

ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
MINUTES OF THE ISO FINANCE & AUDIT COMMITTEE – GENERAL SESSION
7620 Metro Center Drive – Austin, Texas 78744
November 17, 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 7:35 a.m. The Committee met in Executive Session from 7:35 a.m. to 8:00 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	Not Present
Wilkerson, Dan	Bryan Texas Utilities	Municipal	Present

Other Board Members and Segment Alternates:

Armentrout, Mark	Unaffiliated Board Member	Unaffiliated Board Member	Present
Smitherman, Barry T.	Public Utility Commission	PUC Chairman	Present
Walker, Mark	NRG Texas	Independent Generator	Present

ERCOT staff and guests present:

Barry, Sean	PricewaterhouseCoopers (<i>via phone</i>)
Brenton, Jim	ERCOT – Director, Corporate Security
Bruce, Mark	FPL Energy
Byone, Steve	ERCOT – Vice President and Chief Financial Officer
Coffing, Timothy	Luminant
Day, Betty	ERCOT – Director, Commercial Operations
Doolin, Estrellita	ERCOT – Assistant General Counsel
Dreyfus, Mark	Austin Energy
Forfia, David	ERCOT – Senior Director, Information Technology
Fox, Kip	AEP
Grable, Mike	ERCOT – Vice President and General Counsel
Greer, Clayton	J Aron & Company
Grimes, Mike	Horizon Wind
Hinsley, Ron	ERCOT – Vice President and Chief Information Officer
Jones, Don	Reliant
Kahn, Bob	ERCOT – President and Chief Executive Officer
Kolodziej, Eddie	Customized Energy Solutions
Leady, Vickie	ERCOT – Associate Corporate Counsel
Lester, Suzanne	ERCOT – Executive Assistant - Finance
Magness, Bill	Casey, Gentz & Magness, LLP

Moore, John	EON
Pappas, Laurie	Office of the Public Utility Counsel
Petterson, Mike	ERCOT – Controller
Reid, Walter	Wind Coalition
Roberts, Grady	ERCOT – Director, Contract Administration & Procurement
Robinson, Lane	Babcock & Brown
Seely, Chad	ERCOT – Corporate Counsel
Smallwood, Aaron	ERCOT – Director, IT Strategic & Financial Services
Stauffer, Tarra	ERCOT – Legal Assistant
Taylor, William	Calpine
Troxell, David	ERCOT – Director, Program Management Office
Vincent, Susan	Texas Regional Entity – Director, Legal Affairs
Wagner, Marguerite	PSEG, Texas
Wiswell, Steve	Competitive Assets
Wullenjohn, Bill	ERCOT – Director, Internal Audit
Yager, Cheryl	ERCOT – Treasurer

Approval of Prior Meeting General Session Minutes

Nick Fehrenbach moved to approved the minutes for the General Session of the Finance & Audit Committee meeting held on October 21, 2008. Miguel Espinosa seconded the motion. The motion passed by unanimous voice vote with no abstentions.

2008 SAS 70 Audit

Sean Barry joined the meeting via telephone and provided a brief update on the 2008 SAS 70 Audit. Mr. Barry informed the Committee that no significant issues had been identified for the audit period that ended September 30, 2008. He also informed the Committee that the final report was expected to be delivered to the Board in December 2008.

Collateral Management

Cheryl Yager referred to materials that had been distributed prior to the meeting and led a discussion about how ERCOT manages collateral it receives from Market Participants. Ms. Yager reviewed applicable ERCOT Protocol language, historical levels of cash collateral, current ERCOT practices, other ISO practices, possible options for collateral management and next steps for the Committee. Brad Cox acknowledged that any approach for managing collateral would have pros and cons and suggested that ERCOT consider removing itself from between the Market Participant and fund managers by creating escrow accounts. Ms. Yager commented that there was some concern about the level of complexity associated with creating escrow accounts for each Market Participant that posted collateral. Clifton Karnei asked whether an escrow account was an alternative that a Market Participant could request. Ms. Yager responded affirmatively and noted that ERCOT could decline to honor such a request in its sole discretion. She added that ERCOT had received one or two requests to create escrow accounts in the past and that ERCOT had chose not to create the accounts. Mr. Cox suggested that ERCOT Legal and possibly outside counsel review the Protocol language and make suggestions to clarify any ambiguous language.

Miguel Espinosa asked whether the structure of funds maintained for Market Participants had any effect on ERCOT's ability to access funds. Ms. Yager responded that a concern over access to funds during default situations was one reason that ERCOT had held collateral at ERCOT rather than in escrow accounts. She noted that ERCOT does not commingle funds held as collateral with ERCOT, Inc. operating funds and maintains collateral accounts separately from operating accounts.

During the discussion about other ISO practices, Mr. Karnei confirmed that other ISO Market Participants were allowed to select from funds that had been pre-approved by an ISO then asked which entity (the Market Participant or the ISO) would bear the risk of loss. Ms. Yager responded that she had been unable as of the meeting time to get a definitive answer from any of the other ISOs regarding the risk of loss question.

Mr. Cox stressed the importance of diversifying risk and expressed a need to understand with certainty which entity (the Market Participant or ERCOT) would bear the risk of loss in all the structure options being considered. Mr. Espinosa agreed with the comments about diversification and further suggested that he would prefer to see more than four or six funds used and probably no more than \$25 million in any one fund. PUC Chairman Smitherman cautioned the Committee about only considering the number of funds and suggested that they focus on the underlying investments of the funds selected.

Clifton Karnei suggested that the Committee first confirm its primary objective with respect to managing collateral before deciding whether to change the current structure. PUC Chairman Barry T. Smitherman suggested that investing in US Government securities could be an option if there was no obligation to obtain large returns. Mr. Karnei acknowledged that while there was no obligation to obtain large returns, historically there was implicit pressure to keep the returns as high as possible to minimize the negatives associated with requiring collateral. He commented that lower returns would be a bigger hit to Market Participants since they received the benefit of interest income.

Mark Armentrout suggested that ERCOT's primary objectives with respect to managing collateral were (1) to have funds available when needed, (2) preservation of collateral, and (3) complete control of deposited collateral.

Mr. Karnei requested that staff prepare a recommendation (including a legal opinion on the issues previously discussed) for achieving the following three objectives: (1) preserve collateral, (2) timely access to collateral, and (3) ease of returning collateral. Ms. Yager agreed to provide the recommendation after the December meeting.

Financial Corporate Standard

Cheryl Yager referred to the Financial Corporate Standard that had been distributed prior to the meeting and reviewed the proposed changes. **Miguel Espinosa moved to approve the Financial Corporate Standard including the proposed changes; Nick Fehrenbach seconded the motion. The motion passed by unanimous voice vote with no abstentions.**

Investment Corporate Standard

Cheryl Yager led a discussion on the Investment Corporate Standard that had been distributed to the Committee prior to the meeting. Ms. Yager covered investment objectives, risk-return consideration, approaches, identified changes and next steps. Clifton Karnei suggested the Purpose section of the Standard be revised to capture the Committee's conclusions regarding return objectives. In response to Mr. Karnei's suggestion, Ms. Yager agreed to present staff's recommendation regarding changes to the Investment Corporate Standard to the Committee in January. Steve Byone reminded the Committee that changes to the Investment Corporate Standard could have implications on the administration fee since part of operating costs had been offset by revenues from investments in the past.

2008 Year End Projections

Michael Petterson reviewed for the Committee the expected favorable variance in base operating activity projected for 2008. Committee members generally agreed with management's recommendation to make a \$12.5 million principal payment in November 2008 as planned. Mr. Petterson explained that the principal reduction would be made to the revolver rather than the term loan facility to enhance ERCOT's financial flexibility.

Timeline for Approval of Revised 2009 Base Operating Budget

Mike Petterson provided information on the updated timeline for approval of the 2009 Base Operating Budget and solicited input from the Committee. He explained that the original approval schedule, which was very tight and allowed no room for slippage of upstream activity, now required revisions due to delays with preparation of an updated Nodal Program budget. He described the revised approval timeline as a two-step process. The first step being to request approval of a one-month budget for January 2009 in December 2008 and the second step being to request approval of the full, revised 2009 base operating budget in January 2009. Committee members did not voice any opposition to the two-step approval process as described.

Timeline for Nodal Program Budget

Mr. Espinosa asked Ron Hinsley when there would be a completed Nodal budget. Mr. Hinsley responded that the Cost Benefit Analysis would need to be completed before a budget could be finalized. Mr. Karnei commented that Nodal Project budget would be discussed at length during the Executive Session of the Board of Directors meeting.

Nodal Interim Rate Relief Request

Cheryl Yager reviewed for the Committee the facts and circumstances leading up to the need to request an increase in the Nodal fee. She noted that approximately \$12 million per month of spending authority was requested by Nodal Program leadership to continue to progress the Program and that the funding would need to be accomplished through some combination of revenue and/or debt financing. Brad Cox asked whether ERCOT had received from Market Participants reactions regarding the proposed fee increase. Bob Kahn responded that any change to the fee would cause issues because Market Participants' budgets were set. Mr. Kahn added that the rate increase sought was an interim increase. Steve Byone commented that he understood the rate increase would be difficult for Market Participants and reminded the Committee of the need to identify a viable funding source if the Nodal Program was to continue. Charles Jenkins acknowledged the need to fund the Nodal Program with a larger equity proportion than had occurred to date, but expressed discomfort with sourcing the additional costs required—even on an interim basis—with 100 percent equity. Mr. Byone commented that utilizing ERCOT's available debt capacity to fund the Nodal Program would mean less debt to fund other projects such as advanced metering and construction projects and could mean ERCOT would be unable to address unexpected needs.

Charles Jenkins moved to recommend that the Board authorize ERCOT to make a filing with the Public Utility Commission of Texas to request an increase in the Nodal Surcharge from \$0.169 per MWh to an amount that corresponds to a 40 percent equity/ 60 percent debt split (approximately \$0.22 per MWh); Dan Wilkerson seconded the motion. The motion was approved. Clifton Karnei and Nick Fehrenbach opposed the motion.

Audit Committee Meeting Planner for 2009

Steve Byone sought approval of the audit committee meeting planner for the upcoming year and confirmed mutual expectations with management and auditors. He mentioned that the items on

the Yearly Schedule were the same items included in 2008 schedule. No concerns or additions were voiced.

Finance & Audit Committee Self Assessment

Steve Byone reminded Committee members that the Committee Charter required that a self-assessment be completed. He informed them that each Committee member would receive instructions for completing the annual Committee self-assessment via email and that they might have an option to complete the assessment online. He added that results from the assessment would be compiled and prepared for review during the December Committee meeting.

Market Participant Guarantee Agreements

Tim Coffing, Vice-Chair of the Credit Work Group (CWG), addressed the Committee and asked for clarification on the reasons why the draft Guarantee Agreements proposed by CWG were rejected by the Committee. Clifton Karnei responded that the drafts were "watered down" compared to the drafts initially proposed by ERCOT Legal. Mr. Karnei explained that the Committee was inclined to approved the more stringent versions initially proposed by ERCOT Legal without additional rationale from CWG regarding the "watered down" changes. Mr. Coffing responded that he would try to gather and provide more information for the Committee. Messrs. Gent, Karnei and Cox asked that Mr. Coffing provide brief explanation of the reasoning behind each item proposed by ERCOT Legal that was removed or changed in order of most to least significant. Mr. Coffing agreed to try to get the information from Market Participants no later than the January Committee meeting.

Credit Work Group Charter and Membership Requirements

Tim Coffing and Cheryl Yager referred to the Credit Work Group Charter that had been distributed prior to the meeting and reviewed the changes that had been proposed by ERCOT staff and approved by the Credit Work Group (CWG). **Dan Wilkerson moved to approve the CWG Charter including the proposed changes; Nick Fehrenbach seconded the motion. The motion passed.**

Market Credit Risk Standard

Tim Coffing provided an update on the status of the Market Credit Risk Standard under review by the Credit Work Group (CWG). He explained that CWG had not reached consensus regarding the standard and that two camps existed. One camp preferred to revise the standard to give staff more flexibility; the other preferred to approve the standard as proposed. Clifton Karnei encouraged CWG to work towards consensus and come back to the Committee in February with a recommendation.

Committee Briefs

Steve Byone referred to materials distributed prior to the meeting for the following areas:

1. Market Credit
2. Internal Control Management Program
3. Enterprise Risk Management
4. Project Management Organization

He directed the Committee's attention to the Risk Management Event Profile Matrix ("Stop Light Report") and commented that the risk level for Technology Infrastructure was elevated because of data center capacity issues.


Future Agenda Items

Clifton Karnei referrec. to the following future agenda items asked if there were any suggestions for additional future agenda items:

1. Approval of 2009 Internal Audit plan
2. Review results of Finance & Audit Committee self-assessment
3. Assessment of the adequacy and effectiveness of the Internal Audit staff
4. Review and approval of 2009 operating budget
5. Update on ERCOT credit risk standard
6. Update on investments and investment policy
7. Review listing of dealings with financial institutions that are also market participants
8. Committee briefs
9. Future agenda items

Adjournment

Clifton Karnei adjourned the meeting at approximately 9:55 a.m.



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