



ERCOT Finance & Audit Committee Meeting

7620 Metro Center Drive, Austin, Texas

Met Center, Conference Room 206

November 17, 2008; 7:30am – 10:00am*

| Item # | Agenda Item Type | Description/Purpose/Action Required | Presenter | Time |
|--------|-------------------|---|--|--------|
| 1. | | Call to order Executive Session | C. Karnei | 7:30am |
| 2. | Decision required | 2a. Approval of executive session minutes (Vote) (10/21/08) | C. Karnei | 7:30am |
| | Informative | 2b. Internal Audit status report | B. Wullenjohn | 7:33am |
| | For discussion | 2c. Update on proposed 2009 Internal Audit plan | B. Wullenjohn | 7:40am |
| | Informative | 2d. Internal Audit 2008 goals update | B. Wullenjohn | 7:55am |
| | Informative | 2e. EthicsPoint update | B. Wullenjohn | 8:00am |
| | | Recess Executive Session | | 8:10am |
| | | Convene General Session | | |
| 3. | Decision required | Approval of general session meeting minutes (Vote) (10/21/08) | C. Karnei | 8:10am |
| 4. | Informative | Update on SAS 70 audit | S. Barry | 8:15am |
| 5. | For discussion | Collateral Management | C. Yager | 8:20am |
| 6. | Decision required | Review and approval of standards - Financial (Vote) - Investment | C. Yager | 8:40am |
| 7. | Decision required | Financial update - 2008 year end projections - Timeline for approval of revised 2009 base operating budget - Timeline for Nodal program budget - Nodal interim rate relief request (Vote) | M. Petterson M. Petterson R. Hinsley C. Yager | 8:50am |
| 8. | For discussion | Approval of audit committee meeting planner for the upcoming year, confirm mutual expectations with management and the auditors | All | 9:10am |
| 9. | For discussion | Perform Finance & Audit Committee self assessment | C. Karnei | 9:15am |
| 10. | For discussion | Market participant guarantee agreements | T. Coffing | 9:20am |
| 11. | Decision required | Review CWG charter and membership requirements (Vote) | T. Coffing | 9:30am |
| 12. | Informative | Update on status of Market Credit Risk Standard | T. Coffing / C. Yager | 9:40am |
| 13. | Informative | Committee Briefs (Q&A only) | All | 9:45am |
| 14. | Informative | Future agenda items | S. Byone | 9:50am |
| | | Adjourn ISO meeting | C. Karnei | 9:55am |
| | | | | |

* 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, December 9, 2008, at the Austin Airport Hilton, 9515 New Airport Drive, Austin, Texas 78744, in the Wildflower Conference Room.

| |
|-------------------|
| Decision required |
| For discussion |

3. Approval of General Session Minutes Clifton Karnei

- **Approval of General Session Minutes**
 - Vote 10/21/08

DRAFT ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
MINUTES OF THE ISO FINANCE & AUDIT COMMITTEE – GENERAL SESSION
7620 Metro Center Drive – Austin, Texas 78744
October 21, 2008

Pursuant to notice duly given, the Finance & Audit Committee of the Electric Reliability Council of Texas, Inc. convened on the above-referenced date. Clifton Karnei confirmed that a quorum was present and called the meeting to order at approximately **7:30 a.m.** The Committee met in Executive Session from **7:30 a.m. to 9:12 a.m.**, at which time it recessed to General Session.

General Session Attendance

Committee members:

| | | | |
|----------------------------------|--------------------------------|-------------------------------|---------|
| Cox, Brad | Tenaska Power Services | Independent Power Marketer | Present |
| Espinosa, Miguel (Vice Chair) | Unaffiliated Board Member | Unaffiliated Board Member | Present |
| Fehrenbach, Nick | City of Dallas | Consumer | Present |
| Gent, Michehl | Unaffiliated Board Member | Unaffiliated Board Member | Present |
| Jenkins, Charles | Oncor | Investor Owned Utility | Present |
| Karnei, Clifton (Chair) | Brazos Electric Cooperative | Cooperative | Present |
| Thomas, Robert | Green Mountain Energy | Ind. Retail Electric Provider | Present |
| Wilkerson, Dan | Bryan Texas Utilities | Municipal | Present |

Other Board Members and Segment Alternates:

| | | | |
|-------------------------|---------------------------|-----------------------|---------|
| Bartley, Steve | CPS Energy | Municipal | Present |
| Smitherman, Barry T. | Public Utility Commission | Chairman | Present |
| Walker, Mark | NRG Texas | Independent Generator | Present |

ERCOT staff and guests present:

| | |
|--------------------|--|
| Barry, Sean | PricewaterhouseCoopers |
| Bassett, Ryan | PricewaterhouseCoopers |
| Byone, Steve | ERCOT – Vice President and Chief Financial Officer |
| Day, Betty | ERCOT – Director of Markets |
| Deskins, Andy | Wachovia Bank |
| Doolin, Estrellita | ERCOT – Assistant General Counsel |
| Gresham, Kevin | Reliant Energy |
| Leady, Vickie | ERCOT – Associate Corporate Counsel |
| Lester, Suzanne | ERCOT – Executive Assistant (Finance) |
| Petterson, Mike | ERCOT – Controller |
| Seely, Chad | ERCOT – Corporate Counsel |
| Stauffer, Tarra | ERCOT – Legal Assistant |
| Troxtehl, David | ERCOT – PMO Director |
| Wullenjohn, Bill | ERCOT – Director, Internal Audit |
| Yager, Cheryl | ERCOT – Treasurer |

Approval of Prior Meeting General Session Minutes

Nick Fehrenbach moved to approve the minutes for the General Session of the Finance & Audit Committee meeting held on September 16, 2008. **Dan Wilkerson** seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Debt Financing Proposal

The Committee voted on the three debt financing proposals that had been presented by Cheryl Yager during the Executive Session. **Nick Fehrenbach** moved to approve **Proposal 1** as it had been outlined during the Executive Session; **Robert Thomas** seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Dan Wilkerson moved to approve **Proposal 2** as it had been outlined during the Executive Session; **Michehl Gent** seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Michehl Gent moved to approve **Proposal 3** as it had been outlined during the Executive Session; **Nick Fehrenbach** seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Debt and Liquidity Update

Cheryl Yager provided the Committee an update on recent debt financing, possible increase in debt capacity and proposed financing structure that would be discussed in more detail during the Executive Session of the Board meeting later that day.

Quarterly Review of Investment Results

Ms. Yager referred to the Quarterly Review of Investment Results materials that were distributed prior to the meeting and provided a brief overview of the Q3 2008 results. She commented that Steve Byone would provide a more in depth review during the Board meeting later that day. PUC Chairman Barry T. Smitherman pointed the Committee's attention to the Highlights of Investment Standard objectives and asked the Committee to review and consider two items: 1) whether our investments are sufficiently diversified and 2) whether quarterly reports being made to the F&A Committee were consistent with reports being presented to the Board.

Engagement of External Auditor for Other Services

Mike Petterson addressed the Committee regarding engagement of external auditors for other services. As required by the F&A Committee charter, he alerted the Committee in writing by Memorandum all present, that ERCOT had renewed its subscription to Comperio (a web based accounting database provided by PricewaterhouseCoopers) for 2009 at a cost of approximately \$2,000.

External Auditor Independence and Review of the 2008 Financial Audit Plan

Sean Barry and Ryan Bassett spoke to the Committee about external auditor independence and provided materials to attendees regarding ERCOT's Audit Plan for 2008 Financial Statements. Mr. Barry briefly outlined audit objectives, scope, terms of engagement, timing, key issues, strategy and high-risk areas. Mr. Barry clarified that the audit of ERCOT's financial statements would include the TexasRE as a division of ERCOT. He noted that Pricewaterhousecoopers had also been retained under separate engagement with the TexasRE to provide audit services.

Standard Form Guarantee Agreement

Chad Seely addressed the Committee by providing an update on the drafting of a revised Market Participant Guarantee Agreement. ERCOT Legal worked with Credit Work Group (CWG) and outside counsel to negotiate the language of the agreement. In September 2008, the Credit Work Group approved the new version of the Market Participant Guarantee Agreement and Foreign Market Participant Guarantee Agreement. There was a discussion on the extensive concessions made to the original proposed draft such as express affirmations of ownership or benefit, scope of guaranteed obligations and operation of credit support amount. There was additional dialogue on the demand and funding mechanism/retention of defenses, termination provision, expanded representations/covenants and assignability. Messrs. Karnei, Gent, Thomas and Wilkerson asked questions regarding these concessions and Mr. Seely commented that the revised agreement was marginally improved from the original version. Nick Fehrenbach expressed reservations and said he preferred the draft initially proposed by ERCOT Legal. Robert Thomas recommended and Committee members agreed to take no action on the revised Standard Form Guarantee Agreements at the meeting. Mr. Karnei voiced that the Committee would prefer further negotiations to strengthen the language and obtain reasoning behind the changes to the language proposed by ERCOT Legal. Ms. Yager agreed to set a timeline to get feedback from the CWG and report back to the Committee.

Adjournment

Clifton Karnei adjourned the meeting at approximately 9:57 a.m.

Estrellita J. Doolin
Assistant General Counsel and
Finance & Audit Committee Secretary

Informative

5. Collateral Management: Overview

Cheryl Yager

- Protocol language
- Historical levels of cash collateral
- Collateral management – internal vs external options
- Current practice
- Other ISOs
- Options to consider
- Next steps

- **16.2.5.1.2 - Alternative Means of Satisfying ERCOT Creditworthiness Requirements**
- **If the QSE's activity in the market in the ERCOT Region is greater than the maximum unsecured credit allowed under the standards adopted by the ERCOT Board of Directors ("Unsecured Credit Limit"), the QSE shall submit additional alternative security through one of the following means:**
 - (4) The QSE may deposit cash in an account designated by ERCOT with the understanding that ERCOT may draw part or all of the cash so deposited to satisfy any overdue payments owed by the QSE to ERCOT. The account may bear interest payable directly to the QSE, provided, however, any such arrangements shall not restrict ERCOT's immediate access to the funds. The cash so deposited shall be in an amount equal to or greater than the QSE's TEL or EAL, whichever applies, minus the QSE's Unsecured Credit Limit. Each QSE agrees that ERCOT has a security interest in all property delivered by the QSE to ERCOT from time to time in order to meet the creditworthiness requirements and that such property secures all amounts owed by the QSE to ERCOT.**

ERCOT's understanding of this Protocol language:

This language does not require ERCOT to use an escrow structure, but does not preclude ERCOT from using an escrow structure, if it chooses to. It is ERCOT's discretion.

- **Generally, levels of cash collateral have ranged from as low as \$50 million to as high as \$200 million at month ends**
 - Most frequently, cash collateral held is between \$100 million and \$150 million
 - Just prior to and during TCR auctions (particularly the annual auction), levels of cash collateral can spike up to more than \$200 million for several weeks

- **Cash collateral managed by ERCOT is managed in accordance with ERCOT's Investment Corporate Standard**
- **As we step back and take a look at our collateral management process, the first question is whether we want to consider some method of “outsourcing” the management of cash collateral**
 - At the CWG meeting on Nov 7, CWG members did not have a preference on this
 - If desired by F&A, ERCOT would do further research on options for outsourcing

- **Invest cash collateral in ERCOT money market funds used exclusively for collateral**
 - Individual accounts are NOT maintained for each MP
 - Historically invest in a government fund given security and returns
 - Currently invest in multiple treasury or treasury-backed securities funds (2 currently)
- **Monitor returns weekly against similar funds and move collateral to better performing funds and funds meeting Investment Standard requirements**
- **Maintain records relating to cash collateral held at ERCOT**

- **MISO – Uses JPMorgan family of funds, establishes accounts in MISO’s name, sets up individual accounts for each MP, allows MPs to choose one fund from several options**
- **PJM – Uses Black Rock – Temp Fund (includes CP), establishes accounts in PJM’s name, sets up individual accounts for each MP**
- **CAISO – Uses Bank of America family of funds, establishes accounts in CAISO’s name, sets up individual accounts for each MP, doesn’t currently but could allow MPs to choose their fund**

- **Establish escrow account(s) managed by a third party agent**
 - Pros
 - Have a third party fund specialist monitor and manage the fund options
 - Investment is separate from ERCOT, in the event ERCOT has a credit problem
 - Con
 - Does not provide protection if the investment fund has financial issues or incurs losses
 - In the event that the investment fund has a problem, potentially adds a layer of complexity to address the problem (e.g. close the account(s) and move the funds)

5. Collateral Management: Options to Consider

Cheryl Yager

- **Establish individual accounts for each MP at one fund family**
 - Pros
 - Each MP has own account, which may provide detailed info to the MP
 - Potentially provides some investment options within that fund family
 - Cons
 - More complex structure – Administratively burdensome
 - In the event that the investment fund has a problem, adds a layer of complexity to address the problem (e.g. close the accounts and move the funds)
 - Requires more static investment strategy (buy and hold). ERCOT would not change to another fund group (e.g. ERCOT would no longer monitor to ensure reasonable return)
 - Does not provide protection if the investment fund has financial issues or incurs losses

5. Collateral Management: Options to Consider

Cheryl Yager

- **Existing structure**

ERCOT maintaining one investment option for collateral defined by market or BOD (e.g. Treasury fund, etc) but maintains 2 or more funds for liquidity. ERCOT chooses specific funds based on Investment Standard criteria (the rate of return will be the average rate of return)

- Pros

- Flexibility, easier to open accounts and move funds - whether for security or return

- Cons

- MPs do not get direct reports from the bank
- Does not provide protection if the investment fund has financial issues or incurs losses

- **Variation on existing structure.**

ERCOT maintains two accounts with different levels of risk (e.g. Prime vs Treasury), giving MPs the ability to choose the level of risk and corresponding return. ERCOT chooses specific funds based on Investment Standard criteria

- Pros

- Allows MPs to select “level” of risk
- Flexibility, easier to open accounts and move funds - whether for security or return

- Cons

- MPs do not get direct reports from the bank
- Does not provide protection if the investment fund has financial issues or incurs losses

5. Collateral Management: Options to Consider

Cheryl Yager

- **Other ?**

5. Collateral Management: Next Steps

Cheryl Yager

- **Near term – consider improvements to the Investment Corporate Standard for handling all cash investments**
- **Medium term – pursue options suggested by F&A**

Financial standard attached as separate document

<Vote>

ERCOT CORPORATE STANDARD

| | |
|-----------------|-----------------------------------|
| Document Name: | Financial Corporate Standard |
| Document ID: | CS3.1 |
| Effective Date: | November 13, 2007 |
| Owner: | Board of Directors, F&A Committee |
| Approved: | Board of Directors, F&A Committee |

1.0 PURPOSE

This financial corporate standard is a framework from which ERCOT's financial integrity will be maintained while serving the long-term interests of the company and the ERCOT market. ERCOT recognizes that maintaining financial integrity is critical to accomplishing its corporate goals and discharging ERCOT's primary responsibilities.

2.0 DEFINITIONS

| TERM | DEFINITION |
|---|---|
| Budget | The Budget consists of Project Budgets, an Operating and Maintenance Budget and a Texas Regional Entity Division of ERCOT ("TRE") Budget as a component. |
| Project Budgets | Project Budgets consist of proposed expenditures to be made to develop capital assets during ERCOT's Fiscal Year. Any significant projects not included in the approved project budgets will be presented to ERCOT's Board of Directors for approval as they arise. |
| Cash Operating and Maintenance Expenses | Cash Operating and Maintenance Expenses consist of all reasonable and necessary costs (excluding non-cash items such as depreciation and amortization) incurred in the operation and maintenance of ERCOT's facilities, equipment and systems. |
| Fiscal Year | ERCOT's fiscal year is January 1 st through December 31 st . |
| NERC | North American Electric Reliability Corporation, the entity currently certified as the Electric Reliability Organization by FERC. |
| Operating and Maintenance Budget | The Operating and Maintenance Budget consists of all reasonable and necessary costs expected to be incurred during ERCOT's Fiscal Year. |
| TRE Budget | The TRE Budget is the budget (which can include both operating and maintenance and project budgets) for the TRE which is approved by |

| | |
|--------------------------|--|
| | NERC and Federal Energy Regulatory Commission (FERC) and which is used exclusively for the TRE’s proposal and enforcement of Reliability Standards (Federal Statutory duties) and for ERCOT Protocol and Operating Guide compliance investigation activities. |
| Scheduled Debt Service | Scheduled Debt Service is all interest and mandatory principal payments due on ERCOT’s outstanding indebtedness (both long-term and short-term) for a stated period. |
| Strategic Financial Plan | The Strategic Financial Plan will provide current financial information and a five-year projection, which addresses all sources of revenues, including any proposed fee adjustments. It will include projections of operating and maintenance expenses, project expenditures, the funding sources of project expenditures, and debt service requirements as well as the resulting capital structure. |

3.0 FINANCIAL OBJECTIVES

In seeking to fulfill its corporate objectives, ERCOT will maintain a high level of financial stability and will not compromise long-term financial integrity to achieve short-term benefits.

Strategic Financial Plan and Budget. Prior to or in conjunction with the submission of the annual Budget, the Chief Financial Officer will submit an update to the Strategic Financial Plan.

The Budget will be substantially consistent with the Strategic Financial Plan and will be submitted to the Board with sufficient time for the review and approval of the Board prior to the beginning of the Fiscal Year. The TRE Budget component of the Budget may be approved in advance of the full Budget if required to meet deadlines set by regulators.

In developing the Strategic Financial Plan and Budget, ERCOT staff will work to ensure that financial ratios required for compliance with debt instruments are maintained.

ERCOT will pursue financial objectives that will allow it to maintain an investment grade debt rating with Standard & Poor’s, Moody’s or Fitch. If a rating below investment grade is received or expected to be received, staff will promptly recommend a plan for Board consideration to recover or maintain the targeted rating within 18 months.

Overall, the Strategic Financial Plan and the related Budget will seek to assure ERCOT’s financial stability. They will be approved by the Board and will guide ERCOT’s financial planning process.

Fees and Charges. ERCOT will assess fees consistent with the ERCOT Protocols and PUCT rulings. Established fees will include payment of the portion of the TRE Budget for ERCOT Protocol and Operating Guide compliance investigation activities. ERCOT

will also collect fees on behalf of the Electric Reliability Organization as approved by FERC. The TRE will also receive funding for its Federal Statutory duties from NERC, pursuant to a Delegation Agreement. Fees, funding, and charges will be requested to recover the Board-approved Operating and Maintenance Budget (excluding depreciation and amortization), Scheduled Debt Service (less any principal payments reasonably expected to be refinanced), and the portions of Project Budgets that are to be financed with revenue. Fee adjustments, if necessary, will generally be developed and proposed in connection with ERCOT's annual Budget.

ERCOT will use all reasonable means to operate within the approved Budget for the current year. When unforeseen events occur (e.g. MWh's are significantly over or under projected levels, functionality is added or removed, etc.) and as a result, ERCOT experiences or expects to experience in the next 12 month period more than a 25% variance from 1) its Project Budgets, 2) its Operating and Maintenance Budget (excluding depreciation and amortization), or 3) its projected revenue stream, staff will promptly recommend a plan for Board consideration, which may include cost reductions or additions, fee increases or decreases, or other means to ensure that approved functions can be maintained, capital expended and expenses paid in the normal course of business.

Sources of Financing. ERCOT will use a combination of equity (revenue funding) and debt to finance projects. In determining the combination of equity and debt to be used in any particular year, ERCOT will consider the impact of the current year decision on future years.

Generally, ERCOT will structure debt issues such that the average maturity of the debt approximates the average life of the assets financed; however, debt issues may be structured with a longer or shorter average maturity if economically justified.

ERCOT may use variable-rate debt to provide flexibility in its overall financing program and to manage its overall interest rate exposure. However, in no event will ERCOT allow unhedged, variable rate debt to be more than 40% of total debt outstanding.

ERCOT will periodically evaluate the interest rate environment and review ways to manage interest rate exposure within that environment.

As appropriate, ERCOT will periodically evaluate mechanisms to restructure or refinance debt. ERCOT will regularly evaluate alternatives to conventional financing to obtain the lowest overall cost of borrowing while still meeting the objectives of this financial corporate standard.

Liquidity. ERCOT will seek to maintain adequate liquidity to meet its business needs. Liquidity is the combination of available 1) operating cash on hand, 2) operating cash equivalents / short term investments and 3) undrawn borrowing capacity under credit facilities.

ERCOT's targeted minimum level of liquidity will factor in: 1) six months of forecasted Scheduled Debt Service, other than principal payments reasonably expected to be

refinanced, 2) two months of average Cash Operating and Maintenance Expenses, net of projected administrative fee receipts, 3) two months of budgeted project expenditures, and 4) two months of estimated TCRs expected to be paid, net of projected TCR receipts during the same period.

If at any time ERCOT's liquidity is less than or is expected to be less than the targeted minimum level set forth in this corporate standard, staff will promptly recommend a plan for Board consideration to achieve the liquidity target within six months.

Funds received in conjunction with TCR auctions may be utilized to fund ERCOT working capital and project expenditure needs so long as liquidity is at or above the target levels and ERCOT's issuer rating remains investment grade. These funds may be utilized in place of borrowing under short term credit facilities to meet liquidity needs.

4.0 RESPONSIBILITIES

It is the responsibility of the Chief Executive Officer, Chief Compliance Officer and Chief Financial Officer to ensure that this corporate standard is implemented appropriately and to recommend changes in the standard as needed.

5.0 FINANCIAL STANDARD ADOPTION

ERCOT's financial corporate standard will be adopted by resolution of the Board of Directors. The corporate standard will be reviewed annually by the Finance and Audit Committee and any modifications made thereto must be approved by the Board of Directors.

Financial Standard - Redline

ERCOT CORPORATE STANDARD

| | |
|-----------------|-----------------------------------|
| Document Name: | Financial Corporate Standard |
| Document ID: | CS3.1 |
| Effective Date: | November 13, 2007 |
| Owner: | Board of Directors, F&A Committee |
| Approved: | Board of Directors, F&A Committee |

1.0 PURPOSE

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2.0 DEFINITIONS

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| Fiscal Year | ERCOT's fiscal year is January 1 st through December 31 st . |
| NERC | North American Electric Reliability Corporation, the entity currently certified as the Electric Reliability Organization by <u>the Federal Energy Regulatory Commission ("FERC")</u> . |
| Operating and Maintenance Budget | The Operating and Maintenance Budget consists of all reasonable and necessary costs expected to be incurred during ERCOT's Fiscal Year. |
| <u>Texas RE</u> | The <u>Texas RE</u> Budget is the budget (which can include both operating |

| | |
|--------------------------|--|
| Budget | and maintenance and project budgets) for the <u>Texas</u> RE which is approved by NERC and <u>Federal Energy Regulatory Commission (FERC)</u> and which is used exclusively for the <u>Texas</u> RE’s proposal and enforcement of Reliability Standards (Federal Statutory duties) and for ERCOT Protocol and Operating Guide compliance investigation activities. |
| Scheduled Debt Service | Scheduled Debt Service is all interest and mandatory principal payments due on ERCOT’s outstanding indebtedness (both long-term and short-term) for a stated period. |
| Strategic Financial Plan | The Strategic Financial Plan will provide current financial information and a five-year projection, which addresses all sources of revenues, including any proposed fee adjustments. It will include projections of operating and maintenance expenses, project expenditures, the funding sources of project expenditures, and debt service requirements as well as the resulting capital structure. |
| <u>TCR</u> | <u>Transmission Congestion Rights</u> |

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Overall, the Strategic Financial Plan and the related Budget will seek to assure ERCOT’s financial stability. They will be approved by the Board and will guide ERCOT’s financial planning process.

Fees and Charges. ERCOT will assess fees consistent with the ERCOT Protocols and [Public Utility Commission of Texas](#) ~~UCT~~ rulings. Established fees will include payment of the portion of the [Texas](#) RE Budget for ERCOT Protocol and Operating Guide compliance investigation activities. ERCOT will also collect fees on behalf of the Electric Reliability Organization as approved by FERC. The [Texas](#) RE will also receive funding for its Federal Statutory duties from NERC, pursuant to a Delegation Agreement. Fees, funding, and charges will be requested to recover the Board-approved Operating and Maintenance Budget (excluding depreciation and amortization), Scheduled Debt Service (less any principal payments reasonably expected to be refinanced), and the portions of Project Budgets that are to be financed with revenue. Fee adjustments, if necessary, will generally be developed and proposed in connection with ERCOT's annual Budget.

ERCOT will use all reasonable means to operate within the approved Budget for the current year. When unforeseen events occur (e.g. MWh's are significantly over or under projected levels, functionality is added or removed, etc.) and as a result, ERCOT experiences or expects to experience in the next 12 month period more than a [25 percent%](#) variance from 1) its Project Budgets, 2) its Operating and Maintenance Budget (excluding depreciation and amortization), or 3) its projected revenue stream, staff will promptly recommend a plan for Board consideration, which may include cost reductions or additions, fee increases or decreases, or other means to ensure that approved functions can be maintained, capital expended and expenses paid in the normal course of business.

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Generally, ERCOT will structure debt issues such that the average maturity of the debt approximates the average life of the assets financed; however, debt issues may be structured with a longer or shorter average maturity if economically justified.

ERCOT may use variable-rate debt to provide flexibility in its overall financing program and to manage its overall interest rate exposure. However, in no event will ERCOT allow unhedged, variable rate debt to be more than [40 percent%](#) of total debt outstanding.

ERCOT will periodically evaluate the interest rate environment and review ways to manage interest rate exposure within that environment.

As appropriate, ERCOT will periodically evaluate mechanisms to restructure or refinance debt. ERCOT will regularly evaluate alternatives to conventional financing to obtain the lowest overall cost of borrowing while still meeting the objectives of this financial corporate standard.

Liquidity. ERCOT will seek to maintain adequate liquidity to meet its business needs. Liquidity is the combination of available 1) operating cash on hand, 2) operating cash equivalents / short term investments and 3) undrawn borrowing capacity under credit facilities.

ERCOT's targeted minimum level of liquidity will factor in: 1) six months of forecasted Scheduled Debt Service, other than principal payments reasonably expected to be refinanced, 2) two months of average Cash Operating and Maintenance Expenses, net of projected administrative fee receipts, 3) two months of budgeted project expenditures, and 4) two months of estimated TCR repayment obligations expected to be paid, net of projected TCR auction receipts during the same period.

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4.0 RESPONSIBILITIES

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5.0 FINANCIAL STANDARD ADOPTION

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6. Review and Approval of Standards (Investment): Overview

Cheryl Yager

- **Investment objectives**
- **Risk – return considerations**
- **Approaches**
- **Summary of identified changes**
- **Other changes?**
- **Next steps**

6. Review and Approval of Standards (Investment): Objectives Cheryl Yager

1. **Security – minimize risk of loss**

- Invest in high credit quality instruments
- Be able to address issues quickly when they arise

2. **Liquidity**

- Ready access to cash collateral when needed
 - To draw on collateral to pay an invoice when it is due
 - To return collateral when requested
- To support working capital needs

3. **Return**

- Obtain a rate of return consistent with security and liquidity considerations

Note: There are trade offs among the objectives

6. Review and Approval of Standards (Investment): Risk / Return Considerations

- **What are the trade offs? (How secure do we want to be?)**
 - All investments have some level of risk
- **Who gets the benefit of higher rates, and who bears the risk of loss?**
- **Interest income is factored into ERCOT's System Administrative Fee (reduces Fee revenue needed)**
 - 2008 YTD inc \$1.7 million
 - 2007 income \$1.1 million
 - 2006 income \$2.2 million

6. Review and Approval of Standards (Investment): Risk / Return Considerations

| | | Indicative rates @ Nov 7 | Annual return on 100,000,000 | Incremental annual benefit to average "risk free" rate |
|-----------------|------|-------------------------------------|---|---|
| MM - Treasuries | Low | 0.33% | 330,000 | |
| | High | 0.81% | 810,000 | |
| | Ave | | 570,000 | |
| MM - US Govt | Low | 1.85% | 1,850,000 | |
| | High | 2.35% | 2,350,000 | |
| | Ave | | 2,100,000 | 1,530,000 |
| MM - Primary | Low | 2.65% | 2,650,000 | |
| | High | 3.15% | 3,150,000 | |
| | Ave | | 2,900,000 | 2,330,000 |

- **Risk free – stay in Treasury or Treasury-backed funds for all investments and accept lower returns**

If selected: Eliminate all investment options from Investment Corporate Standard other than Treasury related ones.

- **Maintain a defined level of risk for increased returns**

If selected: Review and confirm investment alternative and strengthen oversight (see next page for examples)

- **Vary risk tolerance based on who bears loss**

6. Review and Approval of Standards (Investment): Summary of Identified Changes

- **With the events of the last several months, ERCOT believes certain measures to strengthen oversight of investments held by ERCOT are warranted.**
 - Institute a monthly review of holdings in money market funds
 - Institute a monthly review of concentrations within money market funds holding corporate instruments
 - Provide a list of holdings for each fund held by ERCOT to the Board in conjunction with the quarterly report
 - When a money market fund holds corporate instruments, invest in funds that hold no more than xx% of corporate instruments
 - Limit exposure (considering all accounts) to any one fund to \$50 million.
 - Maintain accounts with at least two different fund families.

6. Review and Approval of Standards (Investment): Other Changes? Cheryl Yager

- **ERCOT has sought input from CWG on collateral management practices**
- **ERCOT seeks input from F&A as to other changes to the Investment Standard that would strengthen oversight**

- **ERCOT recommends holding proposed changes to the Investment Corporate Standard until the December meeting to allow more time for consideration of proposed additional changes**

Investment Standard - Redline

ERCOT CORPORATE STANDARD

| | |
|-----------------|--------------------------------------|
| Document Name: | Investment Corporate Standard |
| Document ID: | CS3.2 |
| Effective Date: | Upon Approval |
| Owner: | Board of Directors, F&A Committee |
| Governs: | ERCOT Personnel |
| Approved: | |

1. PURPOSE

The purpose of the ERCOT Investment **Corporate** Standard is to document the guidelines and related activities approved by the ERCOT Board of Directors for the investment and management of funds held by ERCOT.

It is ERCOT's policy to invest its funds in a manner that provides adequate security; meets daily cash flow demands; conforms to applicable laws, bylaws, board resolutions and debt covenants; and affords reasonable investment returns. ~~with adequate security while meeting daily cash flow demands and conforming to applicable laws, Bylaws, board resolutions and policies and debt covenants.~~

The **corporate** standard applies to activity involving ERCOT funds, except for the Electric Reliability Council of Texas, Inc. 401(k) Savings Plan, which is managed separately.

ERCOT funds specifically include proceeds **held by ERCOT** from:

- 1) the ERCOT System Administration Fee, Nodal Surcharge, NERC funding under a Delegation Agreement, and other fees collected from time to time,
- 2) transmission congestion rights (TCR) auctions,
- 3) market settlement operations,
- 4) security deposits,
- 5) debt issues, and
- 6) other miscellaneous cash received.

2.0 STANDARDS

Standard of Care. ERCOT investments will be made with judgment and care, under circumstances then prevailing, that persons of prudence, discretion and intelligence would exercise in the management of their own affairs, not for speculation but for

investment, considering the probable safety of principal as well as the probable income to be derived.

The standard of prudence to be used by the Designated Investment Officers (defined below) shall be the “prudent person” and/or “prudent investor” standard and shall be applied in the context of managing an overall portfolio. The Designated Investment Officers of ERCOT, acting in accordance with this standard and any other written procedures pertaining to the administration and management of ERCOT’s portfolio and who exercise the proper due diligence, shall be relieved of personal responsibility for an individual security’s credit risk or market price changes.

Investment Objectives. The primary objectives, in priority order, of ERCOT’s investment activities shall be:

- 1) Safety – Safety of principal is the foremost objective of the investment program. Investment of ERCOT funds will be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, ERCOT will diversify its investments by investing funds among a variety of securities offering independent returns and a variety of independent financial institutions.
- 2) Liquidity – ERCOT’s investment portfolio will remain sufficiently liquid to enable ERCOT to meet all operating requirements which might be reasonably anticipated.
- 3) Return on investment – ERCOT’s investment portfolio will be designed with the objective of attaining a benchmark rate of return throughout budgetary and economic cycles, in line with ERCOT’s investment risk constraints and the cash flow characteristics of the portfolio.

Delegation of Authority. Responsibility for the investment program is hereby delegated to the Designated Investment Officers. The Chief Financial Officer and the Treasurer of ERCOT are the Designated Investment Officers of ERCOT and are authorized to enter into and are responsible for all investment transactions undertaken. They will establish a system of controls over the investment program.

The Designated Investment Officers will establish written investment procedures for the operation of the investment program consistent with this corporate standard. No person may engage in an investment transaction except as provided under the terms of this corporate standard and the procedures established by the Designated Investment Officers.

Any two of the following individuals, with at least one being a Designated Investment Officer shall have authority to open and close investment and / or depository accounts with Qualified Institutions (as defined below): Chief Executive Officer, Chief Operating Officer, Chief Financial Officer, General Counsel, Controller and Treasurer.

Qualified Institutions or Money Market Funds. A Designated Investment Officer will select banks and other financial institutions that are approved for investment and / or depository purposes (“Qualified Institutions”). Only firms meeting the requirements of the attached Appendix A will be eligible to serve as Qualified Institutions or Money Market Funds.

If an ERCOT Board member or member of his or her immediate family is an officer or director, is employed by, or owns or has a beneficial interest in more than 10 percent of the stock in a bank or other financial institution that would otherwise be a Qualified Institution, such Board member shall provide full disclosure of such stock holdings or relationship in documented form to be filed with permanent records of ERCOT. Any institutions so disclosed will be excluded from consideration as a Qualified Institution without 1) full disclosure to the Board of Directors of the relationship and 2) approval of the Board to establish the relationship.

Authorized Instruments. ERCOT shall invest only in those types of instruments authorized under this corporate standard and listed in Appendix C and subject to restrictions included in Appendix C.

Safekeeping of Investments. Security transactions, including collateral for repurchase agreements, will be conducted on a “delivery-versus-payment” (DVP) basis. Securities, other than shares in money market mutual funds, will be held for safekeeping, in the name of ERCOT, by a custodian (an independent state or federally-chartered bank) designated by the Treasurer and evidenced by safekeeping receipts. Institutions that offer money market mutual funds are responsible for safeguarding their underlying securities.

Internal Reviews. Credit - To manage credit risk arising from investments, at least monthly ERCOT will review underlying securities held as investments, including investments held through money market funds. Any credit related concerns not satisfactorily resolved with fund managers will result in movement of the investment to an alternative fund. [Note: this review is intended as a sanity check, detail credit analysis will not be done; the review will not redo the work done by the fund managers and will not provide assurance that all holdings are creditworthy.] Concentration – To identify potential imbalance of investment holdings within a money market fund, at least monthly ERCOT will review a summary of fund holdings to ensure that investments held are in compliance with concentration restrictions under this corporate standard. In the event of non-compliance, ERCOT will close the account within 30 days and move the investment to an alternative fund.

Internal Control. The Treasurer shall ensure that the internal controls over investments are reviewed 1) periodically by ERCOT’s internal auditor, and 2) annually in conjunction with the fiscal audit by the external auditor. This review will test compliance with policies and procedures.

Reporting. A Designated Investment Officer will provide quarterly investment reports to the Board of Directors and Finance and Audit Committee which provide a clear picture of the status of the current investment portfolio.

Schedules in the quarterly report will, at a minimum, include the following:

- 1) A listing of individual securities held at the end of the reporting period by authorized investment category. If the investment category is money market, a list of securities held within each money market fund will be provided.
- 2) Average life and final maturity of all investments listed
- 3) Coupon, discount or earnings rate
- 4) Par value, amortized book value and market value
- 5) Percentage of the portfolio represented by each investment category
- 6) Statement of compliance with the Investment Corporate Standard

Investment Corporate Standard Adoption. ERCOT's investment corporate standard will be adopted by resolution of the Board of Directors. The corporate standard will be reviewed annually by the Finance & Audit Committee and any modifications made thereto must be approved by the Board of Directors.

APPENDIX A

Requirements of Qualified Institutions or Money Market Funds

Only entities meeting the following requirements will be eligible to serve as Qualified Institutions:

General Requirements

- 1) The entity has a senior debt rating which is at least the equivalent of A- by Standard & Poor's or A3 by Moody's Investor Service,
- 2) Has provided a current audited financial statement which is on file at ERCOT,
- 3) Has capital of not less than \$100 million, and
- 4) Has assets of not less than \$1 billion.

Additional Requirements for Depositories

- 1) The entity is a federal- or state-chartered bank, and
- 2) Deposits up to \$100,000 are insured by federal agencies

Additional Requirements for Security Dealers

- 1) The entity is a "primary" or regional dealer that qualifies under Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule),
- 2) Is registered as a dealer under the Securities Exchange Act of 1934,
- 3) Is a member in good standing of the National Association of Securities Dealers (NASD),
- 4) The entity has been in business for at least five (5) years,
- 5) A representative of the entity has returned a signed certification (substantially in the form attached as Appendix B) that he/she has read and is familiar with ERCOT's Investment Corporate Standard, and
- 6) The entity has provided such other information as ERCOT requires from time to time.

Only entities meeting the following requirements will be eligible to serve as Qualified Money Market Funds:

- 1) The fund is a money market fund under SEC Rule 2a-7
- 2) Has provided and commits to provide at least month a list of holdings in the fund
- 3) Has assets under management in the fund of at least \$1 billion.

APPENDIX B

**Investment Corporate Standard for
Electric Reliability Council of Texas**

Qualified Institution Certification for Security Dealers

Dealer / Investment Firm: _____

I hereby certify that I have received and thoroughly reviewed the ERCOT Investment Corporate Standard, and the firm I represent

- 1) meets all of ERCOT's Requirements for Qualified Institutions; and
- 2) has implemented reasonable procedures and controls in an effort to preclude investment transactions between this firm and ERCOT that are not authorized by the ERCOT Investment Corporate Standard, except to the extent that this authorization is dependent on an analysis of the makeup of ERCOT's entire portfolio or requires an interpretation of subjective investment standards.

Qualified Representative

Name

Title

Date

APPENDIX C

Authorized Instruments

| <u>Description</u> | <u>Quality Limitation</u> | <u>Maturity Limitation (Note 1)</u> | <u>Limitation per issuer</u> | <u>Category limitation</u> |
|--|---------------------------|-------------------------------------|------------------------------|-------------------------------|
| 1. Obligations of or guaranteed by the US government | n/a | 5 yrs or less | none | none |
| 2. Obligations of or guaranteed by other US governmental entities (e.g. federal agencies, state or municipal, etc) | n/a | 5 yrs or less | \$5,000,000 | 50% of total |
| 3. Certificates of deposit and share certificates | Note 2 | 1 yr or less | \$5,000,000 | 33% of total |
| 4. Repurchase agreements in which the collateral is government or agency securities (1 or 2 above). (Note 3) | Note 2 | 7 days or less | \$5,000,000 | 33% of total |
| 5. Commercial paper | A1/P1 or better | 1 yr or less | \$5,000,000 | 33% of total |
| 6. Banker's acceptances | Note 2 | 1 yr or less | \$5,000,000 | 33% of total |
| 7. Money market mutual funds (MMMF) | Note 4 | Note 4 | Note 4 | <u>Note 5</u> none |

Note 1: To the extent possible, ERCOT will attempt to match its investments with anticipated cash flow requirements. A base level of cash may remain uninvested to meet the operating needs of ERCOT.

Note 2: Investments may be made with financial institutions with a corporate or senior debt credit rating of at least A- with S&P or A3 with Moody's. Investments in repurchase agreements must be subject to a Master Repurchase Agreement signed with the bank or dealer (e.g. a PSA Master Repurchase Agreement or equivalent).

Note 3: Collateral is required for all repurchase agreements. In order to anticipate market changes and provide a level of security for all funds, the collateralization level will be 102% of market value and accrued interest. Collateral may consist only of other instruments approved above. Collateral will always be held by an independent third party with whom ERCOT has a current custodial agreement. A clearly marked evidence of ownership (safekeeping receipt) must be supplied to and retained by ERCOT. The right of collateral substitution is granted.

Note 4: There is no credit rating required given 1) the MMMFs stated objective to preserve capital, 2) the credit quality restrictions placed on MMMFs by the SEC (may hold no more than 5% of middle-rated securities – A2/P2 or equivalent), 3) the SEC restriction that no more than 5% of assets in a MMMF may be invested in any one security (requires diversification) and 4) the restriction that MMMFs can only invest in instruments with maturities of less than 13 months and that the average maturity of all holdings in a MMF cannot extend beyond 90 days. There is no maturity limitation or limitation per issuer for the reasons mentioned above. If MMMFs hold corporate instruments, no more than xx% of the holdings will be in corporate paper.

Note 5: There is no limit on how much money may be placed with MMMFs because of the requirements on those funds outlined in Note 4. However, no more than \$50 million may be held in any one fund, through a combination of all accounts, and ERCOT must maintain accounts with at least two different fund families to diversify risk across fund families.

- **\$5.0 - \$6.0 million favorable variance in base operating activity projected for 2008**
 - \$12.5 million principal payment on term loan is a key factor
 - Management negotiated financial flexibility in wake of credit crisis
 - Payment is no longer a contractual commitment but is an option available at ERCOT's discretion
 - Management recommends making principal payment as originally scheduled given recent developments
 - Projected favorable financial variance reflects the principal payment in November 2008
 - Seeking concurrence from the Finance and Audit Committee

- **2009 base operating budget approved by the Board in May 2008 assuming completion of the Nodal Program by December 2008.**
- **Implementation of the nodal market will not be completed as assumed in the approved 2009 base operating budget.**
- **Management will seek revised budgetary spending authority for 2009 as a result of the delay in implementation of the Nodal Program.**

- **The schedule presented to the Finance and Audit Committee and Board in October was very tight and allowed no room for slippage of upstream activity.**
- **Preparation of an updated Nodal Program budget has not progressed as scheduled.**
- **As communicated in October, the delays lead management to pursue a two-step process to obtain approval of a revised 2009 base operating budget.**
 - In December 2008, seek approval of a one-month budget for planned activity in January 2009.
 - In January 2009, seek approval of the full, revised 2009 base operating budget.

7. Timeline for Approval of Revised 2009 Base Operating Budget

Mike Petterson

| Date | Budget Preparation, Review, and Approval Task |
|-----------------------------|--|
| Monday, Oct. 20 - TBD | <p><u>Special Nodal Program Committee</u> At times to be established by the members of the Special Nodal Program Committee, review and approve the management recommended, revised Nodal Program schedule, resource requirement plan, and budget.</p> |
| Tuesday, Dec. 2 | Distribute the management recommended, one-month budget for activity and transactions in January 2009 to the ERCOT Board of Directors. |
| Tuesday, Dec. 9 | <p><u>Finance & Audit Committee and Public Input Meeting</u> Discuss, review, and obtain from the Finance & Audit Committee a recommendation for approval by the ERCOT Board of the one-month budget for activity and transactions in January 2009. (Vote)</p> <p><u>Board of Directors Meeting</u> Discuss and review the one-month budget for activity and transactions in January 2009 recommended by the Finance & Audit Committee.</p> <p>Obtain approval from the ERCOT Board for the one-month budget for activity and transactions in January 2009. (Vote)</p> |
| Tuesday, Jan. 13 | Distribute the management recommended, revised 2009 base operating budget and PPL to the members of the ERCOT Board of Directors. |
| Tuesday, Jan. 20 | <p><u>Finance & Audit Committee and Public Input Meeting</u> Discuss, review, and obtain from the Finance & Audit Committee a recommendation for approval by the ERCOT Board of the revised 2009 base operating budget and PPL (Vote)</p> <p><u>Board of Directors Meeting</u> Discuss and review the revised 2009 base operating budget and PPL recommended by the Finance & Audit Committee.</p> <p>Obtain approval from the ERCOT Board for the revised 2009 base operating budget and PPL (Vote)</p> |

For discussion

7. Financial Update – Nodal Interim Rate Relief (Vote) Cheryl Yager

- **Nodal spending projection**
- **Factors considered for funding mechanism**
- **Scenarios considered – simplified summary**
- **Recommendation**

7. Financial Update – Nodal Interim Rate Relief (Vote) Nodal Spending Projection

- **As noted, for the Nodal Program to continue to progress, approximately \$12 million per month of spending authority is needed while the CBA requested by the PUCT is completed and then the revised budget and timeline are finalized.**
- **Funding this new spend must be accomplished through some combination of revenue and/or debt financing**

7. Financial Update – Nodal Interim Rate Relief (Vote) Factors Considered for Funding Mechanism

- **Current credit market conditions**
 - Unprecedented turmoil in markets world wide
 - ERCOT’s recent financing efforts, while successful, were more difficult and costly
- **ERCOT’s current debt load**
- **Need to preserve debt capacity**
- **Increased Nodal cost due to interest expense**
- **Uncertainty around total cost to complete the Nodal Program**

7. Financial Update – Nodal Interim Rate Relief (Vote) Scenarios Considered – Simplified Summary

| | \$ | Revenue Contribution Beginning January 1, 2009 | | | |
|---|---------------|--|------------------|------------------|------------------|
| | | 100% | 75% | 66% | 50% |
| Estimated monthly "run rate" (in thousands) | 12,000 | | | | |
| Anticipated average monthly needs | | | | | |
| Fund a portion of Nodal costs based on the current "run rate" | | 12,000 | 9,000 | 7,920 | 6,000 |
| Fund interest costs on outstanding Nodal debt | | 997 | 1,087 | 1,119 | 1,177 |
| Total to be funded | | <u>12,997</u> | <u>10,087</u> | <u>9,039</u> | <u>7,177</u> |
| Fee per MWh | | 0.49 | 0.38 | 0.34 | 0.27 |
| Incremental monthly debt incurred (for Nodal) | | - | 3,000.00 | 4,080.00 | 6,000.00 |
| Estimated annual additional debt incurred | | - | 36,000.00 | 48,960.00 | 72,000.00 |

7. Financial Update – Nodal Interim Rate Relief (Vote) Recommendation

- **After considering the alternatives and in light of ERCOT's current financial position against the backdrop of tight credit markets, ERCOT recommends revenue funding 100 percent of the additional spend in this interim filing.**
 - a) The revenue funding level will be re-evaluated once a final schedule and budget are complete
 - b) Funding current spend only will require ERCOT to re-schedule planned Nodal debt retirements
- **Specifically, ERCOT respectfully requests that the Board authorize ERCOT to make a filing with the PUCT, to request:**
 - a) A change in the Nodal Surcharge rate from \$0.169 per MWh to \$0.490 per MWh, effective no later than February 1, 2009
 - b) Deferral of Nodal debt repayment beginning in 2009 as contemplated in the most recent surcharge filing with the PUCT.
- **See Board decision template Item 8b <Vote>**

8. Approval of Audit Committee Meeting Planner All

- **Approval of audit committee meeting planner for the upcoming year, confirm mutual expectations with management and the auditors.**

8. Approval of Audit Committee Meeting Planner F&A Yearly Schedule

Quarter 1

- Elect officers and confirm financial qualifications
- Review of external auditor quality control procedures and independence
- Review scope of annual financial audit
- Vote on CWG Chair/Vice Chair

Quarter 2

- Report results of annual independent audit to the Board
- Review the procedures for handling Reporting violations
- Review results of annual audit, together with significant accounting policies (including required communications)
- Review ERCOT Annual Report
- Review operating plan and budget assumptions
- Review and approve Internal Audit Department Charter
- Conduct annual review of insurance coverage(s)
- Review the Company's dealings with any financial institutions that are also market participants

Quarter 3

- Appoint the independent auditors for upcoming year
- Approval of independent auditor fees for upcoming year
- Review of committee charter
- Approve the Guidelines for Engagements of External auditors for Other Services (pre-approval policy)
- 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
- Review the Company's dealings with any financial institutions that are also market participants

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

For discussion

| | ERCOT Finance & Audit Committee Self-Evaluation November 2008 | Yes | No | Not Sure | Comments |
|----|--|--------------------------|--------------------------|--------------------------|-----------------|
| 1. | Does the committee have the appropriate number of members? The committee should not be so large that: <ul style="list-style-type: none"> ▪ its ability to operate efficiently and effectively is reduced ▪ members' ability to raise issues is hampered ▪ it is difficult to get a quorum when a time-sensitive issue arises | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 2. | Committee members demonstrate their objectivity during meetings through behaviors such as driving agendas, rigorous probing of issues, consulting with other parties, and hiring experts, as necessary. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 3. | Differences of opinion on issues are resolved to the satisfaction of the committee. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 4. | Committee members challenge the Chair as appropriate. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 5. | The committee charter is used as a document to guide the committee in its efforts, and to help guide the committee's agenda. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 6. | 6.1 Committee members are financially literate, and the committee has determined that it has adequate financial expertise in accordance with its charter. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.2 Committee members participate in some form of continuing education to stay abreast of changes in the financial accounting and reporting, regulatory and ethics areas. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.3 The committee understands how the organization's performance compares with its budgetary targets and its peers, and how management plans to address any unfavorable variances. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.4 The committee discusses the initial selection of or changes in significant accounting policies used in developing the financial statements, the reason for and impact of any changes in policy, and reasons alternative treatments were not adopted. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |

| | ERCOT Finance & Audit Committee Self-Evaluation November 2008 | Yes | No | Not Sure | Comments |
|-----|--|--------------------------|--------------------------|--------------------------|-----------------|
| | 6.5 The committee discusses significant, complex, or unusual transactions with management and the external auditors. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.6 The committee understands which areas represent high risk for material misstatement of the financial statements, and discusses assumptions and approaches used with management and the external auditors. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.7 The committee forms its own view of the risk of material misstatement due to fraud, discusses with management and the external auditors their views on the risk of material misstatement due to fraud, and is comfortable that any differences in views can be reconciled. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.8 The committee fully understands significant changes in financial statements from prior years and from budget, and is provided with sufficient, reliable evidence to support variances. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.9 The committee commits sufficient time to review, discuss, and consider the financial statements. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.10 The committee makes optimum use of the meeting time allotted. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 6.11 The committee meets with financial management to discuss results reported before finalization. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 7. | Committee members have a clear understanding of ERCOT's debt structure and cash management practices. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 8. | Committee members receive sufficient details regarding long-term financial planning. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 9. | The Committee makes appropriate use of workgroups or task forces to investigate issues defined by the Committee. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 10. | The committee engages outside experts as appropriate. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 11. | 11.1 The organization's financial reporting processes are stronger as a result of management's interactions with the committee. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |

| | ERCOT Finance & Audit Committee Self-Evaluation November 2008 | Yes | No | Not Sure | Comments |
|-----|---|--------------------------|--------------------------|--------------------------|-----------------|
| | <p>11.2 The committee understands and agrees with the board on which categories of internal control it oversees. Categories include:</p> <ul style="list-style-type: none"> ▪ Integrity of financial reporting ▪ Compliance with laws and regulations ▪ Operational efficiency and effectiveness | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 11.3 The committee and the board concur with any changes to the committee's internal control oversight mandate. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 11.4 The committee understands the current high-risk areas - including information technology and computer systems - in the categories of controls it oversees, as well as how management addresses those areas. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 12. | The committee is cognizant of the line between oversight and management, and endeavors to respect that line. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 13. | The committee conducts executive sessions in a manner that offers a "safe haven" to the individual, while at the same time asking tough and necessary questions, evaluating the answers, and pursuing issues that might arise to a satisfactory resolution. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 14. | 14.1 The committee does its part to ensure the objectivity of the internal audit team. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 14.2 The committee provides constructive feedback to the chief audit executive at least annually. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 14.3 The committee receives sufficient detail regarding material issues and complaints brought forward which relate to the company's fraud, ethics or accounting practices. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| | 14.4 The committee has developed the scope of work to be done by the independent auditor and by the internal audit department based upon a reasoned review of the risks or exposures to the company. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |

| | ERCOT Finance & Audit Committee Self-Evaluation November 2008 | Yes | No | Not Sure | Comments |
|-----|--|--------------------------|--------------------------|--------------------------|-----------------|
| 15. | The committee communicates at an appropriate level of detail when informing the Board of its actions. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 16. | Committee members receive clear and succinct agendas and supporting written material sufficiently prior to scheduled meetings. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 17. | Committee members have adequate opportunities to discuss issues and ask questions. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 18. | The frequency of committee meetings is appropriate for the responsibilities assigned to the committee. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 19. | Meeting facilities and presentation materials are effective for the conduct of committee activities. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 20. | The committee is efficient and value adding. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |
| 21. | Please add additional comments, questions and suggestions here. | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | |

For discussion

20081021 Finance & Audit Committee Meeting Materials

11. Review CWG Charter and Membership Requirements

Tim Coffing

<Vote>



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

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 ([the F&A Committee](#)), with a copy to the Chair and Vice Chair of the Technical Advisory Committee (TAC). The CWG will provide comments to the TAC subcommittees when [Protocol Revision Requests](#) (PRRs), [Nodal Protocol Revision Requests](#) (NPRRs) or other actions have credit implications.

II. Reporting Relationships

- The CWG reports to the Finance and Audit Committee of the Board as a working group and is not a subcommittee of either the Board or TAC.

III. ERCOT Credit Work Group Functions

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

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

- ~~Provide~~Providing input on credit matters as requested by the ~~Finance and Audit~~&A Committee or by TAC or ~~its~~TAC subcommittees
- Providing input regarding PRRs and NPRRs that impact credit in accordance with this Charter and Board approved credit policies
- Providing input regarding the ERCOT Creditworthiness Standards

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

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

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

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.

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

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.

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

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~~&A Committee.

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

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.

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 (including participation by telephone) at a meeting to constitute a quorum: Independent REPs (and Aggregators), Independent Generators, Independent Power Marketers, Municipals, Cooperatives, Investor Owned Utilities, and Consumers.

Each CWG member or CWG member's company represented on CWG may designate, in writing, an Alternate Member Representative or proxy who may attend meetings and vote on the CWG member's behalf. Alternate Members Representatives must be employees of the 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 Representative or proxy, the CWG member must send to ERCOT notification of the designation of such Alternative Member Representative or proxy in advance of any meeting and the designation shall be valid for the time period designated by the CWG ~~Member~~ member.

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 urgent condition requires shorter notice. Meeting notices for urgent meetings shall be sent to the distribution list and posted on the ERCOT website and shall clearly identify the condition requiring the shorter notice. Except in cases of urgent matters, 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 urgent matter, 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 circumstances causing the urgency shall be clearly identified. All CWG meetings may be attended by any interested observer. Call-in numbers will be provided for those persons wishing to attend via telephone. CWG members may participate in the meeting and vote via telephone. If third-party confidential information is presented during a meeting, all persons except for CWG members may be excluded from the portion of the meeting at which such confidential information is discussed. [Confidential information will not be presented to CWG members participating by telephone.](#)

C. Voting

Votes: At all meetings, each Segment shall have one (1) vote. CWG members present at the meeting ([including participation via telephone](#)) 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 [CWG](#) 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 [CWG](#) 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.

Any dissenting party shall have the right to request time to present its position to the ~~F&A~~Finance and Audit Committee if such dissenting party chooses to do so.

E-mail ~~voting~~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 or Vice 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 Public Area.

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 Public Area 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 draft minutes of each meeting with materials being distributed for the next meeting. 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~~Representatives must meet the qualifications as identified on the attached Qualifications Guidelines for Credit Work Group Membership. The ~~Finance and Audit~~&A 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~~ & A Committee.

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.

Effective on November ~~13, 2007~~, 2008

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~~ Alternate Representatives 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.

Informative

Q&A only

ERCOT Market Credit Status

as of 9/30/2008

as of 10/31/2008

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 | |
|---|------------------------------------|--------------------|--|---------------|
| 11 | 52,249,609 | 9% | 153,577,709 | U |
| <u>QSEs that do not meet ERCOT Creditworthiness Standards</u> | | | | |
| Ratings below BBB- or not rated | | | | |
| Cash & Letters of Credit | 53 | 367,649,882 | 61% | 531,998,991 S |
| Guarantee Agreements | 16 | 178,761,551 | 30% | 503,233,082 S |
| Total Exposure | 80 | 598,661,042 | 100% | |

| # of QSEs* | Estimated Aggregate Liability (\$) | % of EAL | Total Unsec Credit Limit / Security Posted | |
|---|------------------------------------|--------------------|--|---------------|
| 12 | 44,077,227 | 10% | 176,982,396 | U |
| <u>QSEs that do not meet ERCOT Creditworthiness Standards</u> | | | | |
| Ratings below BBB- or not rated | | | | |
| Cash & Letters of Credit | 53 | 279,604,279 | 61% | 561,741,963 S |
| Guarantee Agreements | 15 | 131,772,667 | 29% | 467,233,082 S |
| Total Exposure | 80 | 455,454,173 | 100% | |

Other QSEs in the ERCOT Market (ERCOT owes)

QSEs that meet ERCOT Creditworthiness Standards

Ratings over BBB-

QSEs that do not meet ERCOT Creditworthiness Standards

Ratings below BBB- or not rated

Cash & Letters of Credit

Guarantee Agreements

142

147

Total

62

(52,907,301)

-100%

67

(40,905,396)

-100%

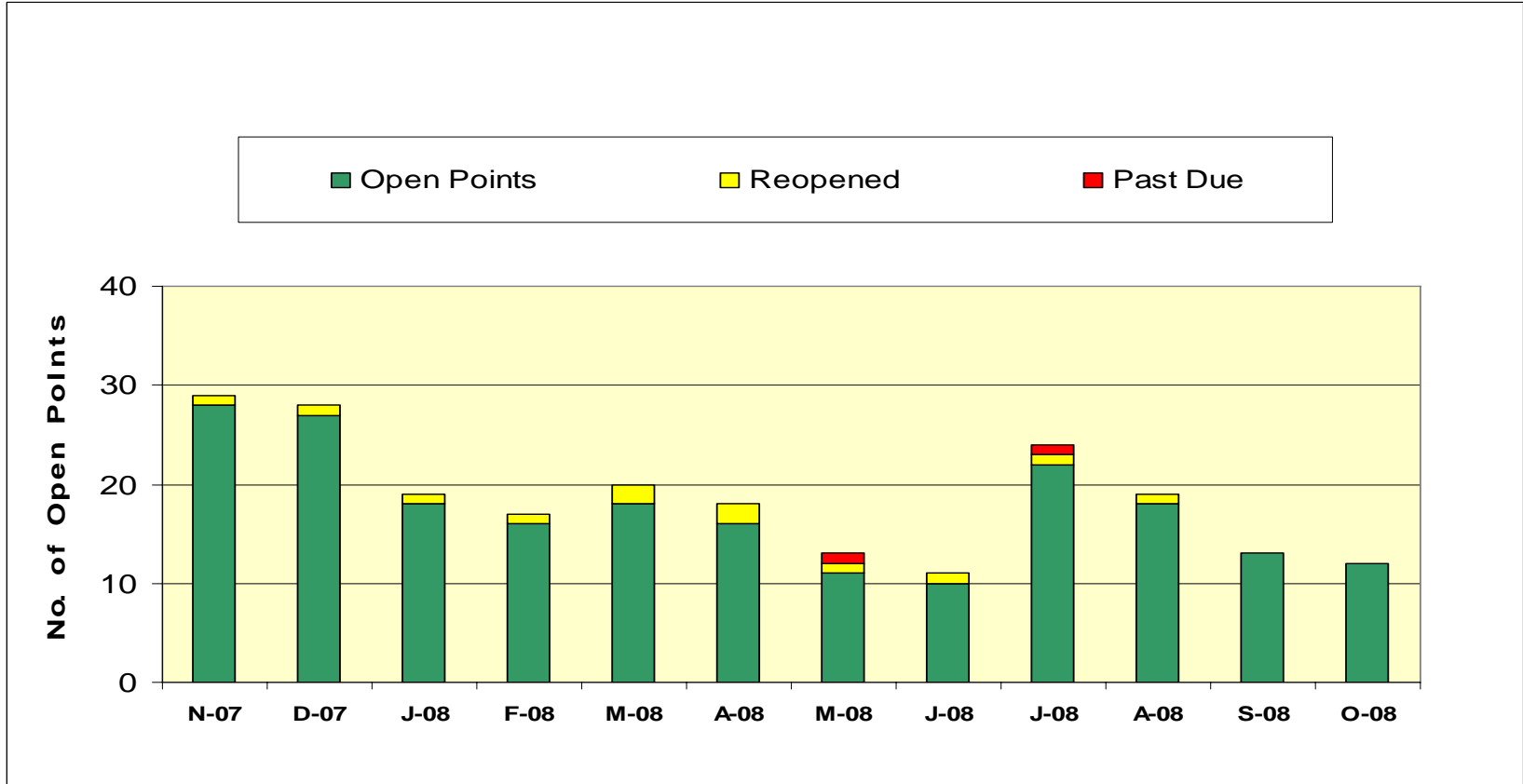
Total

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

13. Committee Brief: ICMP – Status of Open Audit Points

Cheryl Moseley



| | | | | | | | | | | | | |
|-------------------------|---|---|---|---|----|---|---|---|----|---|---|---|
| Audits Completed | 1 | 3 | 0 | 2 | 3 | 2 | 3 | 3 | 3 | 1 | 5 | 7 |
| Points Added | 1 | 5 | 0 | 5 | 11 | 3 | 0 | 6 | 11 | 2 | 0 | 0 |
| Points Completed | 4 | 6 | 8 | 7 | 9 | 6 | 4 | 8 | 0 | 6 | 5 | 1 |

Open audit points projected to be complete by September 30, 2009.

Audits Completed

(last 3 months)

Internal Audits

- REC Program Audits – Austin Energy Pilot Audit (Special Request)
- NERC CIP Standards –Procedural Readiness (Special Request – Part 1 of 2)
- Protocol 1.4 Independence Verification
- Internal Controls Tested
- Nodal Contractor Billings
- Q2 2008 Fraud Auditing Program
- Retrospective Assessment of IBM's Independent Reviews of Nodal Program Controls (Special Request)
- Nodal Procurement Compliance
- Nodal Spending

External Audits*

- Texas Nodal Program Controls- Review #6 (MP Nodal Readiness Evaluation)
- Texas Nodal Program Control – Review #7 (ERCOT Nodal Readiness Evaluation) (IBM – Managed by IAD)
- Benefit Plan Audit (Maxwell, Locke & Ritter)
- 2007 Financial Audit (PricewaterhouseCoopers)

Open Audits

Internal Audits

- Cash and Investments
- Operational Procedure Compliance
- Vendor-Performed Background Checks & Drug Screens for Contractors
- Q3 2008 Fraud Auditing Program
- Protocol 1.4 Ethics Compliance
- Annual Employee Ethics Compliance Audit
- PC Remediation Plan (Special Request- Part 2 of 2)

External Audits*

- SAS70 Audit (PricewaterhouseCoopers)

Planned Audits

(next 3 months)

Internal Audits

- NERC CIP Standards – Auditable Compliance (Special Request – Part 2 of 2)
- Annual Internal Quality Assessment Review – IIA Standards
- FY 2008 Fraud Auditing Program
- 2008 Year End Accruals Review (Special Request)

External Audits*

- Texas Nodal Program Review- New Schedule and Budget Validation (Report #8; Audit to be performed by Utilicast, LLC.)
- 2008 Financial Audit (PricewaterhouseCoopers)

*NOTE: Conducted by resources other than the Internal Audit Department.

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

External Assessments

1 security assessment

**Open Consultation/
Analysis Reviews**

External Assessments

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

External Assessments

1 security assessment
planned for Nodal
1 security assessment
planned

**ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
RISK MANAGEMENT EVENT PROFILE MATRIX (as of November 1st, 2008)**

| Strategic | Operational Excellence | Market Facilitation | Grid Reliability | Reporting | Legal and Regulatory Compliance |
|--|--|--|---|--|--|
| <p> Strategy Development <i>Corporate objective setting adequately incorporates informed stakeholder input, market realities and management expertise.</i></p> | <p> Performance Monitoring <i>Clearly defined and actively monitored performance metrics linked to mission and goals. Performance status communicated and corrective action taken.</i></p> | <p> Customer Choice <i>Market design promotes efficient choice by customers of energy providers with effective mechanisms to change incumbent market participants as desired.</i></p> | <p> Grid Operations <i>Information required to operate the grid is efficiently gathered. Appropriate tools are prudently configured to efficiently operate the system.</i></p> | <p> Review Practices <i>Prudent measures are taken to insure that company disclosures are properly vetted and not misleading.</i></p> | <p> Legal & Legislative <i>Operations are conducted in compliance with all laws and regulations. Impacts of current and proposed legislation are understood and communicated.</i></p> |
| <p> Mission and Goals <i>Corporate objectives and performance standards are understood and followed.</i></p> | <p> Business Practices <i>Business planning, processes and management standards are effective and efficient.</i></p> | <p> Nodal Implementation Project <i>Nodal Implementation on budget on schedule, and within defined scope.</i></p> | <p> Planning <i>Long-range planning methods enable efficient responses to system changes that are necessary to maintain reliability standards.</i></p> | <p> Disclosure <i>Reporting and other disclosures to intended parties is timely, accurate and effective.</i></p> | <p> Internal Control Compliance <i>Internal Control Compliance, processes and management standards are effective and efficient.</i></p> |
| <p>New Strategic Plan needs to be integrated into the latest business planning cycle.</p> | <p>Revisions to Business Continuity, Emergency Response and Pandemic Preparedness plans completed, approved and tested. DR plans and testing (table top only) completed for commercial/corporate applications. The Exchange system is now site redundant and all users will be on the redundant systems by the end of the year. Market Ops BC/DR testing for zonal systems is scheduled for completion by Q2-09.</p> <p>Future efforts will now focus on adding nodal systems to BC/DR Plans to coincide with the start of the 168-hr test. The specific timing of this test will be determined after the revised Nodal Schedule has been approved.</p> | <p>Program is "RED" based on the old schedule and budget. A new budget and schedule under development and will not be finalized until after the cost benefit analysis is completed by CRA.</p> <p>The program continues to hit the milestones identified over the next four months. Critical path items include a validated Common Information Model (CIM) that can be consumed by the energy management and market management systems. Other deliverables include release 5 of the network model management system and CIM importer. CIM importer has exited functional acceptance testing, a significant achievement.</p> <p>Several ERCOT employees have been added to the project while use of contractors has declined. Several leadership roles have changed to ERCOT staff and the program continues to move forward.</p> | <p>The Long Term System Assessment (LTSA) work has started. At the July Regional Planning Group meeting, a draft scope of work was discussed and we obtained helpful stakeholder feedback. The PUCT decision on CREZ Scenario 2 was very helpful in defining the starting point for the study. System Planning department staffing has improved, and a plan is in place to complete the LTSA as required.</p> | <p>ERCOT is reviewing the format and content of nodal reporting to insure information is adequate to support BOD governance function.</p> | <p>ERCOT is developing a process to ensure changes to policies/procedures are periodically communicated to all ERCOT staff and contract workers.</p> |
| <p> Reputation <i>Positive perceptions by stakeholders lead to less cost and greater flexibility resulting in enhanced enterprise value.</i></p> | <p> Workforce <i>Organization design, managerial and technical skills, bench strength and reward systems aligned with corporate goals.</i></p> | <p> Counterparty Credit <i>Maintain credit risk exposure for overall market within acceptable limits.</i></p> | <p> Bulk System Resources <i>Market Participants construct and make available adequate bulk electric grid resources.</i></p> | <p> Communication <i>Internal & external communications are timely and effective.</i></p> | <p> Industry Standards <i>Business practices provide stakeholders with required assurances of quality.</i></p> |
| <p>Increased publicity associated with the delay of the Nodal market and the potential for associated cost increases, anticipated new fee filings for the nodal surcharge and System Administration fee, high congestion, high price volatility and recent credit defaults have the potential to negatively impact ERCOT's reputation.</p> | <p>Turnover rate has improved and we are currently at 10.8% for voluntary turnover. The nodal readiness metric for employee staffing remains amber. There are a large number of contractors with expiration dates of December 2008 so work is underway to evaluate the continued need and extend contracts, as necessary. Since most contracts have a termination notice period of 30 days or less, ERCOT is extending the contracts beyond December 2008 to calm short term concerns. Succession plans are in place for employees at the officer and director level and a succession plan is being developed for critical nodal resources to also mitigate this risk. ERCOT is current recruiting for approximately 30 positions.</p> | <p>A draft Credit Risk standard has been circulated and is being reviewed with stakeholders. A proposal is expected to be submitted to F&A in December/January.</p> | | | <p>Initiation of ERO/TRE reliability standard Compliance Monitoring and Regional Entity Compliance Program in June introduces additional audit and penalty risks which ERCOT is still assessing. Although current decentralized compliance activities are adequate, ERCOT is in the process of centralizing the compliance function to provide more focus on these issues. The Chief Compliance Officer position is posted. The NERC Compliance Audit occurred September 9-12.</p> |
| <p> Fiscal Management <i>ISO design requires competent, prudent and cost effective provision of services.</i></p> | <p> Technology Infrastructure <i>Information systems, supporting facilities and data are effectively managed and are reliable.</i></p> | <p> Administration, Settlement & Billing <i>Market rules fairly applied to all participants. Accounting is timely and accurately reflects electricity production and delivery.</i></p> | <p> Operational Responsibility <i>Market participant conduct their operations in a manner which facilitates consistent grid reliability.</i></p> | <p> Adequacy and Integrity <i>Robust processes exist to support management assertions embodied within financial reports.</i></p> | <p> Regulatory Filings <i>Evidence, testimony and other supporting materials are compelling and successful.</i></p> |
| <p>ERCOT is beginning a review of collateral management practices and the company's Investment Policy. We continue to actively monitor the liquidation process associated with ERCOT funds held by The Reserve.</p> | <p>Systems remain stable in nearly all areas. Retail systems struggling to maintain SLA levels, especially Texas Market Link (TML). Implementation of system performance upgrades have improved overall system performance and stability. Normal operation growth patterns are increasing the demands on data center capacity and options to add capacity are limited until new facilities are built.</p> | | <p>Response of generators and LaaRs 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 which will provide additional incentive for improved performance. Increased wind generation will present additional operational challenges that a study indicated can be met. A joint ERCOT Staff and Market Participant Wind Operations Task Force is addressing several operational issues regarding wind generation and is making recommendations on changes to more reliably integrate wind generation.</p> | | <p>ERCOT has withdrawn its fee increase request filed last June with the Public Utility Commission in light of the delay in the nodal market implementation.</p> |

Legend: Elevated Risk Level Reduced Risk Level

(New Risk Categories / Descriptions Indicated in Green)

13. Committee Brief: PMO David Troxtell

Year to Date Project Activity by Division

| | Phase | Not Started | Initiation | Planning | Execution | Closing | Closed | Totals Excluding Non-Active | Cancelled | On Hold | Deferred | Totals by CART | Go-Live* (To Date) | Projected Go-Live (by Y.E.) |
|-------------|--------------------------|-------------|------------|----------|-----------|---------|--------|-----------------------------|-----------|---------|----------|----------------|--------------------|-----------------------------|
| CART | Corporate Operations | 7 | 1 | 9 | 10 | 2 | 15 | 44 | 9 | 0 | 4 | 57 | 12 | 12 |
| | IT Operations | 0 | 0 | 0 | 5 | 1 | 12 | 18 | 1 | 0 | 0 | 19 | 10 | 15 |
| | Market/Retail Operations | 0 | 0 | 3 | 6 | 2 | 7 | 18 | 1 | 1 | 13 | 33 | 7 | 10 |
| | System Operations | 0 | 0 | 1 | 3 | 0 | 3 | 7 | 0 | 0 | 0 | 7 | 2 | 4 |
| | Totals by Phase | 7 | 1 | 13 | 24 | 5 | 37 | 87 | 11 | 1 | 17 | 116 | 31 | 41 |
| | Total Non-Active | | | | | | | | 29 | | | | | |

* Note: Some projects in Closing and Closed Status went live in 2007

* Projects Gone Live in October 2008

(IO) PR-80023_01 Firewall Replacement

(CO) PR-60094_01 Physical Access Control Upgrade

(CO) PR-50015_03 Lawson Procurement Process Efficiency









(CO) PR-60020_02 Lawson 9.x Upgrade

13. Committee Brief: PMO David Troxtell

Year to Date Project Priority List (PPL) Status

| PPL Iterations | Origination | Project Phases | | | | | | | | Deferred Projects | Subtotal | Grand Total |
|---|-------------|----------------|------------|----------|-----------|---------|--------|---------|-----------|-------------------|----------|-------------|
| | | Not Started | Initiation | Planning | Execution | Closing | Closed | On Hold | Cancelled | | | |
| Original 2008 (October) PPL | | | | | | | | | | | 64 | |
| | PUCT | | | | | | | | | | 0 | |
| | Market | | | | 1 | 1 | | | | 1 | 3 | |
| | ERCOT | 7 | 1 | 5 | 13 | 2 | 9 | | 8 | 16 | 61 | |
| Unexpected Carry Over From 2007 | | | | | | | | | | | 30 | |
| | PUCT | | | | | | | | | | 0 | |
| | Market | | | | 1 | | 1 | | | | 2 | |
| | ERCOT | | | 2 | 4 | 1 | 19 | 1 | 1 | | 28 | |
| New Projects Added (Since PPL Approval in October 2007) | | | | | | | | | | | 22 | |
| | PUCT | | | | | | | | | | 0 | |
| | Market | | | | 1 | | | | | | 1 | |
| | ERCOT | | | 6 | 4 | 1 | 8 | | 2 | | 21 | |
| 2008 PPL Totals to Date | | | | | | | | | | | 116 | |
| | PUCT | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | |
| | Market | 0 | 0 | 0 | 3 | 1 | 1 | 0 | 0 | 1 | 6 | |
| | ERCOT | 7 | 1 | 13 | 21 | 4 | 36 | 1 | 11 | 16 | 110 | |
| Totals by Project Phase | | 7 | 1 | 13 | 24 | 5 | 37 | 1 | 11 | 17 | 116 | |

Year to Date Projects Over \$1 Million

| (CART) Project Number and Description | Total Budget | Total Committed | Metrics | |
|---|--|------------------------|--|--|
| (Duration) Phase (Sponsor) | Scheduled Completion | | Schedule | Budget |
| (CO) PR-60075_01: Identity Access Management <i>Schedule stoplight red due to time taken to re-schedule around Nodal 168 hour test.</i> | \$2.46M | \$2.21M |  |  |
| <i>(2006-2009) Currently in Execution (B. Kahn)</i> | <i>Expected Completion 1st Qtr 2009</i> | | | |
| (CO) PR-80001_01: (2 sub-projects, PR-80001_02 & PR-80001_03) MET Center Facility Analysis Deployment Phase 2 | \$70M | \$781K |  |  |
| <i>(2008 - 2011) PR-80001_01, PR-80001_02 & PR-80001_03 currently in Planning (B. Kahn)</i> | <i>Expected Completion 4th Qtr 2011</i> | | | |
| (MO/RO) PR-70007_01: MarkeTrak Enhancements | \$1.62M | \$1.35M |  |  |
| <i>(2007-2009) Currently in Execution (T. Doggett)</i> | <i>Expected Completion 1st Qtr 2009</i> | | | |
| (IO) PR-70054_01: (1 sub-project, PR-70054_02) Blade Refresh Deployment Phase 2 | \$2.50M | \$2.18M |  |  |
| <i>(2007-2008) PR-70054_01 Currently in Closed & PR-70054_02 Currently in Execution, (R. Hinsley)</i> | <i>Expected Completion 4th Qtr 2008</i> | | | |

13. Committee Brief: PMO David Troxtell

Baseline Budget vs. Actuals for Projects Closed in Lawson for 2008

| Project | Description | Year Implemented | Baseline Budget | Actuals | \$ Variance Fav/(Unfav) | % Variance Fav/(Unfav) | Explanation |
|----------|---|------------------|-----------------|-----------|-------------------------|------------------------|---|
| 70023_01 | Firewall Access Control Rationalization | 2008 | 450,485 | 160,640 | 289,860 | 64% | The AlgoSec software was negotiated and purchased at a much less cost than was originally estimated. |
| 70040_01 | IMM TRE Build Out | 2008 | 207,590 | 85,592 | 122,008 | 59% | Did not utilize contingency. The original plan was based on deploying cubicle spaces; the final plan did not utilize cubicle work spaces but tables against the walls (less expensive). |
| 70044_01 | MET Center Analysis | 2007 | 236,884 | 105,765 | 131,135 | 55% | ERCOT labor less than forecasted and consulting fees and contractor costs were 40% less than forecasted. Additionally, should not have included contingency of 10% on the contracted amounts for contractor services and equipment. |
| 60082_01 | Dynamic Rating Data to TSP | 2007 | 108,668 | 50,786 | 57,914 | 53% | 60082_01 was an unusual project. It took much longer than planned to complete, but it also required much less work than expected. The project turned out to be more of a configuration item than a software development project. |
| 70006_01 | ERCOT.com Outage Notification | 2007 | 118,428 | 57,612 | 60,788 | 51% | Scope split to deliver the remaining work in 70006_02. |
| 70055_01 | Additional Production SAN Capacity | 2008 | 1,749,999 | 903,708 | 846,292 | 48% | There were significant cost savings regarding hardware due to price negotiations. |
| 70026_01 | Virtual Tape Backup | 2007 | 1,349,999 | 768,534 | 581,466 | 43% | The \$581,466 variance for the 70026 project was due to price negotiations of hardware. All pricing was negotiated for lower costs than originally expected. |
| 60097 | Desk Side Standardization | 2007 | 760,930 | 522,884 | 238,016 | 31% | Used internal resources more than anticipated (thus reducing the number of hours worked by contracted resources) for the deskside systems replacement effort and Altiris redesign effort. Software purchased for hardware-independent imaging reduced the number of internal labor hours required for creating standards. |
| 70037_01 | OC-3 Microwave Replacement | 2007 | 325,995 | 229,359 | 96,641 | 30% | Change Control 2, processed on December 17th 2007, decreased the project budget from 350,000 to 250,000 which left a budget variance of 8.9%. No re-baseline was requested. |
| 60013_01 | Enhanced Digital Certificate Program | 2008 | 228,083 | 168,258 | 59,842 | 26% | The reason for the variance on the 60013_01 project was due to credits received from VeriSign in the amount of \$28,229. There was also \$20,135 for servers and operating systems that was not spent due to Nodal purchasing them for the MPIM project. |
| 70030_01 | Tellabs DSC Replacement | 2008 | 535,000 | 426,357 | 108,643 | 20% | The total budget was initially \$535K, but when we got to 2008 the current year budget was reduced to \$130K - this reduced the overall project budget to \$428K, which is the amount on the PSR. |
| 70005_01 | MO SAS 70 Proc Optimization | 2008 | 285,999 | 229,827 | 56,173 | 20% | Tasks over estimated by 10% and 10% contingency. |
| 60077_01 | ERCOT_com Secured Area Enhancements | 2007 | 207,590 | 284,399 | (76,799) | (37)% | Completed the project with FTE's instead of Contractors |
| 70053_01 | Video Conferencing | 2008 | 131,837 | 106,747 | 25,053 | 19% | Actuals is reduced due to a true-up with Accounting for project closure |
| 70048_01 | MV90xi System Upgrade | 2008 | 89,249 | 73,452 | 15,748 | 18% | IT hardware cost reductions due to volume discount purchases. |
| 60055_01 | Enterprise Service Management | 2008 | 1,612,831 | 1,334,826 | 277,974 | 17% | Savings through sales tax exemptions, maintenance charges booked to pre-pay accounts. Labor costs lower than budgeted. |
| 70012_01 | Secure Remote Access | 2008 | 403,041 | 337,169 | 65,831 | 16% | Slight reduction in scope based on problems experienced during rollout with drive mapping, memory utilization on intranet controllers, and issues with VMWare. |

13. Committee Brief: PMO David Troxtell

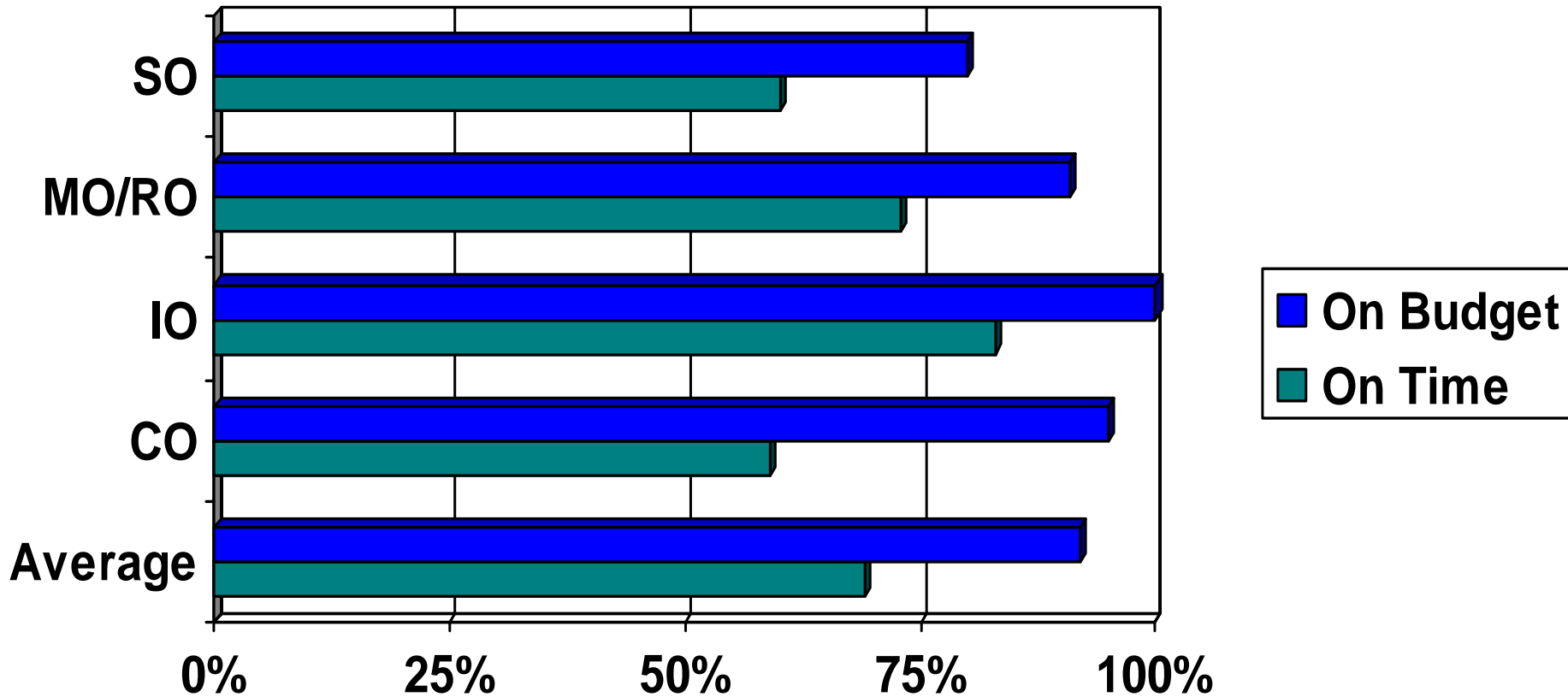
Baseline Budget vs. Actuals for Projects Closed in Lawson for 2008

| Project | Description | Year Implemented | Baseline Budget | Actuals | \$ Variance Fav/(Unfav) | % Variance Fav/(Unfav) | Explanation |
|----------|--|-------------------|----------------------|----------------------|-------------------------|------------------------|--|
| 70039_01 | Risk and Compliance Management | 2007 | 366,800 | 318,583 | 48,217 | 13% | Invoices were accrued against the project that should not have been which resulted in the lower actuals. |
| 70041_01 | Control Room Display Replacement | 2008 | 418,300 | 366,562 | 51,738 | 12% | Did not use contingency and equipment was \$14,000 less than forecasted. |
| 80022_01 | Additional SAN Capacity for Projects | 2008 | 1,950,000 | 1,717,133 | 232,867 | 12% | Internal labor costs were lower than budgeted because the project was completed early. |
| 80035_01 | Intranet Assessment for HR and Communications | 2008 | 14,600 | 13,053 | 1,548 | 11% | Did not use contingency. |
| 60099_01 | TCC2 Finish-out and Annex Construction | 2007 | 2,362,000 | 2,142,026 | 219,974 | 9% | |
| 70049_01 | San Hardening | 2007 | 880,000 | 805,429 | 74,571 | 8% | |
| 70038_01 | ERCOT com Infrastructure Enhancement | 2008 | 397,200 | 363,607 | 33,593 | 8% | |
| 70050_01 | EIS ETL Tool Implementation | 2007 | 478,500 | 442,473 | 36,027 | 8% | |
| 70051_01 | Exempt Non Exempt | 2008 | 89,800 | 86,967 | 2,833 | 3% | |
| 50031 | EDW EMMS Decommission | 2007 | 485,600 | 476,864 | 8,736 | 2% | |
| 60104_01 | EMMS Hardware Replacement | 2008 | 905,400 | 899,726 | 5,674 | 1% | |
| 60073_01 | eRecruiting Deliverables | 2008 | 127,200 | 130,416 | (3,216) | (3)% | |
| 50123_03 | Document Management - Ph III | 2007 | 137,400 | 141,913 | (4,513) | (3)% | |
| 50024 | Enhancements to SCR727 | 2007 | 1,607,300 | 1,674,678 | (67,378) | (4)% | |
| 70013_01 | Corporate Document Management | 2008 | 69,700 | 72,878 | (3,178) | (5)% | |
| 70035_01 | REC 2007 | 2008 | 146,300 | 159,280 | (12,980) | (9)% | |
| 50137_02 | Maestro Replacement - Ph II | 2007 | 10,000 | 11,207 | (1,207) | (12)% | PR-50137_02 had a change in scope and a budget reduction on the 2007 PPL to \$10,000 in early 1Q of 2007. The budget was allocated for a fixed-fee consultant contract of \$10,000 that was executed in December 2007. However, the PPL budget allocation did not account for additional travel expenses for the consultant, which amounted to a total of \$1,207 and was accrued in 2007. |
| 60077_01 | ERCOT_com Secured Area Enhancements | 2007 | 207,600 | 284,399 | (76,799) | (37)% | Completed the project with FTE's instead of Contractors |
| 70047_01 | Corporate Application Environment True up | 2008 | 220,500 | 320,677 | (100,177) | (45)% | Accounting error--a pending journal entry will remove \$92,794.39 in HW/SW Maintenance costs from this project |
| 50070_01 | Unit Testing Automation and Electronic Submittal via Web | 2008 | 180,000 | 263,510 | (83,510) | (46)% | PRR750 added the Unannounced Testing scope. Internal ERCOT added the following functionality. (Ability to test Combined Cycle Units, Add color coding to identify QSE entered fields, Disable 90% of HSL field if Unit if not applicable & EMS Batch Load Process) |
| 50017_02 | Collateral Calculation | 2008 | 359,100 | 598,164 | (239,064) | (67)% | Several iterations for requirements clarification required. |
| 50071_01 | Governor Analysis Enhancements | 2008 | 92,000 | 160,901 | (68,901) | (75)% | Business requested additional functionality adding to the scope of the project. The additional costs reflects the scope changes. |
| 60086_01 | Lawson Time Entry | 2007 | 68,900 | 125,089 | (56,189) | (82)% | Original resources were replaced with contract resources that were at a higher rate as they brought specific Lawson experience. |
| | | Count = 40 | \$ 22,669,100 | \$ 19,117,500 | \$ 3,551,600 | 16% | |

NOTES:

1. Baseline budget does not include change controls that were approved without granting a new baseline budget.
2. List and totals include projects delivered and reported in previous years Project Management reports but closed in Lawson in 2008.
3. Favorable is when a project is delivered under budget. (UnFav)orable is when a project is delivered over budget.
4. Explanations are not required for variance + or - 10%

2008 Active Projects Performance



Note: Includes projects started in previous years.
Projects that change to inactive states will impact results.

Go Live Projects for October

- **PR-80023_01 Firewall Replacement**
 - **Scope:** This project provided the following benefits
 - minimized configuration overhead
 - increased efficiency
 - reduced probability of error
 - consolidated logging
 - **Deliverables:** Replaced existing Nokia Check Point firewalls with Cisco PIX (ASA).
 - **Timeline:** June 2008 – October 2008

Go Live Projects for October

- **PR-60094_01 Physical Access Control Upgrade**
 - **Scope:** Upgrade the current physical access control system, which is used to control and monitor people entering and exiting ERCOT facilities and restricted areas.
 - **Deliverables:** Purchase and deployment of the Lenel physical access system, to include the master and regional servers, security workstations, and the physical access software. This project also included the purchase of mustering stations and the installation and configuration of the badge creation software.
 - **Timeline:** October 2006 - October 2008

Go Live Projects for October

- **PR-50015_03 Lawson Procurement Process Flow**
 - **Scope:** Provide foundation to eliminate Procurement Requisition Form
 - **Deliverables:**
 - Installation of Lawson Requisition Self Service (RSS) module
 - Pilot Program of RSS in the area of Information Technology (IT)
 - Development of a Procurement Portal to track a requisition through the current “procure to pay” process
 - **Timeline:** September 2006 - October 2008

Go Live Projects for October

- **PR-60020_02 Lawson 9x Upgrade**
 - **Scope:** To upgrade ERCOT's Lawson financial tool from 8.0 to 9.0 version.
 - **Deliverables:** The project delivered all functionality that was in the 8.0 version in the 9.0 version. In addition, the project delivered a Production, Testing, and Development environment. This application is hosting externally to ERCOT.
 - **Timeline:** September 2007 – October 2008

13. Committee Brief: PMO – ERCOT Enterprise Projects Summary Report

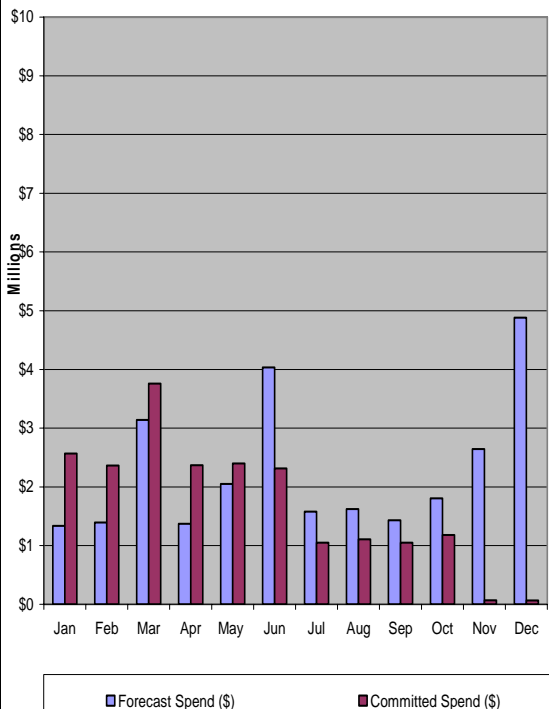
ERCOT Overall Projects Report

Reporting Period: 11/4/2008

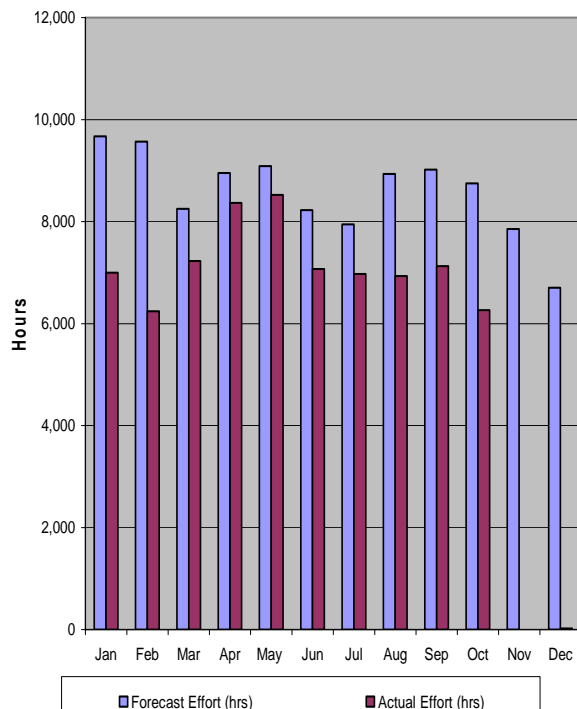
| Summary | ERCOT Projects Leadership | | Projects in ERCOT's Portfolio | | | | | Portfolio Performance | | |
|-------------|---------------------------|--------------|-------------------------------|-----------------------|----------|-----------|---------|-----------------------|--------------|------------|
| | Executives | | On Hold | Initiation | Planning | Execution | Closing | Schedule | Budget | Milestones |
| | Kent Saathoff | Trip Doggett | 1 | 1 | 13 | 25 | 5 | Y | G | Y |
| Ron Hinsley | Steve Byone | Closed | 37 | Total Active | | 44 | | | | |
| | | Cancelled | 11 | Projects Not Started: | | 7 | | | | |
| | | | | | | | | Current Year Funding: | \$33,746,880 | |

Portfolio Performance Summary

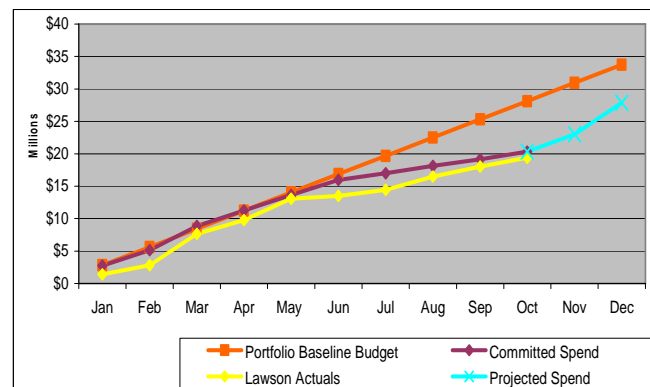
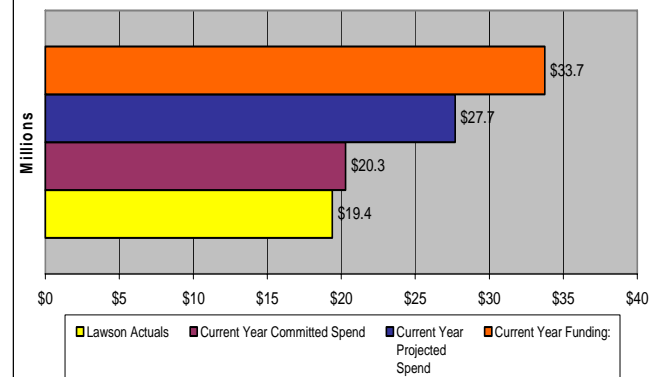
ERCOT Projects
Current Year - Spend



ERCOT Projects
Current Year - Effort



ERCOT Projects
Current Year to Date Financials



Notes

Note:
Project/Status Count/Budget Variance:
 CO:(4 Deferred); MORO:(13 Deferred); SO-DPO:(1 NODAL in Execution).



Future Agenda Items – December 2008

- **Approval of 2009 Internal Audit plan**
- **Review results of Finance & Audit Committee self assessment**
- **Assessment of the adequacy and effectiveness of the Internal Audit staff**
- **Review and approval of 2009 operating budget**
- **Update on ERCOT credit risk standard**
- **Update on investments and investment policy (Vote)**
- **Review listing of dealings with financial institutions that are also market participants**
- **Committee briefs**
- **Future agenda items**

F&A Yearly Schedule

Quarter 1

- √ •Elect officers and confirm financial qualifications
- √ •Review of external auditor quality control procedures and independence
- √ •Review scope of annual financial audit
- √ •Vote on CWG Chair/Vice Chair

Quarter 2

- √ •Report results of annual independent audit to the Board
- √ •Review the procedures for handling Reporting violations
- √ •Review results of annual audit, together with significant accounting policies (including required communications)
- √ •Review ERCOT Annual Report
- √ •Review operating plan and budget assumptions
- √ •Review and approve Internal Audit Department Charter
- √ •Conduct annual review of insurance coverage(s)
- √ •Review the Company's dealings with any financial institutions that are also market participants

Quarter 3

- √ •Appoint the independent auditors for upcoming year
- √ •Approval of independent auditor fees for upcoming year
- √ •Review of committee charter
- √ •Approve the Guidelines for Engagements of External auditors for Other Services (pre-approval policy)
- √ •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
- Review the Company's dealings with any financial institutions that are also market participants

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