responsible for compliance with reliability standards. The Organization Registration and Certification Function is the direct responsibility of REs. Owners, operators, and users of the bulk power system shall provide to their respective RE such information as is necessary to complete the registration. All information is forwarded to NERC.

Some entities that are registered as responsible reliability entities will have to meet certain criteria to demonstrate that they are able to perform the tasks required by the standards. Texas RE Compliance will administer an Organization Registration and Certification Program to meet NERC's program goals and requirements. The program goals will be accomplished by audits and periodic reviews.

ERCOT Compliance has been leading an effort to register all entities that are users, owners, and operators of the bulk power system that will be responsible for complying with NERC Reliability Standards. The latest draft list includes:

- 107 Generator Owners
- 30 Generator Operators
- 29 Transmission Planners
- 31 Transmission Owners
- 2 Distribution Providers with responsibility for complying with the requirements of the under-frequency load shedding program
- ERCOT ISO (Reliability Coordinator, Transmission Operator, Balancing Authority, Planning Authority, Resource Planner, Transmission Service Provider, and Purchasing Selling Entity)

The Texas RE will maintain an accurate registration list of all owners, operators, and users of the bulk power system for compliance monitoring purposes.

- Update and confirm the registration list as needed (at least annually).
- Provide necessary registration information to NERC and appropriate government authorities.

- Review the completeness of the organization registration list and determine if additional efforts are necessary to identify other entities or collect more information from bulk power system owners, operators, and users.

The Texas RE will also implement organization certification.

- Maintain processes and procedures for carrying out the delegated certification activities that are required by the certification standards.
- Conduct certification audits scheduled in 2008.

Compliance Report Generation – It is anticipated that 50 to 60 Compliance Reports will be written each year as a result of audits and investigations conducted by Texas RE Compliance Staff. It is most efficient and effective to have staff available that has specific expertise in writing reports. This would allow the Texas RE Compliance Staff to monitor and enforce compliance with NERC Standards and ERCOT-Specific Standards.

Proposed Additional Staff for 2008

Records/Document Coordinator – The Texas RE will have a high volume of documents that will be created, received, used, stored, or maintained in the course of business as evidence of business activity. It is essential that the Texas RE manage this information and these records. The current draft ERCOT Compliance Registry contains 169 Registered Entities that will be engaged in one or more compliance activities (Compliance Audits, Readiness Audits, Organization Certification Audits, Self-certifications, Spot checks, Investigations, & Critical infrastructure Protection Standards compliance) each year. Each activity can potentially produce numerous documents that must be retained and managed.

Reliability Readiness Evaluation and Improvement Program

Reliability Readiness Evaluation and Improvement Program Resources (in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	1.0	0.5	0.5
Total Direct Funding	0		58,345
Total Indirect Funding	175,326		35,913
Total Funding	175,326		94,258

Background

The NERC Reliability Readiness Evaluation and Improvement Program was developed in response to the August 2003 blackout in the Northeastern United States and Canada. Readiness evaluations are comprehensive reviews of entities operating the bulk power system and are conducted to ensure that operators of the bulk power system have facilities, tools, processes, and procedures in place to operate reliably under future conditions. NERC's reliability readiness evaluations identify opportunities for improvement and examples of excellence that help the evaluated entity, and other entities, improve their ability to operate the bulk power system. These reviews help Balancing Authorities, Transmission Operators, and Reliability Coordinators recognize and assess their reliability responsibilities and evaluate how their operations support those responsibilities.

In 2005, NERC expanded the coverage of its Reliability Readiness Evaluation and Improvement Program to include local control centers – those local control centers performing delegated tasks. In ERCOT, these entities might include Transmission Operator Sub-Entities and QSEs with Resources. In 2006, NERC continued to expand the coverage of its readiness evaluations to include additional local control centers with the objective to review all entities that perform bulk power system reliability functions. Readiness evaluations are conducted on a three-year cycle. Reliability readiness evaluation teams consist of industry volunteers with appropriate technical expertise. Evaluation teams prepare and publicly publish a report of the team's findings on the NERC Web Site.

Reliability Readiness Evaluation and Improvement Objectives

- Before additional NERC Reliability Readiness Evaluations of ERCOT Transmission Owner and Qualified Scheduling Entity Local Control Centers (LCC) are conducted, development of criteria to determine which, if any, LCCs will be subject to readiness evaluations must be completed. A determination on what frequency they will be conducted should also be made (i.e., 3-year cycle, 5-year cycle, etc.).
- Once criteria are established, Texas RE Staff will work with NERC Staff to schedule appropriate readiness evaluations – including co-leading the evaluation team, assisting audited entities in developing mitigation plans for implementing recommendations from the reliability readiness audits, and tracking those mitigation plans to completion.
- In conjunction with NERC, develop a process for verifying the implementations of the readiness evaluation recommendations.

- Report quarterly the status and mitigation of each recommendation identified in the reliability readiness evaluation process.
- Texas RE Compliance and Standards Staff is expected to participate on six NERC Reliability Readiness Evaluations in 2008.
- Perform an assessment of the Reliability Readiness Audit and Improvement Program to evaluate the success and effectiveness of the program in achieving its mission as it relates to LCCs.

Training, Education, and Operator Certification Program

Training, Education, and Operator Certification Program Resources (in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	0.5	0.5	0.5
Total Direct Funding	0		143,503
Total Indirect Funding	87,663		35,913
Total Funding	87,663		179,416

Background

ERCOT Compliance continues to play a key role in System Operator training activities. ERCOT Compliance Staff chairs and actively participates on the Operations Training Seminar Oversight Working Group which is responsible for developing, planning, arranging, and monitoring the annual ERCOT Operations Training Seminar. The working group is responsible for measuring how the Seminar is meeting its objectives which are to provide training on power system fundamentals, current events, issues related to marketing, and other timely issues determined by the working group. Despite including subjects on various issues, emphasis is placed on topics that focus on enhancing the performance of bulk power system operating personnel. The target audience for the seminar is ERCOT ISO System Operators, Qualified Scheduling Entity (QSE) Operators, and Transmission/Distribution System Provider (TDSP) Operators and those who provide management, supervision, and support for the operators. The seminar is also open to Power Generation Company (PGC) Operators, Wholesale Power Marketers, Retail Electric Providers, and others associated with the bulk power system.

Training, Education, and Operator Certification Objectives

Participating in the development of training and education programs for bulk power system operating personnel and the other targeted audiences of these programs will be an important component of the Texas RE. Providing a training and education program for the operating personnel of owners, operators, and users of the bulk power systems of North America relating to their compliance with regional reliability standards and other reliability-related job functions will help to achieve a high level of knowledge and competence among these operating personnel in the performance of their reliability-related functions. It also helps to promote a culture of compliance within the industry, and thereby will help to further ensure the reliable operation of the ERCOT Bulk Power System.

Beginning in 2007, NERC Continuous Education Hours (CEH) were offered for attending the ERCOT Training Seminar. System Operators attending the seminar received up to 19 CEHs. Many of these hours can also be used to satisfy NERC and ERCOT requirements for system emergency training.

Auditor training for Texas RE Staff who participate in audits and investigations conducted by the Texas RE will also be developed and maintained.

Texas RE Staff will also continue to coordinate and facilitate the ERCOT Operator Certification Test given to System Operators and operations support personnel. Texas RE Staff will continue to maintain and update the ERCOT Fundamentals Training Manual which was designed and written to serve as a study tool for System Operator Certification Tests and to serve as a readily available reference document. The Manual contains descriptions of fundamental topics in electrical power and ERCOT power system operations.

Reliability Assessment and Performance Analysis Program

Reliability Assessment and Performance Analysis Program Resources (in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	7.5	6.5	7.5
Total Direct Funding	312,761		811,514
Total Indirect Funding	1,314,949		538,697
Total Funding	1,627,710		1,350,211

Background

As described earlier, the purpose of the Texas RE Compliance Monitoring and Enforcement Program (CMEP) is to maintain the reliability of the ERCOT Bulk Power System. NERC oversees each Region's Compliance Program and each region is responsible for reviewing the compliance of its members with NERC and regional reliability standards and requirements. Going forward, this will be accomplished by:

- Monitoring and enforcing compliance with the NERC and regional reliability standards and requirements for all entities within ERCOT, including the ERCOT ISO.
- Reporting all violations of all standards, including regional standards, to NERC.
- Maintaining processes for data gathering, reporting, investigating, auditing, assessing, penalizing and sanctioning violators, and mitigating non-compliance.
- Performing the compliance and enforcement functions of the NERC CMEP by exercising the authority delegated to the ERCOT Regional Entity (RE) by NERC in its delegation agreement.

There are eight sources of an alleged violation, according to the Compliance Monitoring and Enforcement Program: self report, self certification, audit report, investigation, exception report, spot check, complaint, or a data submittal.

Monitoring, auditing, investigating, and enforcing compliance with reliability standards by owners, operators, and users of the bulk power system, like the development and adoption of the regional reliability standards, is at the core of the Texas RE's mission. Through a rigorous program of monitoring, audits, and investigations, mitigation activities, and the imposition of penalties and sanctions for non-compliance with reliability standards, the Texas RE will strive to maintain a high level of reliable operation of the ERCOT Bulk Power System by its owners, operators, and users. Ensuring the reliable operation of the bulk power system will benefit all owners, operators, and users of the ERCOT Bulk Power System and, ultimately, all users and consumers of electric power in the ERCOT Region, will provide a broad-based benefit to the public and will be in the public interest.

The current CMEP has focused on the ERCOT ISO and those ERCOT Entities that are performing delegated Balancing Authority (BA) and Transmission Operator (TOP) Tasks. This includes 30 Qualified Scheduling Entities (QSEs) with resources and 16 Transmission Operator Sub-Entities. There have been a few selected standards and requirements that have applied to other entities such as Transmission and Generator Owners.

Currently, there are 83 FERC-approved NERC Reliability Standards and more are in the standards development and approval process. These 83 approved standards have nearly 350 requirements and nearly 400 sub-requirements.

A key component of the CMEP is conducting compliance audits of all responsible entities, which are expected to significantly increase as a result of the increased number of entities being registered as users, owners, and operators of the bulk power system. The Texas RE will maintain a program of proactive enforcement audits. Each owner, operator, or user of the bulk power system responsible for complying with NERC and regional reliability standards and requirements shall be audited by the Texas RE. A Compliance Audit is a process in which a detailed review of an owner, operator, or user of the bulk power system is performed to determine if that owner, operator, or user of the bulk power system is complying with approved reliability standards. Compliance Audits are currently conducted on a three-year cycle and an audit report is issued for each audit.

In years when an entity does not receive a Compliance Audit, Texas RE Compliance may request compliance self-certification from the entity using electronic forms developed and distributed by Texas RE Compliance. The entity must certify that it is in compliance with each designated measure or disclose any non-compliance and submit the self-certification to Texas RE Compliance by the date specified in the request by Texas RE Compliance. Spot checks may be performed by Texas RE Compliance on a sample of these self-certifications by telephone or site visit. Deficiencies found in self-certifications and spot checks will be treated as if they were audit findings.

The ERCOT Region is required to conduct periodic assessments of the reliability and adequacy of the ERCOT Bulk Power System. In accordance with this responsibility the ERCOT Region prepares three reliability assessments each year: a long-term reliability assessment report; a summer assessment report; and a winter assessment report. These reports analyze electricity demand and the adequacy of supply in the ERCOT Region as well as examine the adequacy of the transmission system. The Texas RE will review these assessments and submit them to NERC as required. Reliability assessment reports will also be prepared as conditions warrant. Results of independent assessments of the overall reliability and adequacy of the ERCOT Bulk Power System will be reviewed and reported for 2008 summer, 2008/2009 winter, and 2008-2017.

Further, the Texas RE will analyze significant events that occur on the ERCOT Bulk Power System. Significant events occasionally occur involving the ERCOT Transmission System and Generation Resources. Often, these events require investigation to determine the root cause and to identify lessons learned and whether the event was an isolated occurrence or one that requires further analysis. This analysis is needed to determine if the system(s) and equipment involved are operating correctly and are being properly applied, maintained, and/or tested.

Compliance Enforcement Program Objectives

The Reliability Assessment and Performance Analysis Group will focus on the following:

- Compliance Audits
- Readiness Audits
- Organization Certification Audits
- Self-certifications

- Spot checks
 - Investigations
 - Critical infrastructure Protection Standards compliance
- a. Audits
- i. Through 2006, ERCOT Compliance has been conducting Compliance Audits on 16 ERCOT Transmission Operator Sub-Entities and 30 Qualified Scheduling Entities (QSE) with Resources on a three-year cycle – approximately 15 each year. In accordance with ERO requirements, the Texas RE will audit all entities responsible for complying with NERC and regional reliability standards. Audits will be performed on a three-year cycle for the following registered entities: Transmission Owners/Planners (29), including those with Transmission Operator Sub-Entities; Distribution Providers (2); Generator Operators (30); and the ERCOT ISO (TOP, PA, RC, TSP, BA, & RP). It is proposed that the following registered entities be audited on a 6-year cycle: Generator Owners (107). This will increase the number of audits to 169 (~39 each year). The Texas RE is currently reviewing the need to expand the list of Registered Entities to include Purchasing-Selling Entities (PSE) and Load Serving Entities (LSE). There are currently approximately 103 PSEs (~34 additional audits each year) and 34 LSEs (~11 additional audits each year). If these entities are registered, the Texas RE proposes that they be audited on a 6-year cycle. This would increase the number of audits by 137 (23 each year).
 - ii. Although not yet clearly defined, ERCOT’s 16 Transmission Operator Sub-Entities and 30 QSEs with Resources (Local Control Centers) may also receive Reliability Readiness Audits on a three-year cycle (~15 each year).
 - iii. Organization Certification Audits of TOPs, RCs, and BAs may also be performed. It has not yet been determined if those entities performing delegated TOP (16 ERCOT Transmission Operator Sub-Entities) and BA (30 QSEs with Resources) tasks will need to be certified or which additional entities will require certification, or whether Reliability Readiness Audits will be used in place of Organization Certification Audits.
 - iv. Regional Compliance Staffs will also participate on NERC Reliability Readiness Audit Teams (entities outside ERCOT). Texas RE Staff will plan to participate on six (6) NERC Reliability Readiness Audits.
 - v. As the number of entities being NERC-certified increases, the number of responsible entities in ERCOT will increase and a larger number of annual Self-Certifications will be required (~130 each year – TO/TP, DP, GO, & GOP Functions + ERCOT ISO). Spot checks will be performed as needed (~15 to 25 each year). Additional annual self-certifications will be required for PSEs and LSEs (~114 each year). Spot checks will be performed as needed (~10 to 20 each year).
- b. Investigations of significant events that jeopardize the reliability of all or part of the ERCOT system will be required. Texas RE Compliance will investigate events using the data gathered from the ERCOT ISO and involved entities. From the data gathered, Texas RE Compliance will develop a report that includes findings, observations, and recommendations. In 2006, 52 events were reported to ERCOT Compliance. Of those 52 events, 10 events met requirements that required closer review by ERCOT Compliance. Of those 10 events, 3 required a detailed investigation and report.
- c. Currently penalties and sanctions are not enforced for non-compliance with NERC Reliability Standards (simulated penalties are calculated and reported to NERC). Careful consideration will be required when determining penalties and sanctions for non-

compliance to ensure consistency and comparability. This is because of the number of mitigating (potential to reduce the penalty) and aggravating (potential to increase the penalty) factors that can be considered when determining the seriousness of the violation.

- d. Because penalties and sanctions will be enforced, appeals of violations as well as penalties and sanctions will likely occur. These appeals will need to be addressed.

Proposed Additional Staff for 2008

Senior Compliance Engineer – Additional staff is required to provide high level technical support to review and interpret information and data received in the course of conducting compliance activities. The Senior Compliance Engineer will provide a resource with extensive technical experience to assist other compliance staff and perform technical assessments and other duties as determined to meet the needs of reliability functions.

Situation Awareness and Infrastructure Security Program

Situation Analysis and Infrastructure Security Program Resources			
(in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	0.0	0.5	0.5
Total Direct Funding	108,032		46,925
Total Indirect Funding	0		35,913
Total Funding	108,032		82,838

Background

This function will monitor and enforce compliance with the Critical Infrastructure Protection (CIP-001 thru 009) Standards, report any non-compliance to the ERO, and determine and assess penalties and sanctions. The intent of the NERC Cyber Security Standards is to ensure that all entities responsible for the reliability of the bulk power system identify and protect critical cyber assets that control or could impact the reliability of the bulk power system. The CIP Standard Requirements are being communicated to all responsible entities to ensure compliance in accordance with the Cyber Security Standards Implementation Plan. This requires a significant amount of communication with the ERCOT Security Department and entities responsible for complying with the CIP Standards. Compliance Audits, self-certifications, and spot checks will be required to verify compliance.

Responsible Entities must begin work to become compliant with a requirement, substantially compliant with a requirement, compliant with a requirement, and auditably compliant with a requirement in accordance with the CIP Standards Implementation Schedule. The implementation plan specifies a compliance schedule for NERC Functional Model Entities. Each Functional Model Entity is required to demonstrate progress towards compliance in accordance with the compliance schedule. The ERCOT ISO is the only designated Balancing Authority (BA), Transmission Operator (TOP), and Reliability Coordinator (RC) in the ERCOT Region and was required to self-certify compliance to NERC's Urgent Action Cyber Security Standard 1200. As such, the ERCOT ISO must be either compliant or substantially compliant with all CIP Standards Requirements by the end of the second quarter 2008; either auditably compliant or compliant with all of the CIP Standards Requirements by the end of the second quarter 2009; and auditably compliant with all CIP Standards Requirements by the end of the second quarter 2010.

Entities registered in ERCOT as Transmission Owners, Generator Owners, Generator Operators, or Load-Serving Entities should begin work on being compliant with all CIP Standards Requirements during the second quarter 2007. These entities must also be substantially compliant or compliant with all CIP Standards Requirements within twelve months after registration is completed; compliant or auditably compliant with all CIP Standards Requirements within twenty-four months after registration is completed; and auditably compliant with all CIP Standards Requirements within thirty-six months after registration is completed. All new Responsible Entities must also become compliant with all CIP Standards Requirements in accordance with the compliance schedule.

Texas RE Compliance will continue to play an active role during the implementation of the CIP Standards Requirements. To provide time for Responsible Entities to examine their policies and procedures, to assemble the necessary documentation, and to meet the requirements of the CIP Standards, compliance assessment will begin in 2007. Status reports will also be requested from Responsible Entities that are not required to be auditably compliant until 2010 to verify that entities are on schedule and meeting the implementation plan.

Administrative Services

Administrative Services Resources			
(in whole dollars)			
	2007 Budget	2007 Projection	2008 Budget
Total FTEs	5.0	5.0	6.0
Total Direct Funding	2,980,550		1,364,698
Total Indirect Funding	0		0
Total Funding	2,980,550		1,364,698

General and Administrative

The Chief Compliance Officer (CCO) shall carry on the general affairs of the Texas RE as the chief executive officer. The CCO will be independent of any market participant, and will be an independent member of the staff of ERCOT, reporting exclusively to the ERCOT Board. The CCO shall be responsible for:

- Overseeing and managing the activities of the Texas RE
- Retaining or terminating outside counsel or other advisors as deemed appropriate
- Making an annual report and periodic reports to the ERCOT Board concerning the activities and expenditures of the Texas RE
- Ensuring that the Texas RE files all required reports with NERC
- Monitoring the expenditures of the monies received by the Texas RE to ensure that such are deployed in accordance with the approved Texas RE Budget (in cooperation with the Finance Staff)
- Making employment-related decisions for all employees of the Texas RE
- Performing such other duties as may be determined from time to time by the ERCOT Board, for the benefit of the Texas RE

An Executive Assistant will be responsible for providing executive-level administrative support to the Texas Regional Entity (RE) Chief Compliance Officer (CCO). The Executive Assistant will also perform general office manager activities and provide support to other Texas RE Staff as needed.

Members' Forums

N/A

Information Technology

IT Staff will provide a broad range of Information Technology support to the Texas RE. IT Staff will perform a variety of technical and administrative tasks in the development, deployment, and ongoing support of computer applications and systems and provide training and technical support to users on them. IT Staff will assist in the design, implementation, and management of the Texas RE Website to support the communication of information to the market and will participate in the design and development of database models, web-enabled applications, data extraction and delivery methods, and data presentation. Other IT objectives include:

- Determining long-term system needs.
- Assist the Compliance Group on Critical Infrastructure Protection Standards compliance enforcement as needed.
- Assist in determining system and hardware needs for the Texas RE.
- Liaison with ERCOT IT Staff related to IT systems and tools.
- Assist in ensuring all information systems are functional and secure, and that all applications running on those systems meet business requirements for performance, availability, and security.

2007 Budgeted Positions – 1

2007 Projection – 1

2008 Budgeted Positions – 1

Legal and Regulatory

Legal staff is required to provide legal assistance and counsel to Texas RE Staff on all corporate legal matters with primary emphasis on regulatory enforcement proceedings and related legislative matters involving the Texas Legislature, PUCT, FERC, and NERC. The Texas RE Legal Staff will represent the Texas RE in its quasi-prosecutorial role in PUCT, FERC, and NERC enforcement and rulemaking proceedings and supervise outside counsel responsible for larger enforcement matters. Additional objectives include:

- Participate in all settlement processes and review all settlements for consistent application of settlement principles.
- Review all enforcement actions for consistent application in all violations of standards.
- Manage all enforcement action appeals.

2007 Budgeted Positions – 1

2007 Projection – 1

2008 Budgeted Positions – 2

Proposed Additional Staff for 2008

Sr. Paralegal – Oversees and coordinates the preparation of Texas RE filings with the PUCT, FERC, Texas Legislature, and other governmental and regulatory entities; monitors and notifies appropriate Texas RE personnel of PUCT, FERC, legislative, and other governmental matters; and performs research and file management of governmental and regulatory matters for the Texas RE. The Sr. Paralegal will manage complex procedural requirements including interpretation of legal procedure, case file management, protecting confidential information, and ensuring timely compliance with legal filing requirements. This position will also assist with preparation of ERCOT Board Packet and agenda, as needed.

Human Resources

Human Resources support will be provided by ERCOT, Inc. The Texas RE Executive Assistant will liaise with the ERCOT Human Resources Department to ensure that human resources policies and procedures, including staffing, compensation, benefits, employee relations, and training and development are communicated to Texas RE Staff.

Finance and Accounting

Finance Staff is required to formulate and monitor the Texas RE budget for controlling funds to implement the Texas RE's objectives and will also review and evaluate the performance of key processes for maintaining tight financial controls in a cost-effective and efficient manner. Finance Staff will guide the annual budget process for the Texas RE and measure performance of all key aspects of the Texas RE to ensure performance matches or exceeds expectations, including the analysis of trends affecting budget needs and developing periodic financial reports. Finance Staff will liaise with ERCOT Finance Staff to ensure all finance and budget-related requirements are communicated, met, and adhered to.

2007 Budgeted Positions – 1

2007 Projection – 1

2008 Budgeted Positions – 1

Section B — 2008 Budget

2007 Projection and 2008 Budget Comparison

Table 1

Statement of Activities 2008 Budget		2007 Projection	2008 Budget	Variance
Funding				
	ERO Funding	\$ 4,870,755	\$ 3,178,280	\$ (1,692,475)
	Membership Dues	-	-	-
	Testing Fees	-	-	-
	Services & Software	-	-	-
	Workshops	-	70,000	70,000
	Interest	-	-	-
Total Funding		\$ 4,870,755	\$ 3,248,280	\$ (1,622,475)
Expenses				
Personnel Expenses				
	Salaries	\$ 1,187,000	\$ 1,682,088	\$ 495,088
	Payroll Taxes	106,800	139,613	32,813
	Benefits	154,310	201,850	47,540
	Retirement Costs	118,700	196,804	78,104
Total Personnel Expenses		\$ 1,566,810	\$ 2,220,355	\$ 653,545
Meeting Expenses				
	Meetings	\$ 1,500	\$ 73,240	\$ 71,740
	Travel	35,000	93,235	58,235
	Conference Calls	250	1,000	750
Total Meeting Expenses		\$ 36,750	\$ 167,475	\$ 130,725
Operating Expenses				
	Consultants	\$ 110,000	\$ 89,000	\$ (21,000)
	Contracts	-	-	-
	Office Rent	63,300	203,000	139,700
	Office Costs	5,000	17,450	12,450
	Professional Services	525,000	256,000	(269,000)
	Computer Purchase & Maint.	-	-	-
	Miscellaneous/Contingency	253,900	295,000	41,100
Total Operating Expenses		\$ 957,200	\$ 860,450	\$ (96,750)
Total Expenses		\$ 2,560,760	\$ 3,248,280	\$ 687,520
Change in Assets		\$ 2,309,995	\$ -	\$ (2,309,995)

Summary Explanation

Funding

- **ERO Funding (2008 only)** — New mandatory funding mechanism. Funding required through the LSEs (or designee) is the net of total expenses less funding from all other sources detailed below. Does not include additional funding to return reserve balances to approved levels.
- **Membership Dues (2007 only)** — Funding from regional reliability councils under voluntary membership agreements.
- **Testing Fees** — Fees charged to system operators for administration of system operator certification program.
- **Services and Software** — Fees charged to support the maintenance of various services and software programs (see Appendices A and B for details)
- **Interest** — Interest earned on bank balances.

Expenses

- **Salaries** —
- **Payroll Taxes** —
- **Benefits** —
- **Savings & Retirement** —
- **Meetings** —
- **Travel** —
- **Contracts & Consultants** —
- **Office Rent** —
- **Office Costs** —
- **Professional Services** —
- **Computer Purchases and Maintenance** —
- **Furniture & Equipment** —

Detailed analysis of income and expenses are contained in the following appendices:

- **Appendix X** — 2007 projection and 2008 budget by program category. Each program's sources of funding and related expenses are analyzed.
- **Appendix X** — 2007 projection and 2008 budget by statement of activity section. An expanded view of each line item on the statement of activities is shown.
- **Appendix X** — 2007 projection by program category including system of accounts code detail. Shown are detailed schedules by funding, personnel, meetings, and operations.
- **Appendix X** — 2008 budget by program category including system of accounts code detail. Shown are detailed schedules by funding, personnel, meetings, and operations.

Personnel Analysis

Table 2

Total FTE's by Program Area	2007 ¹	2008 ²	Change
Operational Programs			
Reliability Standards Program	2.0	2.0	0.0
Compliance Enforcement and Organization and Certification Program	6.0	8.0	1.0
Reliability Readiness Audits and Improvement Program	1.0	0.5	0.0
Training, Education and Personnel Certification Program	0.5	0.5	0.0
Reliability Assessment and Performance Analysis Program	7.5	7.5	1.0
Situational Awareness and Infrastructure Security Program	0.0	0.5	0.0
Operational Programs Total FTEs	17.0	19.0	2.0
Administrative Program			
Members Forums	0.0	0.0	0.0
General and Administrative	2.0	2.0	0.0
Information Technology	1.0	1.0	0.0
Legal and Regulatory	1.0	2.0	1.0
Human Resources	0.0	0.0	0.0
Finance and Accounting	1.0	1.0	0.0
Administrative Programs Total FTEs	5.0	6.0	1.0
Total FTEs	22.0	25.0	3.0

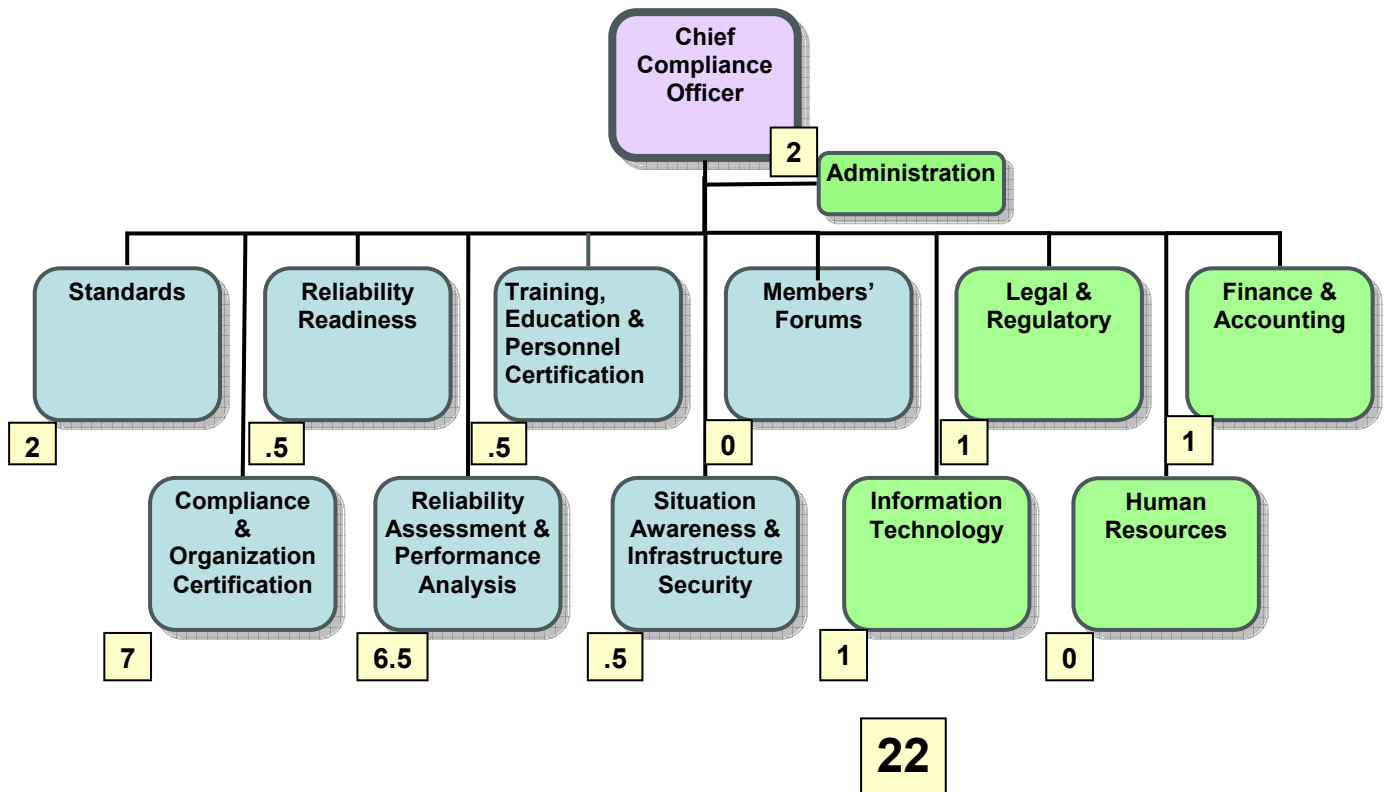
¹ Total FTEs are projected by year-end. As of this draft, there were 13 FTEs on staff leaving 9 positions to be filled.

² Total FTEs are projected to be 22 as of January 1, 2008.

2007 Organizational Chart

Shown below in Table 3 is the organizational chart for 2007, including the staff expected to be hired in each program area by the end of 2007.

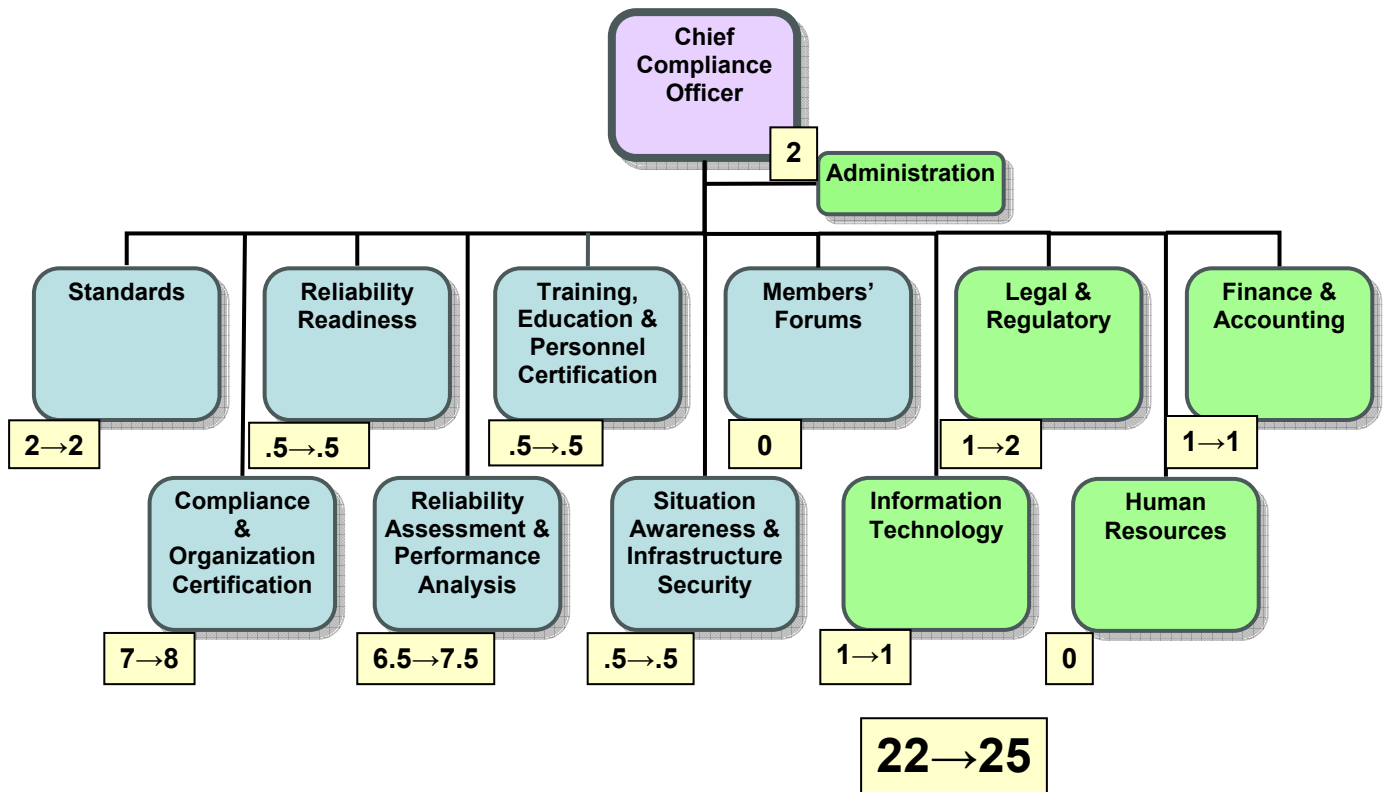
Table 3



2008 Organizational Chart

Shown below in Table 4 is the organizational chart for 2008 with the 2007 staffing levels, plus the additional staff that will be hired to support the increased ERO activities in 2008.

Table 4



Group Discussion

ERCOT Market Credit Status

as of 3/31/2007

as of 4/30/2007

Exposure in the ERCOT Market (owed to ERCOT)

QSEs that meet ERCOT Creditworthiness Standards

Ratings over BBB-

# of QSEs	Estimated Aggregate Liability (\$)	% of EAL	Total Unsec Credit Limit / Security Posted	
5	31,409,390	9%	58,000,000	U

# of QSEs	Estimated Aggregate Liability (\$)	% of EAL	Total Unsec Credit Limit / Security Posted	
(Note 1)				
6	14,892,024	5%	52,026,345	U

QSEs that do not meet ERCOT Creditworthiness Standards

Ratings below BBB- or not rated

Cash & Letters of Credit

Guarantee Agreements

43	160,366,631	46%	286,824,934	S
13	157,412,395	45%	444,275,122	S
61	349,188,416	100%		

44	155,869,023	52%	307,562,161	S
12	126,541,570	43%	431,747,955	S
62	297,302,617	100%		

Total Exposure

Other QSEs in the ERCOT Market (ERCOT owes)

QSEs that meet ERCOT Creditworthiness Standards

Ratings over BBB-

13	(11,891,788)	-24%	96,026,345	U
----	--------------	------	------------	---

11	(12,129,384)	-26%	92,000,000	U
----	--------------	------	------------	---

QSEs that do not meet ERCOT Creditworthiness Standards

Ratings below BBB- or not rated

Cash & Letters of Credit

Guarantee Agreements

50	(25,195,642)	-51%	22,104,971	S
8	(12,797,854)	-26%	155,200,000	S
71	(49,885,284)	-100%		

37	(17,058,705)	-37%	10,317,452	S
8	(17,177,210)	-37%	168,200,000	S
56	(46,365,299)	-100%		

Total

Total

132

118

U: Unsecured since these QSEs meet the creditworthiness standards

S: Secured i.e. required to post collateral since these QSEs do not meet the creditworthiness standards

Note 1: The decrease in the number of QSEs between March and April 2007 is due to eliminating certain inactive QSEs that have left the market from the stats.

ALERT RELIABLE COUNCIL OF TEXAS, INC.
RISK MANAGEMENT EVENT PROFILE MATRIX (as of May 1st, 2007)

Strategic Position	Operational Excellence	Market Facilitation	Grid Reliability	Reporting	Compliance
<p> Strategy Development</p> <p><i>Objective setting adequately incorporates informed stakeholder input, market realities and management expertise</i></p> <p>ERCOT Board and Staff need awareness of ERCOT's short and long-range strategic plan. The Nodal project and the proposed ERO/RE environment have been adequately factored into plans.</p>	<p> Performance Monitoring</p> <p><i>Clearly defined performance metrics linked to mission and goals; actively monitored, status communicated and corrective action taken</i></p> <p>Management has rolled out a revision of the Executive Dashboard based on defined KPI's and have instituted regular Quarterly Business Reviews to discuss key business activities in addition to weekly executive team meetings, constant grid monitoring, IT SLA's, and generation / transmission assessments.</p>	<p> Customer Choice</p> <p><i>Market design promotes efficient choice by customers of energy providers with effective mechanisms to change incumbent market participants as desired.</i></p> <p>IT components supporting Customer Choice are currently not at the desired levels to meet SLA's. Successful replacement of SeeBeyond Application with TIBCO has had a significant impact on Customer Choice operations which has reduced overall levels of risk, however other IT related Retail issues continue.</p>	<p> Grid Operations</p> <p><i>Information required to operate the grid is efficiently gathered and appropriate tools are prudently configured to efficiently operate the system</i></p> <p>Current tools utilized by (including the State Estimator and the accuracy /availability of SCADA data) need continuing maintenance and enhancement. An Operator Training Simulator will be operational in May 2007. Improved accuracy of Load Forecast. Emergency Interruptible Load Program implemented.</p>	<p> Review Practices</p> <p><i>Prudent measures are taken to insure that company disclosures are properly vetted and not misleading</i></p> <p>Board of Director's review of management activities on an ongoing basis assists in ensuring proper review and disclosure practices.</p>	<p> Legal & Legislative</p> <p><i>Operations are conducted in compliance with all laws and regulations and current and proposed legislation is understood and communicated</i></p> <p>Increased efforts have been made to inform members of the legislature about ERCOT and the performance of its functions. Enhanced efforts are being undertaken to maintain records according to established record retention policies.</p>
<p> Mission and Goals</p> <p><i>Corporate objectives and performance standards are understood and followed</i></p> <p>Current management initiatives related to goal setting and the development of Key Performance Indicators (KPI's) have increased awareness of organizational goals and related to high-level corporate objectives and priorities for individual divisions, departments, and employees.</p>	<p> Business Practices</p> <p><i>Business planning, processes and management standards are effective and efficient</i></p> <p>Disaster recovery plans are currently below desired expectations. Additional development activities required to implement and test these procedures. However solid overall business practices are confirmed via: Internal and External audit, Operational review, Regional Entity / Compliance, and RMC and Disclosure Committee review.</p>	<p> Nodal Implementation</p> <p><i>Nodal Implementation is progressing in a timely fashion on budget and schedule within a defined scope.</i></p> <p>Risks continue to exist with scope management and deliverable tracking. Scope management has improved. Vendor resourcing and internal staffing has improved significantly. Risks exists in time line management, software quality (unknown) and software integration. Market readiness assessment is underway. Financial risk over approval of surcharge exists until PUCT ruling are complete.</p>	<p> Planning</p> <p><i>Long-range planning methods enable efficient responses to necessary system changes to maintain reliability standards</i></p> <p>Lack of timely and accurate information necessary to build reasonable system models and forecasts and insufficient ability to conduct long-range (6-10 years out) planning resulting in possible inefficiencies in ERCOT's transmission expansion plan.</p>	<p> Disclosure</p> <p><i>Reporting and other disclosures to intended parties is timely, accurate and effective</i></p> <p>A Disclosure Committee has been institutionalized to discuss and report issues related to external reporting and compliance.</p>	<p> Internal Control Compliance</p> <p><i>Internal Control Compliance, processes and management standards are effective and efficient</i></p> <p>Audit findings are actively monitored by management as well as Internal Audit. Additional training activities are required to ensure all staff members are aware of ongoing internal control compliance processes and procedures.</p>
<p> Reputation</p> <p><i>Positive perceptions by stakeholders typically lead to less cost and greater flexibility resulting in enhanced enterprise value</i></p> <p>High visibility of initial Nodal implementation impact ERCOT reputation as could increased scrutiny on ERCOT activities occurring during the bi-annual state legislative session. Additional focus is on ERCOT's transmission and generation adequacy planning as a valued, objective, and knowledgeable resource to regulators, legislators, and the market.</p>	<p> Work Force</p> <p><i>Organization design, managerial and technical skills, bench strength and reward systems are aligned with corporate goals</i></p> <p>The number of open employment positions has declined to less than 60 openings but certain positions in the IT area remain hard to fill. Contractor usage remains high. Overcrowding has lead to morale issues. Employee turnover has remained consistent at 11%.</p>	<p> Counterparty Credit</p> <p><i>Bankruptcies and other capital deficiencies increase the cost for market participants and potentially impact Grid reliability through participant failure</i></p> <p>Processes for removing defaulting participants from the market increases the potential for credit losses. A medium to large market participant default could materially impact the ERCOT market, grid reliability, and ERCOT's reputation. Recent PRR's related to shortening the timeframe related to drops to POLR have reduced exposure by an estimated 37%.</p>	<p> Bulk System Resources</p> <p><i>Market Participants have constructed and made available adequate bulk electric grid resources</i></p> <p>Uncertainty surrounding generation projects, installed and operational capacity, and the high dependency on natural gas in Texas' generation fleet may impact reliability. The risk exists for a hotter than normal summer or cooler winter to increase load demand to a level that reduces reserve margins below acceptable minimum levels.</p>	<p> Communication</p> <p><i>Internal and external communications are timely and effective</i></p> <p>A crisis management project for communications has been completed and ERCOT has restructured its legal and communications departments. Issues remain relating to the effective communications of retail systems outages on an ongoing and consistent basis.</p>	<p> Industry Standards</p> <p><i>Business practices provide stakeholders with required assurances of quality</i></p> <p>SAS 70 Audit Issues and qualifications remain to be addressed with remediation activities underway to address preliminary findings. Also, new NERC Physical / Cyber Security Standards have been approved and are in the process of being adopted. In addition to SAS 70 Audit Issues, ERCOT has outstanding issues with filings related to its retirement and benefit plans.</p>
<p> Fiscal Management</p> <p><i>ISO design requires competent, prudent and cost effective provision of services</i></p> <p>Current fiscal practices are effective in managing and controlling costs. Adequacy of Nodal budget and staffing allocation to be addressed through the updated Nodal surcharge filing.</p>	<p> Technology Infrastructure</p> <p><i>Information systems and data are effectively managed and are reliable</i></p> <p>Loss of Disaster Recovery Coordinator is being managed by Enterprise Architecture team while search for replacement continues. AIX conversion project is underway and risks for database migration to new platforms are being mitigated.</p>	<p> Administration, Settlement & Billing</p> <p><i>Market rules are fairly applied to all participants and accounting is timely and accurately reflects electricity production and delivery</i></p> <p>ERCOT's settlement/dispute processes has a significant number of ADR's related to the RPRS policy debate outstanding, however these are being addressed in a timely fashion. Increased levels of ADR's may pose a future risk if they are no longer able to be timely addressed.</p>	<p> Operational Responsibility</p> <p><i>Market participants conduct their operations in a manner which facilitates consistent grid reliability</i></p> <p>Response of generators to grid operation events has been improving. Enhanced enforcement of NERC standards and ERCOT Protocols and Operating Guides will exist through the ERO / TRE and IMM. Increased wind generation will present additional operational challenges.</p>	<p> Adequacy and Integrity</p> <p><i>Robust processes exist to support management assertions embodied within financial reports</i></p> <p>Financial and Operations management information has been redesigned to enable management to effectively monitor and manage the business.</p>	<p> Regulatory Filings</p> <p><i>Evidence, testimony and other supporting materials are compelling and successful</i></p> <p>Filings are completed timely and accurately.</p>

Legend: Elevated Risk Level

Reduced Risk Level

(New Risk Categories / Descriptions Indicated in Green)

Rationale for Category Risk Assessment Changes

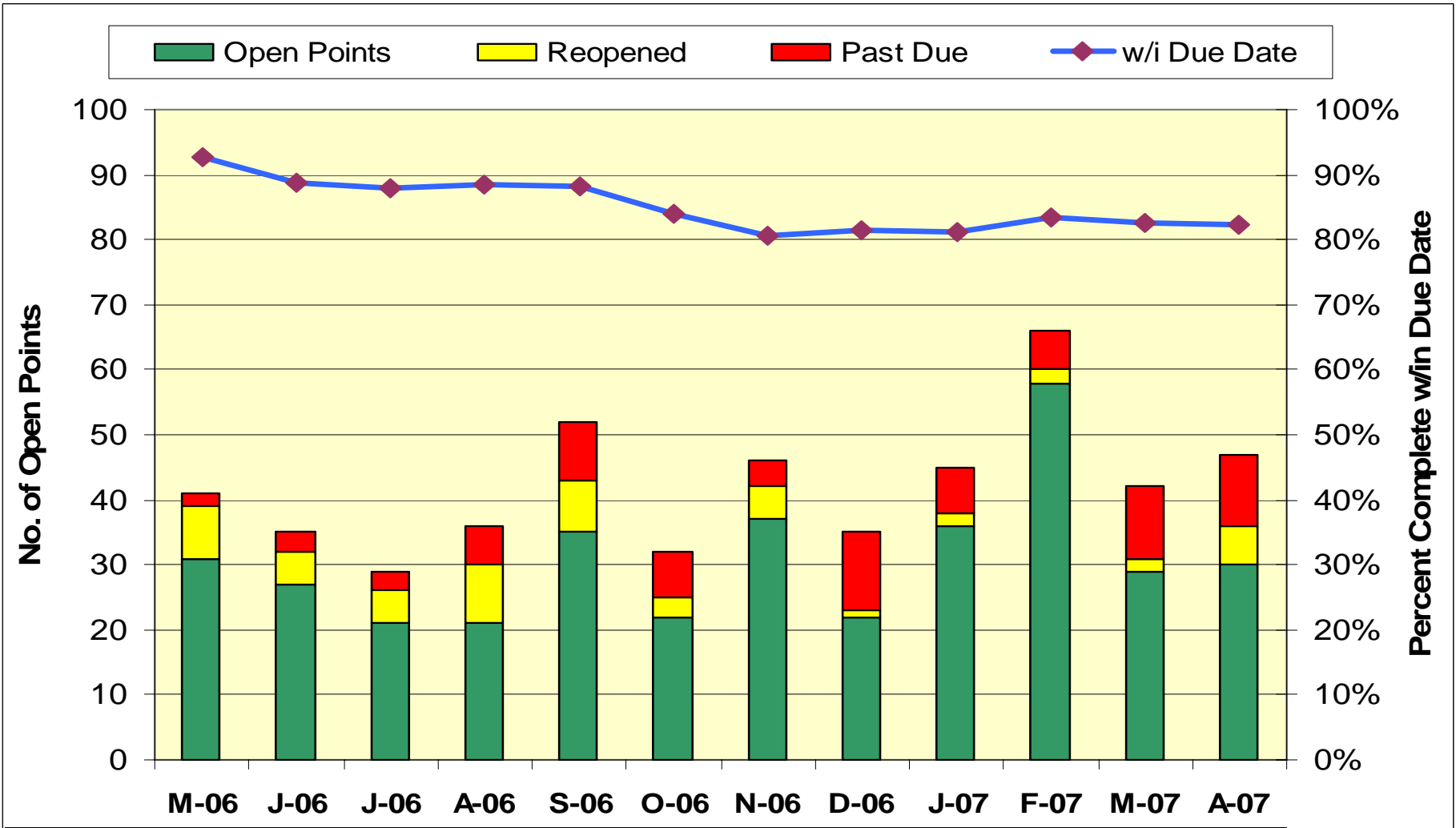
Nodal Implementation

Upgrade: Red > Yellow

ERCOT has further scoped the nodal project, hired additional key staff members, and funding has largely been obtained.

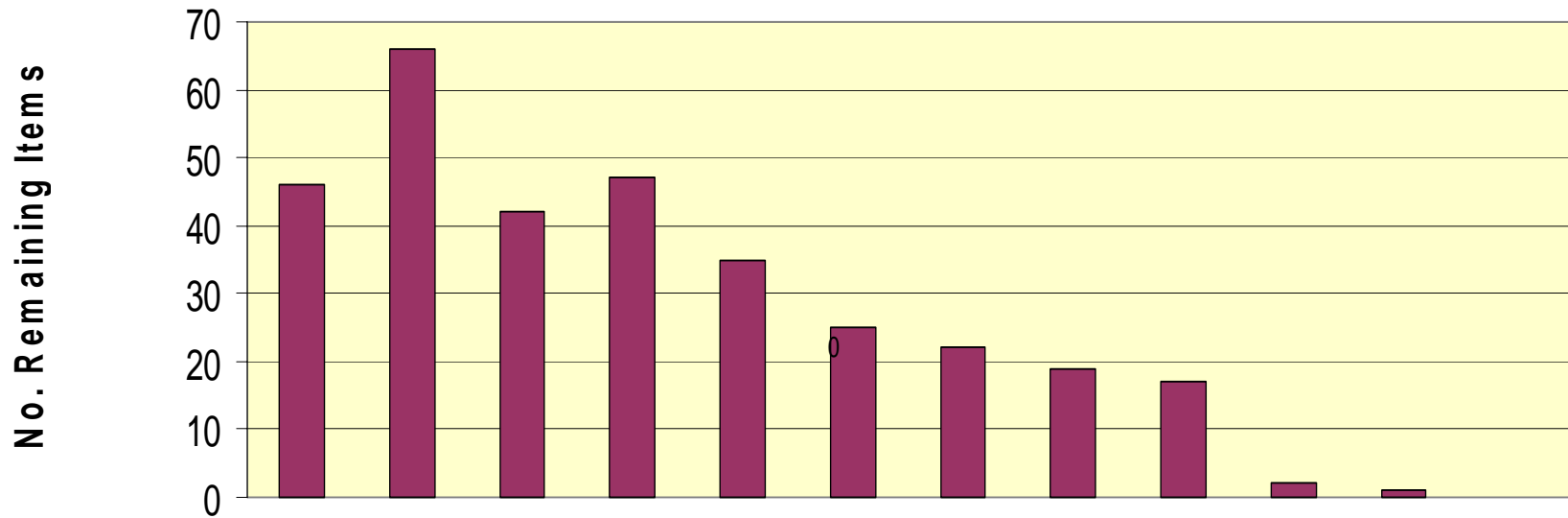
Committee Brief: ICMP – Status of Open Audit Points

Cheryl Moseley



Audits Completed	0	3	0	2	2	0	3	2	5	2	2	3
Points Added	0	15	0	7	30	2	28	8	36	35	0	7
Points Completed	6	21	6	0	14	22	14	19	26	14	24	2

Projected Audit Point Progress



	Jan-07	Feb-07	Mar-07	Apr-07	May-07	Jun-07	Jul-07	Aug-07	Sep-07	Oct-07	Nov-07	Dec-07
■ Audit Points	46	66	42	47	35	25	22	19	17	2	1	0

Audits Completed (last 3 months)

Internal Audits

- SCADA Applications
- Registration/Qualification of Market Participants
- Budget Process
- Nodal Recruiting
- Nodal Ethics Compliance
- SAS70 Pre-Audit Testing
- Accounts Payable
- Procurement Approval Process (Special Request)

External Audits

- Texas Nodal Program Controls - Review #2 (IBM-managed by IAD)
- Securicon Vulnerability Assessment (Managed by IAD)

Open Audits

Internal Audits

- Nodal Timetracking
- Nodal Signing Authority/Delegation of Authority
- PMO (Non-nodal)
- Nodal PMO (Targeted Review)
- Employee Background/Reference Checks (Targeted Review)
- NERC Compliance*

External Audits

- 2006 Financial Audit (PwC)
- 2007 SAS70 (PwC)
- 2006 Final MPP
- Texas Nodal Program Controls – Review #3 - IBM (Managed by IAD)

Planned Audits (next 3 months)

Internal Audits

- Protocol/Market Guide Approvals/Revisions
- Texas Regional Entity Planning & Budget
- Contract Audit of 21st Century
- Congestion Mgmt./TCRs
- Nodal Acctg./Allocation
- Nodal Compliance w/Procurement Guidelines

External Audits

- Texas Nodal Program Controls – Review #4 - IBM (Managed by IAD)

* NOTE: Conducted by internal resources other than Internal Audit

**Consultation/
Analysis Reports
Completed**
(last 3 months)

External Assessments

- 1 security assessment with combined consulting service completed in February

**Open Consultation/
Analysis Reviews**

External Assessments

- 1 security assessment started in March

**Planned Consultation/
Analysis Reviews**
(next 3 months)

External Assessments

2007 Year to Date Project Activity by Division

	Phase	Not Started	Initiation	Planning	Execution	Closing	Completed	Cancelled	On Hold	Totals by CART	Go-Live*
CART	Corporate Operations	19	0	3	8	3	1	0	0	34	1
	IT Operations	7	1	3	4	2	0	0	0	17	0
	Market Operations	2	3	4	9	4	2	5	1	30	1
	System Operations	2	2	7	5	5	4	1	3	29	4
	Totals by Phase	30	6	17	26	14	7	6	4	110	6

Note: Additional Projects Gone Live this month









PR-40007 (MO/RO)

PR-70031 (IO)

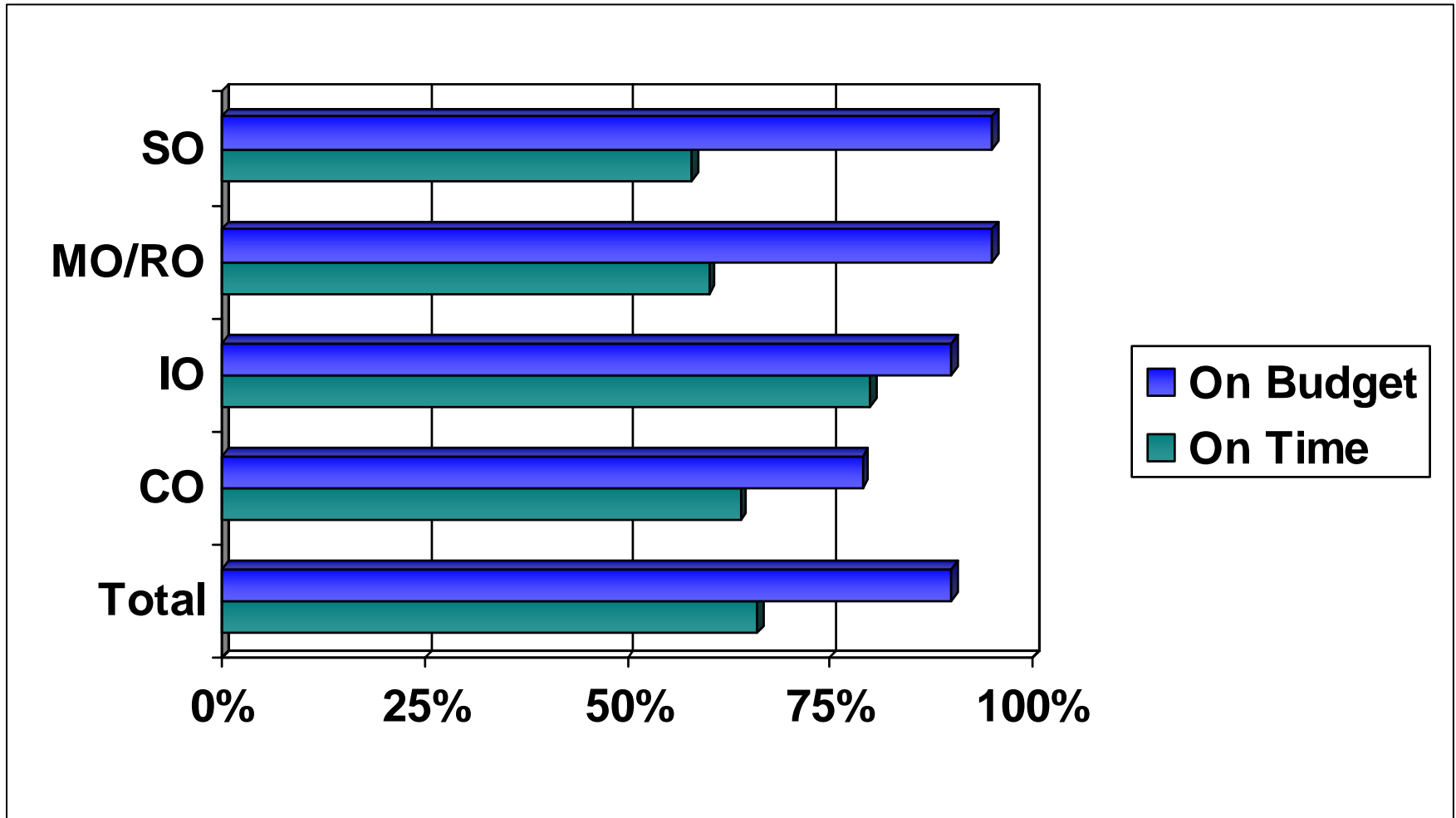
Year to Date Project Priority List (PPL) Status

PPL Iterations	Origination	Project Phases								Subtotal	Grand Total
		Not Started	Initiation	Planning	Execution	Closing	Completed	On Hold	Cancelled		
Original 2007 PPL											72
	PUCT	1			1	1		2		5	
	Market	1	1	1	3		1		4	11	
	ERCOT	24	1	10	9	2	2	1	2	51	
	Compliance			4				1		5	
	System Maintenance									0	
Unexpected Carry Over From 2006											22
	PUCT						2			2	
	Market	1				2	2			5	
	ERCOT				7	8				15	
	Compliance									0	
	System Maintenance									0	
New Projects Added (Since PPL Approval in August 2006)											16
	PUCT		1							1	
	Market		1		1					2	
	ERCOT	3	2	2	5	1				13	
	Compliance									0	
	System Maintenance									0	
2007 PPL totals as of January 31, 2007											110
	PUCT	1	1	0	1	1	2	2	0	8	
	Market	2	2	1	4	2	3	0	4	18	
	ERCOT	27	3	12	21	11	2	1	2	79	
	Compliance	0	0	4	0	0	0	1	0	5	
	System Maintenance	0	0	0	0	0	0	0	0	0	
Totals by Project Phase		30	6	17	26	14	7	4	6	110	

Projects Over \$1 Million

Projects Over \$1M	Total Budget	Total Committed To Date	Metrics	
Duration/Information (Sponsor)	Phase/Scheduled Completion		Schedule	Budget
(MO/RO) PR-40038_01: TX SET 3.0	\$1.628M	\$.992M		
<i>Currently in Execution (R. Giuliani)</i>	<i>Execution Phase/2nd Qtr 2007</i>			
(SO) PR-40090_02: Operator Training Simulator (2005-2007)	\$3.8M	\$2.70M		
<i>Training Simulator System for Operators (S. Jones)</i>	<i>Execution Phase/2nd Qtr 2007</i>			
(MO/RO) PR-50024_01: Enhancements to SCR727 (2005-2007)	\$1.9M	\$1.17M		
<i>Entered into Execution (R. Giuliani)</i>	<i>Execution Phase/2nd Qtr 2007</i>			
(CO) PR-60099_01 TCC1 Build-Out Phase One	\$2.65M	\$.136M		
<i>Currently in Execution (S. Jones)</i>	<i>Expected Completion/3rd Qtr 2007</i>			

2007 Completed and Active Projects Performance



Capital Projects – Budget vs. Actuals for Projects Completed YTD

Completed Projects	Baseline Budget	Actuals	\$ (Over)/Under Baseline Budget	% (Over)/Under Baseline Budget
PR-30105 (Congestion Management Reports)	105,300	86,716	18,584	18%
PR-60002_01 (Increase Number of Seats for Study Markets Clearing Engine) *	179,823	86,718	93,105	52%
PR-60090_01 (Load Profiling Software Upgrade) *	140,979	96,273	44,706	32%
PR-70031_01 (Spectel Hotline System Expansion) *	504,028	196,938	307,090	61%

NOTES:

(a) Baseline Budget does not include change controls that were approved without granting a new baseline budget.

* Substantially closed in Lawson - Actuals may change - Awaiting closing status in Lawson

Go Live Projects for April

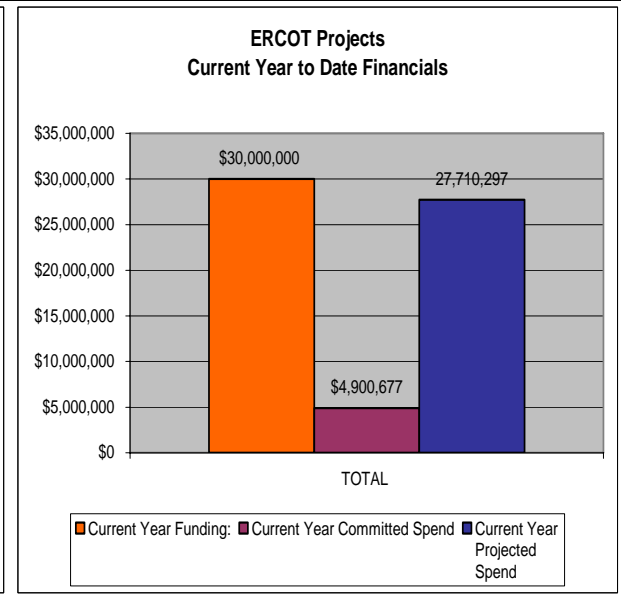
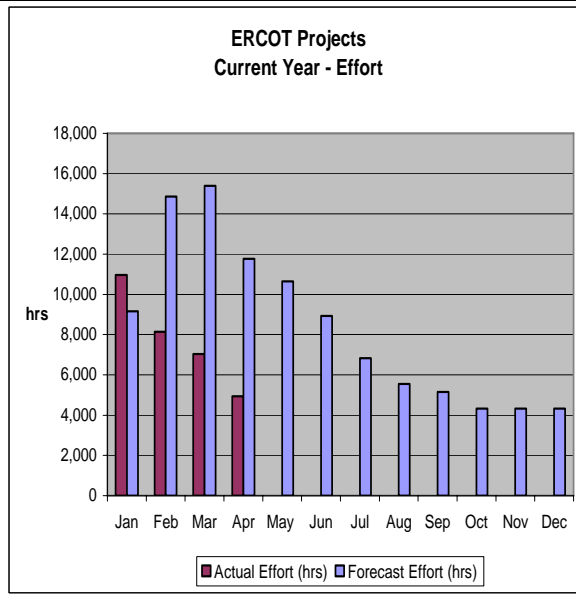
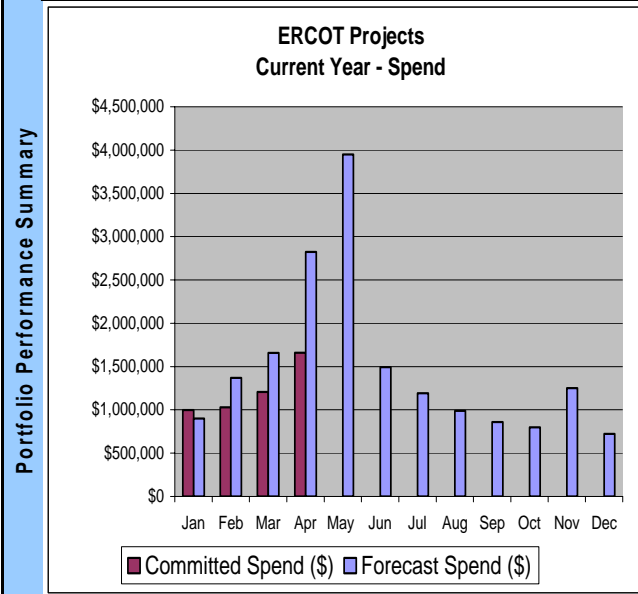
- **PR-40007 – SCR727 Phase II Enhancements**
 - **Scope:** Move the ESIID Service History and Usage Extract (a.k.a. SCR727) to the Lodestar Operational Data Store (ODS) environment.
 - **Deliverables:** As of April 20, 2007, all Market Participants receiving the ESIID Service History and Usage extract were automatically opted in to continue to receive the extract from the Lodestar ODS.
 - **Timeline:** January 2005 – April 2007

Go Live Projects for April

- **PR-70031_01 Spectel Hotline System Expansion**
 - **Scope:**
 - Expand the existing Spectel Hotline system to accommodate continued growth of Market Participants while maintaining functionality to support Grid Operations
 - **Deliverables:**
 - Contract with consultants to perform conference port provisioning
 - Expand existing hotline system by an additional 48 software conference ports
 - Provision additional T1 lines to support new ports (24 each)
 - **Timeline:** February 2007 – April 2007

Enterprise Projects Summary Report

ERCOT Overall Projects Report				Reporting Period: 4/30/2007		YTD					
ERCOT Projects Leadership			Projects in ERCOT's Portfolio					Portfolio Performance			
Executives			On Hold	Initiation	Planning	Execution	Closing	Schedule	Budget	Risk	Milestones
Kent Saathoff	Ray Giuliani		4	6	17	26	14	Y	G	G	\$ -
Ron Hinsley	Steve Byone		Completed	7	Total Active		70				
			Cancelled	6	Projects Not Started:		30	Prior Year Funding:	\$0	Current Year Funding:	\$30,000,000



Notes

Projections trending below Budget

- Testing environments contentions due to HP UNIX to IBM AIX UNIX transition
- Resource contentions (mainly Nodal)
- Projects on hold/not approved to start by sources (PUCT, Compliance, IMM)



Future Agenda Items – June 2007

- **Internal Audit status report**
- **Review and approve ERCOT annual report**
- **2007 Year-end financial projection**
- **Review Credit Review proposals**
- **2008 Budget status update**
- **Update on debt financing**
- **Report of external auditor pre-approval status/limits**
- **Review procedures for handling reporting violations**
- **Committee briefs**

Quarter 1

- √ •Elect officers and confirm financial qualifications
- Review Finance Audit Committee charter
- √ •Approve the Guidelines for Engagements of External auditors for Other Services (pre-approval policy)
- √ •Required written communication and discussion of auditor independence
- √ •Review scope of annual financial audit
- √ •Report by CWG Chair on ERCOT credit policy
- √ •Vote on CWG Chair/Vice Chair

Quarter 2

- √ •Report results of annual independent audit to the Board
- Report of external auditor pre-approval status/limits
- Review the procedures for handling reporting violations
- Review conflict of interest and ethics policies
- √ •Review results of annual audit (including required communications)
- Review and approve ERCOT Annual Report
- Review operating plan and budget assumptions
- Review and approve Internal Audit Department Charter

Quarter 3

- Appoint the independent auditors for upcoming year
- Approval of independent auditor fees for upcoming year
- Assessment of compliance, the internal control environment and systems of internal controls
- Review and approval of annual operating budget
- Report by CWG Chair on ERCOT credit policy
- Review updated year-end forecast

Quarter 4

- Approve audit committee meeting planner for the upcoming year, confirm mutual expectations with management and the auditors
- Review and approval of Financial & Investment policies
- Approve scope of internal auditing plan for upcoming year
- Assessment of the adequacy and effectiveness of the Internal Audit staff
- Perform Finance & Audit committee Self Assessment
- Review requirements for membership in CWG
- Review and approve CWG charter
- Review updated year-end forecast

Recurring Items

- Review minutes of previous meeting
- Report monthly matters to the Board (chair)
- Review EthicsPoint activity
- Review significant audit findings and status relative to annual audit plan
- Review investment results quarterly