

## ERCOT CORPORATE STANDARD

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|-----------------|--|
| Document Name:  | Investment <del>Corporate</del> 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~~held by ERCOT, whether those funds arise from ERCOT operations or are held by ERCOT on behalf of the ERCOT market.

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

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

### 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. ERCOT staff will not duplicate credit analysis performed by fund managers and are not expected to provide assurance that all holdings are creditworthy

**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 Losses.**

Option A All investment losses incurred on funds held by ERCOT on behalf of Market Participants are attributable to Market Participants and are not borne by ERCOT while investment losses on ERCOT, Inc. funds are borne by ERCOT, Inc.

Option B Investment losses incurred on funds held by ERCOT on behalf of Market Participants for collateral are attributable to Market Participants and are not borne by ERCOT while all other losses are borne by ERCOT, Inc.

ERCOT shall not have any fiduciary relationship with Market Participants and no implied covenants, functions, responsibilities, duties, obligations or liabilities shall be read into this corporate standard. Investment losses attributable to Market Participants shall be addressed in the ERCOT Protocols or by direction from ERCOT Board of Directors.

**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 monthly 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. <del>Repurchase agreements in which the collateral is obligations</del> Obligations [cy1] of or guaranteed by <del>the</del> US government. (Note 3) <del>at entities (e.g. federal agencies, state or municipal, etc)</del> | Note 2                            | 7 days or less                      | \$5,000,000                   | 33% of total                   |
| <del>3. Certificates of deposit and share certificates</del>  | <del>Note 2</del>                 | <del>1-yr or less</del>             | <del>\$5,000,000</del>        | <del>33% of total</del>        |
| <del>4. Repurchase agreements in which the collateral is government or agency securities (1 or 2 above). (Note 3)</del>   | <del>Note 2</del>                 | <del>7 days or less</del>           | <del>\$5,000,000</del>        | <del>33% of total</del>        |
| <del>3. Money market mutual funds (MMMF) invested only in obligations of or guaranteed by the US government</del> 5. Commercial paper   | <del>Note 4</del> A1/P1 or better | <del>Note 4</del> 1-yr or less      | <del>Note 4</del> \$5,000,000 | <del>Note 5</del> 33% of total |
| <del>6. Banker's acceptances</del>  | <del>Note 2</del>                 | <del>1-yr or less</del>             | <del>\$5,000,000</del>        | <del>33% of total</del>        |
| <del>7. Money market mutual funds (MMMF)</del>  | <del>Note 4</del>                 | <del>Note 4</del>                   | <del>Note 4</del>             | <del>none</del>                |

Note 1: To the extent possible, ERCOT will attempt to match its investments with anticipated cash flow requirements. ~~Some~~A-base level of cash may remain uninvested to meet the ~~liquidity~~operating needs of ERCOT, Inc. and the ERCOT market or to address unusual situations as they arise.

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.

Note 5: There is no limit on how much money may be placed with MMMFs in this category because of the requirements on those funds outlined in Note 4. However, ERCOT must diversify investments held in money market accounts across at least two different fund families. Based on availability of funds meeting the above investment criteria, ERCOT will seek to ensure that no more than \$100 million is maintained in any one fund.