



**ERCOT Finance & Audit Committee Meeting**  
**7620 Metro Center Drive, Austin, Texas**  
**Met Center, Conference Room 206**  
**June 15, 2010; 8:00am – 9:55am\***

Item #	Agenda Item Type	Description/Purpose/Action Required	Presenter	Time
1.		Call to order Executive Session	C. Karnei	8:00am
2.		2a. Announcement of proxies	C. Karnei	8:01am
	Decision required	2b. Approval of executive session minutes (Vote) (5/18/10)	C. Karnei	8:02am
	For discussion	2c. Review second draft of F&A survey of Internal Audit	B. Wullenjohn / T. Doggett	8:05am
	For discussion	2d. Update on timeline for 2011 Internal Audit plan	B. Wullenjohn	8:20am
	For discussion	2e. Internal Audit status report	B. Wullenjohn	8:25am
	Informative	2f. EthicsPoint update	B. Wullenjohn	8:30am
	Decision required	2g. Discussion of debt financing proposal (Vote)	C. Yager	8:35am
3.	Informative	Contracts, personnel, litigation and security	Various	8:50am
		Recess Executive Session		8:55am
		<b>Convene General Session</b>		
4.	Decision required	Approval of general session minutes (Vote) (05/18/10)	C. Karnei	8:55am
5.	Decision required	Approval of debt financing proposal (Vote)	C. Karnei	8:57am
6.	For discussion	Review the procedures for handling financial reporting violations	M. Petterson	9:00am
7.	For discussion	Preparation for 2011 budget	M. Petterson	9:05am
8.	For discussion	Texas Regional Entity financial summary	M. Petterson	9:20am
9.	Informative	Parent guarantees for financial institutions	C. Greer	9:25am
10.	Informative	Committee Briefs (Q&A only)	All	9:40am
11.	Informative	Future agenda items	M. Petterson	9:45am
12.		Other business	M. Petterson	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, July 20, 2010, at ERCOT, 7620 Metro Center Drive, Austin, Texas 78744, in Room 206.

Decision required
For discussion

## 4. Approval of General Session Minutes Clifton Karnei

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### **Approval of General Session Minutes**

- Vote 05/18/10

**DRAFT ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.  
MINUTES OF THE FINANCE & AUDIT COMMITTEE – GENERAL SESSION**

7620 Metro Center Drive (Room 206) – Austin, Texas 78744  
May 18, 2010

Pursuant to notice duly given, the Finance & Audit Committee (“Committee”) of Electric Reliability Council of Texas, Inc. (“ERCOT”) convened on the above-referenced date. Committee Chairman Clifton Karnei confirmed that a quorum was present and called the meeting to order at approximately **7:35 a.m.** The Committee immediately went into Executive Session, where it remained until it recessed and reconvened to General Session at **9:09 a.m.**

**Committee members:**

Crowder, Calvin	American Electric Power Service Corporation	Investor Owned Utility	Present
Dreyfus, Mark	Austin Energy	Municipal	Present
Espinosa, Miguel (Vice Chair)	Unaffiliated Board Member	Unaffiliated Board Member	Present
Fehrenbach, Nick	City of Dallas	Commercial Consumers	Absent
Gent, Michehl	Unaffiliated Board Member	Unaffiliated Board Member	Present
Karnei, Clifton (Chair)	Brazos Electric Power Cooperative	Cooperative	Present
Zlotnik, Marcie	StarTex Power	Independent REP	Present

**Other Board Members and Segment Alternates:**

Walker, Mark	NRG Texas	Independent Generator	Present
Whittle, Brandon	DB Energy Trading	Independent Power Market Representative	Present

**ERCOT Staff and Guests:**

Baker, Randy	ERCOT – Director, Credit Risk Management
Beckham, Rebecca	ERCOT – Senior Financial Analyst
Bruce, Mark	MJB Consulting
Day, Betty	ERCOT – Director, Commercial Operations
Deskins, Andy	Wachovia
DiPastena, Phil	ERCOT – Manager, Enterprise Risk
Doggett, Trip	ERCOT – Interim President and Chief Executive Officer
Forfia, David	ERCOT – Director, IT Infrastructure
Jefferis, Don	Opportune
Lester, Suzanne	ERCOT – Executive Assistant, Finance
Manning, Chuck	ERCOT – Vice President and Chief Compliance Officer
Medina, Eric	ERCOT – Opportune Consultant
Morais, Matt	ERCOT – Assistant General Counsel
Morehead, Juliana	ERCOT – Associate Corporate Counsel
Morgan, Richard	ERCOT – Vice President and Chief Information Officer
Petterson, Mike	ERCOT – Controller
Seely, Chad	ERCOT – Senior Corporate Counsel
Swanson, Leslie	ERCOT – Manager, Treasury (Contractor)

Wullenjohn, Bill	ERCOT – Director, Internal Audit
Yager, Cheryl	ERCOT – Treasurer

### **Announcement of Proxies**

Chairman Clifton Karnei confirmed that a quorum was present and no proxies had been submitted.

### **Approval of Prior Meeting General Session Minutes**

Michehl Gent asked that the April 20, 2010 General Session F&A Committee meeting minutes be revised to reflect that Miguel Espinosa called the meeting to order confirmed a quorum was present.

**Mr. Gent moved to approve the minutes for the General Session of the Committee meeting held on April 20, 2010 as revised. Calvin Crowder seconded the motion. The motion passed unanimously with no abstentions.**

### **Approval of the Internal Audit Department Charter**

Bill Wullenjohn presented the Internal Audit Department Charter for approval and reminded the Committee that it reviewed and discussed the proposed Internal Audit Department Charter (“Charter”) at the Committee meeting in April 2010. The proposed Charter included recommended changes to conform to new Institute of Internal Auditors (“IIA”) guidelines. Mr. Wullenjohn added that Trip Doggett, Interim Chief Executive Officer, had also reviewed the proposed Charter.

**Mr. Crowder moved to approve the Internal Audit Department Charter. Marcie Zlotnik seconded the motion. The motion passed unanimously with no abstentions.**

### **Approval of a Debt Financing Proposal**

Mr. Karnei commented that the Committee had reviewed various debt financing proposals during Executive Session. He stated that there would be no action taken at the Board of Directors meeting later that day, but the Committee would be reviewing the proposals in more depth and planned to recommend action to the Board at the June 2010 meeting.

### **Approval Review of Market Credit Risk Corporate Standard**

Randy Baker directed the Committee to materials provided prior to the meeting, which outlined the Market Credit Risk Corporate Standard (“Standard”). Mr. Baker gave the Committee an overview of the annual review of the Standard, and fielded Committee questions. He added that the Standard was originally approved by the Board of Directors in May 2009, and was being presented for renewal with minor revisions and clarifications.

Mr. Baker discussed potential future risk exposure and requested an exemption from running the current zonal model for second and third quarters of 2010, given the impending Nodal go-live. He noted the following clarification changes to language in the Standard: (a) additional language to address the request for a review of the model after one year following Nodal go-live; and (b) revised language concerning the running of stress scenarios by the Board, TAC, or Credit Work Group.

Mr. Crowder asked about the approach taken in developing the additional risk factors for the nodal market. Mr. Baker replied that he attempted to capture the high-level aspects of the nodal market for which ERCOT did not have coverage under the zonal market model. Mr. Baker further stated that ERCOT was planning to work on the model through summer 2010, and anticipate completion of the model in fall 2010.

Mr. Karnei entertained a motion for approval of the revised Standard.

**Calvin Crowder moved to approve the Market Credit Risk Corporate Standard with noted revisions. Marcie Zlotnik seconded the motion. The motion passed unanimously with no abstentions.**

Mr. Karnei noted that the Standard was approved, with changes noted.

### **Review Company Dealing with Financial Institutions Who Are Market Participants**

Leslie Swanson provided the Committee with a brief update on Market Participant financial institutions doing business with ERCOT (i.e., JP Morgan and Bank of America). She informed the Committee that there had been no change to the entities previously disclosed, but that this agenda item was a disclosure item, required each six months.

### **Pre-Approval of Non-Audit Services from Independent Auditor**

Mike Peterson directed the Committee to the Board Decision Template in the materials concerning non-audit services from ERCOT's independent auditor, Ernst & Young. Mr. Petterson stated that the Committee was required to pre-approve engagement of independent auditors for non-audit services (e.g., financial statement audit and review services related to the 2009 IRS Form 990 ("Form 990")). He further explained that Ernst & Young had the expertise and ability to offer cost effective services relative to outside legal firms, and others less familiar with ERCOT. Mr. Petterson noted that ERCOT staff was seeking preapproval to engage Ernst & Young in non-audit tax advisory services related to the preparation of the 2009 IRS Form 990. He added that although the Form 990 was complex, ERCOT did not expect to use the full budget requested, but preferred to have it available in the event of need.

Mr. Crowder inquired about the due date for filing the Form 990. Mr. Petterson explained that a request for an extension until August 15, 2010 was granted. He added that Staff planned to bring the completed Form 990 back to the Committee and Board in July 2010 to ensure that the August 2010 deadline was met, but a second extension to October 15, 2010 was an option, albeit not guaranteed.

Mr. Gent asked how the Form 990 had changed from previous years. Mr. Petterson explained that it had only been slightly modified from 2008 to 2009, and the major change in complexity was from 2007 to 2008. Mr. Petterson added that he believed ERCOT filed the 2008 Form 990 on time, in complete compliance with the requirements, and noted that the objective was to do the same for the 2009 Form 990 filing. Mr. Karnei expressed that he thought it prudent to have another set of eyes review the Form 990 for ERCOT.

Mr. Karnei entertained a motion for approval of engaging Ernst & Young to perform non-audit services, as discussed in the Committee meeting.

**Miguel Espinosa moved to approve the Non-Audit Services from Independent Auditor related to the 2009 IRS Form 990. Mr. Gent seconded the motion. The motion passed unanimously with no abstentions.**

### **Review of Procedures for Handling Reporting Violations**

Mike Petterson referred to Committee materials concerning the annual Committee review of procedures for handling reporting violations. He began by reminding the Committee that the F&A Committee Charter states that this was an annual check to ensure the Committee had satisfied the requirement to establish procedures for the receipt, retention and treatment of complaints received by the company regarding accounting, internal accounting controls and auditing matters. Mr. Petterson added that ERCOT management established processes that allowed employees, contractors and other individuals to lodge complaints or issues concerning financial reporting practices.

Mr. Crowder asked about proactive inquiries opposed to the reaffirmation of ethics agreements each year. Messrs. Wullenjohn and Petterson provided examples of different means for gathering information. Mr. Petterson explained that there had been few, if any, reporting violations over the last couple of years.

Mr. Espinosa asked about tracking violations, and the presence of a repository for documenting violations. Mr. Petterson said the any violations that he was aware of would be tracked using a Management Action Plan ("MAP") with verification and confirmation that the MAP was implemented.

Following discussion on various types of reporting, Mr. Karnei summarized that Mr. Petterson would extract the Charter language relating to the Committee's responsibility under the Charter as it pertained to financial reporting items, for review and discussion at the June 2010 meeting .

### **Committee Briefs**

Mr. Crowder then inquired about the Risk Management Event Profile Matrix (i.e., the yellow designation for Nodal implementation). Phil DiPastena responded that the designation had been yellow for a while, and though things were going well, the designation had not been changed to yellow/green, but could be if the Committee and executive management so desired. Mr. Karnei asked Mr. DiPastena to give the Committee a brief explanation of the color designations. Mr. DiPastena explained that the Risk Management Committee had a meeting once a month with ERCOT's executive team to review the Matrix and discuss whether any of the risks contained therein should be rated differently.

Mr. Crowder inquired about the items on counterparty credit, and when the Committee could review risk factors associated therewith. Ms. Yager replied that they would be provided to the Committee once the model was developed (i.e., likely in the fall 2010).

Mr. Crowder asked Mr. Doggett about bulk system resources, to which Mr. Doggett stated that ERCOT had a change in the magnitude of peak demand downward, and several resources added on the positive side to balance out resources.

Mr. Crowder noted the importance of making clear to the Board that it had until the following Monday to fill out a questionnaire contained in the Board materials.

Ms. Yager informed the Committee that ERCOT Credit was working with Market Trials 5 to start incorporating credit constraints, and that those early stages would likely be bumpy, but that was to be expected as data and system issues were worked out.

### **Future Agenda Items**

The following items were identified as future agenda items:

1. Standing Internal Audit agenda items
2. Review operating plan and budget assumptions
3. Discussion of P-card limits and possibilities of increasing these limits for better throughput & efficiencies
4. Assessment of compliance, the internal control environment and system of internal controls
5. Reporting Violations – Summary of Charter Language
6. Revisit of debt issue
7. Financial Summary of TRE Status (accounting and financial statement impact)
8. Preparation for the 2011 Budget
9. Review information concerning Joint Board/IRC meeting
10. Review Market Credit Risk Model
11. Committee Briefs
12. Future Agenda Items

### **Other Business**

None.

### **Adjournment**

Mr. Karnei adjourned the meeting at approximately **9:54 a.m.**

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Juliana Morehead  
Associate Corporate Counsel

## 5. Approval of Debt Financing Proposal Clifton Karnei

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**<Vote>**



## 6. Review the Procedures for Handling Financial Reporting Violations Mike Petterson

***At the Finance and Audit Committee's May 18, 2010 meeting, Committee members expressed a desire to review the responsibilities established in the Committee charter relating to the monitoring of complaints.***

### **Excerpts from the Finance & Audit Committee Charter:**

#### **Purpose:**

7. Establish and maintain procedures for the receipt (including anonymous submission), retention and treatment of complaints regarding accounting, internal controls, and auditing;" *page 1*

#### **With respect to the Company's financial statements:**

5. Review with management and the independent auditor any correspondence with regulators or governmental agencies and any employee complaints or published reports that raise material issues regarding the Company's financial statements or accounting policies." *page 5*

#### **With respect to periodic reviews and reports:**

5. The Committee shall establish procedures for:
  - a. The receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters; and
  - b. The confidential, anonymous submission by the Company's employees of concerns regarding accounting or auditing matters." *page 6*



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

**Purpose**

The Finance and Audit Committee (the “Committee”) of the Board of Directors of ERCOT (the “Company”) shall:

1. Oversee the development of and adherence to a Company budget;
2. Provide recommendations to the Board of Directors for financing Company needs, including both debt and revenue financing;
3. Review and make recommendations to the Board of Directors regarding investment and financial guidelines for the Company;
4. Review and make recommendations to the Board of Directors regarding credit standards, procedures, governance, ERCOT Protocols and other market rules which impact credit risk;
5. Ensure that the Company’s financial statements are timely audited by qualified accountants who are independent;
6. Assist the Board of Directors in fulfilling its oversight responsibility with respect to the Company’s maintenance of an effective internal audit function;
7. Establish and maintain procedures for the receipt (including anonymous submission), retention and treatment of complaints regarding accounting, internal controls, and auditing;
8. Perform such other duties and responsibilities enumerated in and consistent with this Charter.

The Committee’s function is one of oversight, recognizing that the Company’s management is responsible for preparing the Company’s financial statements, and the independent auditor is responsible for auditing those statements. In adopting this Charter, the Board of Directors acknowledges that the Committee members are not employees of the Company (with the exception of ERCOT’s Chief Executive Officer) and are not providing any expert or special assurance as to the Company’s financial statements or any professional certification as to the external auditor’s work or auditing standards. Each member of the Committee shall be entitled to rely on the integrity of staff and external auditors to provide accurate, complete financial and other information to the Committee, absent actual knowledge to the contrary, and shall also exercise their fiduciary duties as Directors, including their duties of care, loyalty, and obedience.

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

The Committee shall provide assistance to the Board in fulfilling its oversight responsibility relating to the Company’s financial statements and the financial reporting process, the systems of internal accounting and financial controls, the annual independent audit of the Company’s

financial statements and the legal compliance and ethics programs as established by management and the Board. In so doing, it is the responsibility of the Committee to maintain free and open communication between the Committee and the Company's independent auditors, internal accounting personnel and management.

### **Membership**

The Committee shall be comprised of at least five Board members, at least three of which are from Market Segments and two or more of which must be Independent Board members of the Company. Each Member must be able to read and understand fundamental financial statements, including the balance sheet, income statement and cash flow statement. At least one Member shall be designated a "financial expert" as such term may be defined from time to time by the Board of Directors consistent with definitions generally accepted by the accounting industry or other regulatory authorities (the "Financial Expert"). At a minimum, the Financial Expert must have past employment experience in finance or accounting, requisite professional certification in accounting or any other comparable experience or background which ensures the individual's financial sophistication, including a past or current position as a Chief Executive Officer ("CEO"), Chief Financial Officer ("CFO") or other senior officer with financial oversight responsibilities.

The Board members shall decide from among themselves who shall participate in the Committee. The term shall be for not more than one year.

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

Any member of the public may attend and participate in the open session of Committee meetings. For the executive session of Committee meetings, the Committee shall close the Committee meeting to the public to address sensitive matters such as confidential personnel information, contracts, lawsuits, competitively sensitive information, or other information related to the security of the regional electrical network. For such executive sessions of Committee meetings, the Committee may request that any officers or employees of the Company, or any other person, whose advice and counsel are sought by the Committee, attend any meeting of the Committee to provide such pertinent information as the Committee requests. In addition, for such executive sessions of the Committee meetings, the Committee may exclude any persons who are not Directors, the Directors' Segment Alternates or the Directors' Designated Representatives.

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

### **Qualifications**

Each member of the Committee shall also meet any experience requirements as may be established from time to time by the Board of Directors. The Board of Directors shall endeavor to appoint at least one member to the Committee as the Financial Expert.

### **Authority**

In discharging its oversight role, the Committee is empowered to investigate any matter brought to its attention with full access to all books, records, facilities and personnel of the Company and the power to retain outside counsel or other experts for this purpose. All employees are directed to cooperate as requested by the Committee or any of its Members for Committee purposes. The Committee may request any officer or employee of the Company, the Company's outside counsel or the Company's independent auditor to attend a meeting of the Committee or to meet with any Member or any consultants to the Committee.

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

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

### **Structure**

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

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

### **Duties and Responsibilities**

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

#### ***With respect to budget oversight and financing:***

1. Annually, on a schedule to be established by the Board of Directors, the Committee shall review staff's proposed budget for the following year, including proposed staffing levels, proposed capital expenditures, and other proposed expenditures.

2. The Committee shall review the staff's recommendation of the amount and type of financing needed, both revenue and debt financing, to support the proposed budget, including the staff's proposed financial performance measures (e.g. ratios).
3. Following the Committee's review of the above items, the Committee shall recommend to the Board of Directors a staffing level, a proposed budget, proposed fees, and proposed financial performance measures for the following year.
4. As needed, the Committee shall review staff's recommendations among debt financing alternatives and recommend to the Board of Directors a debt structure or facility that meets the Company's liquidity needs.

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

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

***With respect to the Company's credit policies and standards:***

1. Establish a standard by which the Board will seek to maintain the long-term financial integrity of the ERCOT market and review this standard at least annually, recommending updates to the Board of Directors as needed.
2. The Committee shall review the Company's credit policies to consider:
  - a. Appropriateness of credit practices and creditworthiness standards established for market participants;
  - b. Compliance with existing creditworthiness standards by market participants;
  - c. Compliance with credit-related Protocols and market rules; and
  - d. Development of appropriate methods to evaluate and mitigate credit risk;
3. In establishing or reviewing the standard under Item 1 above and in conducting the review under Item 2 above the Committee shall consider the recommendations of staff and the Credit Work Group and the decisions and recommendations of the appropriate stakeholder groups, including the Technical Advisory Committee and the Market Credit Work Group.
4. Following each such review, the Committee may, in its discretion, recommend to the Board of Directors any proposed changes to the previously approved standard or credit policies.

***With respect to the independent auditors:***

1. Annually, the Committee shall recommend to the Board of Directors the selection and engagement of the Company's independent auditor. The Committee shall fulfill the oversight responsibility of the Board of Directors with respect to the independent auditors' audit of the books and accounts of the Company and for the fiscal year for which it is appointed.
2. The Committee shall approve the provision of all auditing and non-audit services (in excess of \$5,000) by the independent auditor to the Company in advance of the provision of those services and shall also approve the fees for all non-audit services provided by the independent auditor.
3. Provision of non-audit services of less than or equal to \$5,000 by the independent auditor to the Company do not require pre-approval from the Committee, but shall be communicated in writing to the members of the Committee at the first meeting following the engagement for the non-audit services at issue.

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

***With respect to the Company's financial statements:***

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

***With respect to periodic reviews and reports:***

1. Periodically, the committee shall meet separately with senior management, the Chief Audit Executive and the independent auditors.

2. The Committee shall review with the independent auditor any audit problems or difficulties and management's response to them.
3. The Committee shall review the Company's policies with respect to risk assessment and risk management.
4. The Committee shall inquire of management and the independent auditors about significant risks or exposures to the Company and the Company's market and assess the steps management has taken to minimize such risks.
5. The Committee shall establish procedures for:
  - a. The receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters; and
  - b. The confidential, anonymous submission by the Company's employees of concerns regarding accounting or auditing matters.
6. The Committee shall review a summary of the Company's dealings with any financial institutions that are also market participants.
7. The Committee shall communicate to the Board of Directors the matters discussed at each meeting of the Committee, including any issues with respect to the quality or integrity of the Company's financial statements, the performance and independence of the Company's independent auditors or the performance of the internal audit function.
8. The Committee shall review and assess the adequacy of this Charter annually and recommend any proposed changes to the Board of Directors.

***With respect to Internal Audit:***

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

**Meetings**

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

### **Minutes**

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

### **Evaluation**

The Committee shall undertake an annual evaluation assessing its performance and, in light of this, consider changes in its membership, charter or procedures. The Committee shall report to the Board the results of its evaluation, including recommended charter, membership and other changes, if any.



## 7. Preparation for 2011 Budget Mike Petterson

- **2011 budget preparation process has been initiated**
- **Transition to a nodal market has significant budgetary impact including topics such as the following:**
  - Staffing and organizational assessment
  - Market and technology stabilization
  - Technology support and maintenance
- **Efficiency of service and cost control remain focus areas**
- **Options for maintaining the existing level of fees are being developed and evaluated.**
  - All else equal, maintaining the existing System Administration Fee may require up to a \$55-\$65 million reduction in revenue requirements (costs)
- **Complexity of issues will extend the budget preparation, review, and approval process; however, Board members will be provided regular opportunity to evaluate and contribute to preparation of ERCOT's 2011 budget.**

## 7. Preparation for 2011 Budget Mike Petterson

Action	New Date	Previous Date
<b>Finance and Audit Committee Meeting</b> Discuss and Review the 2011 Budget/PPL Status and Budget Assumptions  <b>Board of Directors Meeting</b> Discuss and Review with the Board the 2011 Budget/PPL Status and Budget Assumptions (Briefing and Request for Public Comment)	<b>August 17, 2010</b>	<b>June 15, 2010</b>
<b>Finance and Audit Committee Meeting</b> Prepare and Present the 2011 Preliminary Budget/PPL (Courtesy Copy to all Board Members)	<b>September 21, 2010</b>	<b>July 20, 2010</b>
<b>Finance and Audit Committee Special Meeting and Public Input Meeting</b> Discuss and Review the 2011 Budget and PPL (Courtesy Copy to all Board Members)	<b>October 18, 2010</b>	<b>August 16, 2010</b>
<b>Finance and Audit Committee Meeting</b> Obtain 2011 Budget Recommendation <b>Board of Directors Meeting</b> Seek Board Approval of the 2011 Budget and PPL -Vote	<b>November 16, 2010</b>	<b>September 21, 2010</b>

## 8. Texas Regional Entity Financial Summary: Overview of Divestiture Mike Petterson

- **Effective July 1, 2010, a newly formed company, Texas Reliability Entity, Inc., will assume the business, rights, and obligations of Texas Regional Entity (TRE), an independent division of ERCOT.**
- **As of this date, ERCOT will transfer substantially all assets, liabilities, and retained earnings of TRE to the new Texas Reliability Entity. Based on current knowledge, ERCOT expects no losses due to this transfer.**
- **All TRE employees will cease employment with ERCOT and will be employed by the new Texas Reliability Entity.**

## 8. Texas Regional Entity Financial Summary: Divestiture Planning

Mike Petterson

- ERCOT and TRE assembled a cross-functional divestiture management team. This team was led by Steve Grendel, Director of Facilities, and included representation by Legal, Procurement, Human Resources, Accounting, IT, and Facilities.
- ERCOT staff researched various accounting literature to gain an understanding of best divestiture practices.
- Starting 2009, the accounting group began tracking TRE transactions through a distinct and separate general ledger to enable a clean and accurate separation.
- In 2009, Ernst & Young performed a separate audit of the TRE financial statements, resulting in a clean opinion.
- The TRE financial statements for the six month period ended June 30, 2010 will receive a stand alone audit from Ernst & Young.

## 8. Texas Regional Entity Financial Summary: Financial Statement Impact

- **The transfer of TRE assets, liabilities, and retained earnings will have a minimal impact on ERCOT's Statement of Financial Position**
  - 0.7% reduction of assets (includes transfer of cash, accounts receivable, and property and equipment)
  - 0.6% reduction of liabilities (includes transfer of payables, accrued liabilities, deferred revenue, and regulatory liability)
  - 0.1% reduction of retained earnings
- **As TRE is designed to be a cost-recovery entity, the divestiture will have a negligible impact on ERCOT's Statement of Activities and Net Assets.**

**Divestiture plan for separation as of July 1<sup>st</sup> will result in:**

**Support Recovery**

- Elimination of TRE support services in Human Resources, Accounting, Procurement, Facilities, Security and Information Technology
- Net projected unfavorable service recovery variance of \$0.4M

**Protocol Services**

- Contract negotiations between ERCOT, PUCT and Texas Reliability Entity, Inc. are underway
- Net projected favorable savings of \$0.5M (assuming no significant increase in service cost for remainder of year)

**Net projected favorable impact of divestiture = \$0.1M**

# 9. Parent Guarantees for Financial Institutions

Clayton Greer

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**Informative**

**Q&A only**



## ERCOT Market Credit Status

as of 4/30/2010

as of 5/31/2010

### 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	
Ratings over BBB-	10	58,805,903	16%	149,136,588	U
<u>QSEs that do not meet ERCOT Creditworthiness Standards</u>					
Ratings below BBB- or not rated					
Cash & Letters of Credit	52	169,348,926	46%	321,306,822	S
Guarantee Agreements	17	143,971,388	39%	427,137,410	S
<b>Total Exposure</b>	<b>79</b>	<b>372,126,217</b>	<b>100%</b>		

	# of QSEs*	Estimated Aggregate Liability (\$)	% of EAL	Total Unsec Credit Limit / Security Posted	
Ratings over BBB-	11	44,254,424	14%	175,177,081	U
<u>QSEs that do not meet ERCOT Creditworthiness Standards</u>					
Ratings below BBB- or not rated					
Cash & Letters of Credit	50	180,204,038	56%	332,703,620	S
Guarantee Agreements	19	100,129,679	31%	441,387,399	S
<b>Total Exposure</b>	<b>80</b>	<b>324,588,141</b>	<b>100%</b>		

### 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

**Total**

**165**

**166**

U: For QSEs that meet ERCOT's Creditworthiness Standards, amount of unsecured credit granted.

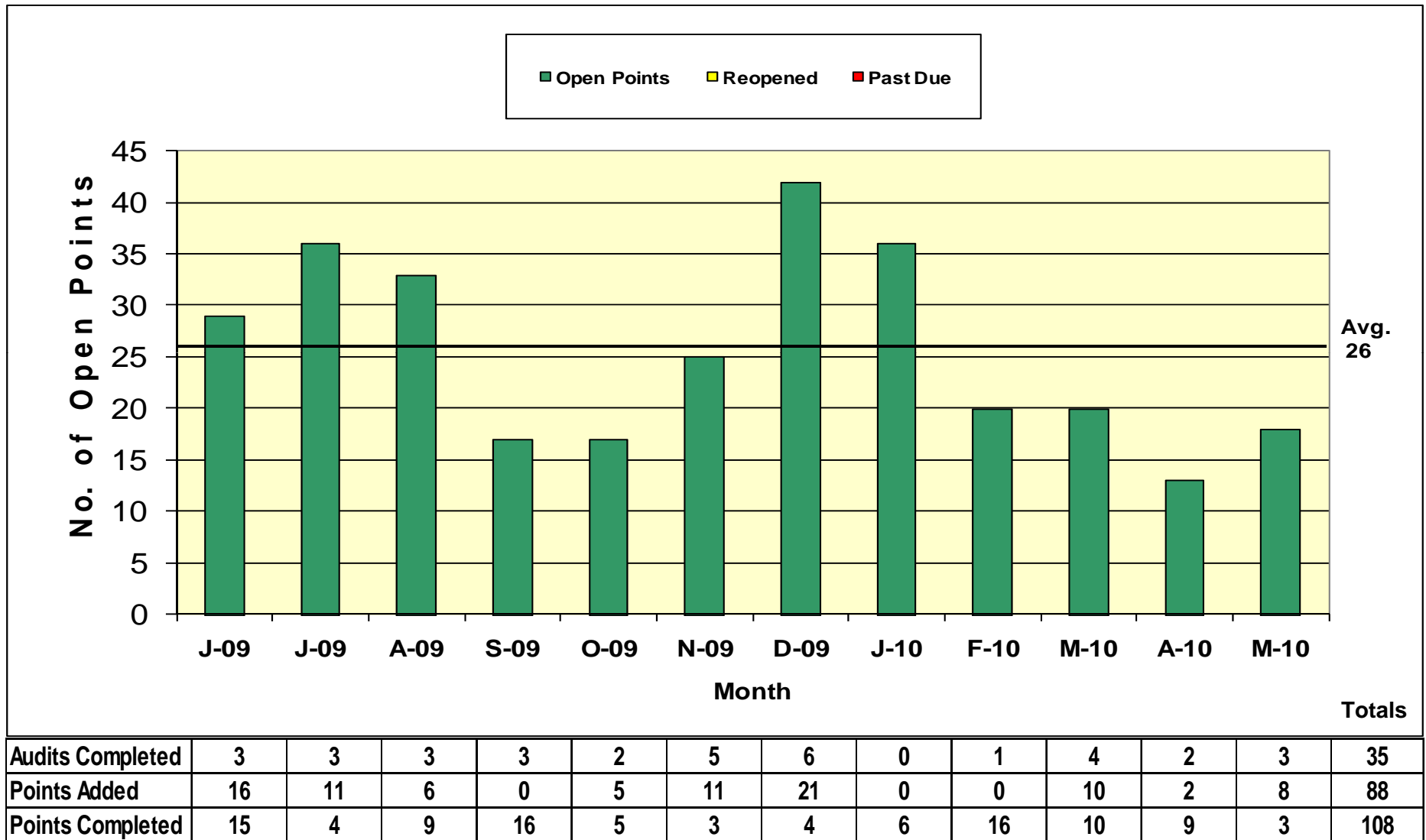
S: For QSEs that do not meet ERCOT's Creditworthiness Standards, amount of Security posted.

Note 1: Guarantee Agreements provided to meet a QSE's collateral requirements by entities that meet ERCOT's Creditworthiness Standards.

Guarantee Agreements provided to meet financial statement requirements by entities that do not meet ERCOT's Creditworthiness Standards are not included on this schedule.

# 10. Committee Brief: ICMP – Status of Open Audit Points

Cheryl Moseley



All audit points except 2 are expected to be complete by 12/31/10.

## 10. Committee Brief: ICMP – Audits Cheryl Moseley

### **Audits Completed**

(last 3 months)

#### **Internal Audits**

- Taylor Data Center (Special Request)
- Bastrop Data Center & Control Center (Special Request)
- Oracle Software License Compliance (Special Request)
- 2010 Nodal Budget-to-Actual Mgmt. (Special Request – Follow-up)
- Renewable Energy Credits System – IT & Program Admin.
- Procurement Card

#### **External Audits**

- 2009 Financial Audit (Ernst & Young, LLP)

### **Open Audits**

#### **Internal Audits**

- Protocol 1.4 Required Audit – Confidentiality
- Q1 2010 Fraud Auditing
- Protocol 1.4 Required Audit – Independence Verification
- Payroll
- Nodal Program Spending (Part 1 of 2)
- Vendor Assessments (Targeted Review)
- Patch Management and Server Hardening
- Cash and Investments

#### **External Audits**

- 2010 Zonal SAS70 Audit (SAS70 Solutions, Inc.)

### **Planned Audits**

(next 3 months)

#### **Internal Audits**

- Q2 2010 Fraud Auditing
- Pre-Audit Testing for 2011 Nodal SAS70 Audit
- Credit Risk Model

#### **External Audits**

- 2010 Benefit Plan Audit (Auditor – TBD)

## 10. Committee Brief: ICMP – Security Assessments Cheryl Moseley

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### **Consultation/Analysis Reports Completed**

(last 3 months)

#### **External Assessments**

- Assessment of Nodal Systems

### **Open Consultation/ Analysis Reviews**

#### **Assessments**

- 1 Security Assessment (Internal)

### **Planned Consultation/ Analysis Reviews**

(next 3 months)

#### **Assessments**

**ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.**  
**RISK MANAGEMENT EVENT PROFILE MATRIX (as of June 1, 2010)**

Strategic	Operational Excellence	Market Facilitation	Grid Reliability	Reporting	Legal and Regulatory Compliance
<b>Strategy Development</b> Corporate objective setting adequately incorporates informed stakeholder input, market realities and management expertise.	<b>Performance Monitoring</b> Clearly defined and actively monitored performance metrics linked to mission and goals - Performance status communicated and corrective action taken.	<b>Customer Choice</b> Market design promotes efficient choice by customers of energy providers with effective mechanisms to change incumbent market participants as desired.	<b>Grid Operations</b> Information required to operate the grid is efficiently gathered. Appropriate tools are prudently configured to efficiently operate the system.	<b>Review Practices</b> Prudent measures are taken to insure that company disclosures are properly vetted and not misleading.	<b>Legal &amp; Legislative</b> Operations are conducted in compliance with all laws and regulations. Impacts of current and proposed legislation are understood and communicated.
<b>Mission and Goals</b> Corporate objectives and performance standards are understood and followed.  Market Reform organizational assessment completed. Study will be used as one of the inputs into developing the 2011 budget.	<b>Business Practices</b> Business planning, processes and management standards are effective and efficient.	<b>Nodal Implementation Project</b> Nodal Implementation on budget on schedule, and within defined scope.  Full market trials functionality testing continues. 2-hr LFC test successfully completed in May; 8-hr LFC test is on target for mid-June. Reporting support for DAM/RUC/SASM continues to be upgraded. ERCOT provided initial overview of system cut-over timeline to market participants in early June, with additional details scheduled for release in July.	<b>Planning</b> Long-range planning methods enable efficient responses to system changes that are necessary to maintain reliability standards.  Demand for planning studies exceeds ERCOT's ability to perform them. ERCOT has received two awards totaling \$3.5 million to produce long-term resource and transmission planning studies in 2011. Hiring resources to work on these studies has commenced.	<b>Disclosure</b> Reporting and other disclosures to intended parties is timely, accurate and effective.	<b>Internal Control Compliance</b> Internal Control Compliance processes and management standards are effective, efficient, and provide stakeholders with required assurances of quality.  Efforts underway to streamline and increase the effectiveness of ERCOT's internal controls program and integrate it with the company's Enterprise Risk Management program.
<b>Reputation</b> Positive perceptions by stakeholders lead to less cost and greater flexibility resulting in enhanced enterprise value.  ERCOT addressing reputation issues by 1) refocusing communication efforts, 2) continuing to complete Nodal on time and on budget, 3) preparing a well thought out budget for 2011, and 4) increasing accountability.	<b>Workforce</b> Organization design, managerial and technical skills, bench strength and reward systems aligned with corporate goals.  Market Reform's organizational study has identified a number of areas for improvement as ERCOT moves beyond nodal.	<b>Counterparty Credit</b> Maintain credit risk exposure for overall market within acceptable limits.  Credit risk reflected by the PFE model has been fairly consistent over the past year. Color remains yellow pending the review of risk factors (e.g. counterparty probabilities of default, impact of new markets and instruments, collateral levels, price volatility) in the Nodal market requested by F&A.	<b>Bulk System Resources</b> Market Participants construct and make available adequate bulk electric grid resources.  The May update of the Capacity, Demand and Reserve (CDR) report is forecasting reserve margins for the entire 5 year time horizon to be above the 12.5% target.	<b>Communication</b> Internal & external communications are timely and effective.	<b>Industry Standards</b> Business and operational activities are in compliance with all applicable regulatory, financial and accounting requirements, standards and directives.  Received 2009 NERC audit report for the Operations and Planning (693) portion of the standards. Still waiting for the final 2009 NERC audit report for the Critical Infrastructure Protection (CIP) portion. TRE delivered its final 2010 Protocol and Operating Guide report revealing ERCOT's 100% compliance with those requirements audited.
<b>Fiscal Management</b> ISO design requires competent, prudent and cost effective provision of services.  ERCOT is currently forecasting a year-end positive budget variance of between \$7.0 and \$7.5 million.	<b>Technology Infrastructure</b> Information systems, supporting facilities and data are effectively managed and are reliable.  Systems remain stable. Sufficient system and computer room capacity exist for Nodal 'go-live'. Austin data center capacity is near maximum and may not be able to accommodate additional unforeseen expansion prior to switchover to Bastrop. Capacity requirements continue to be closely monitored.	<b>Administration, Settlement &amp; Billing</b> Market rules fairly applied to all participants. Accounting is timely and accurately reflects electricity production and delivery.	<b>Operational Responsibility</b> Market participant conduct their operations in a manner which facilitates consistent grid reliability.  There is still a lack of consensus over reactive power and frequency response requirements to existing wind generation resources. However, RTWG is planning to bring a draft of the Texas Renewables Integration Plan (TRIP) to TAC by mid-Summer.	<b>Adequacy and Integrity</b> Robust processes exist to support management assertions embodied within financial reports.	<b>Regulatory Filings</b> Evidence, testimony and other supporting materials are compelling and successful.

Legend: Elevated Risk Level

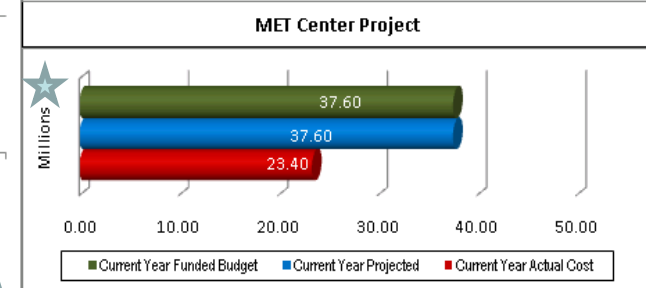
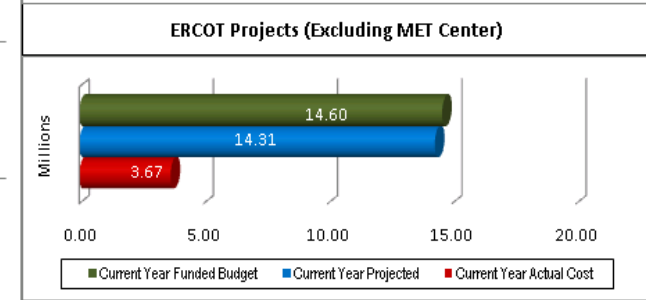
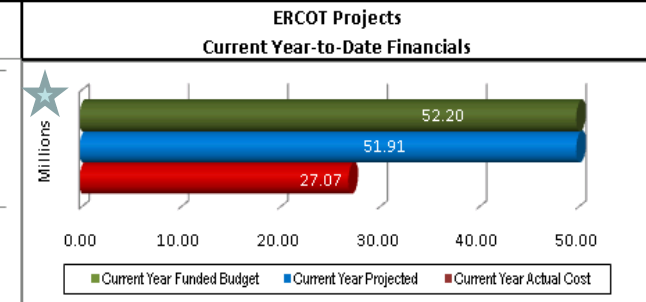
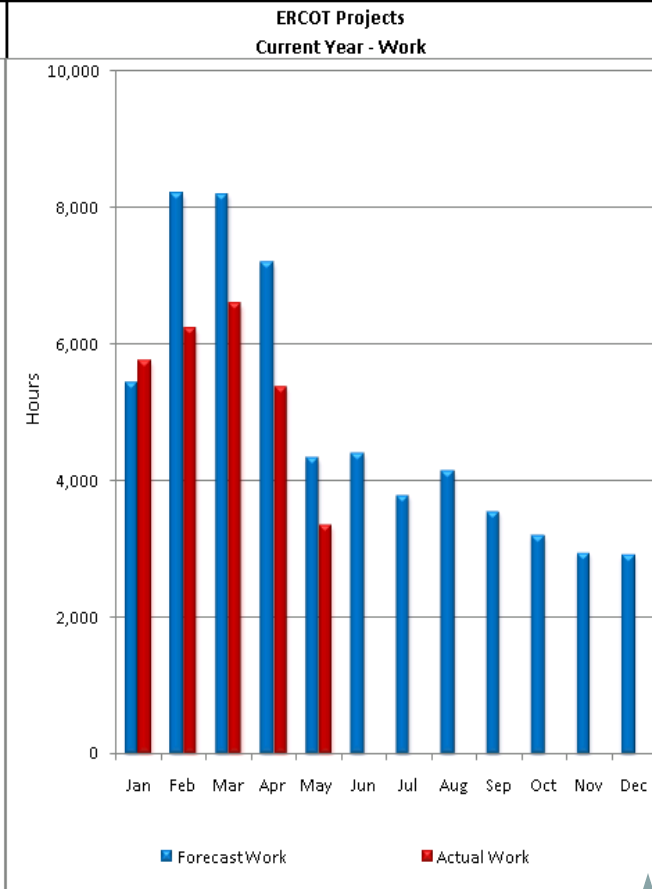
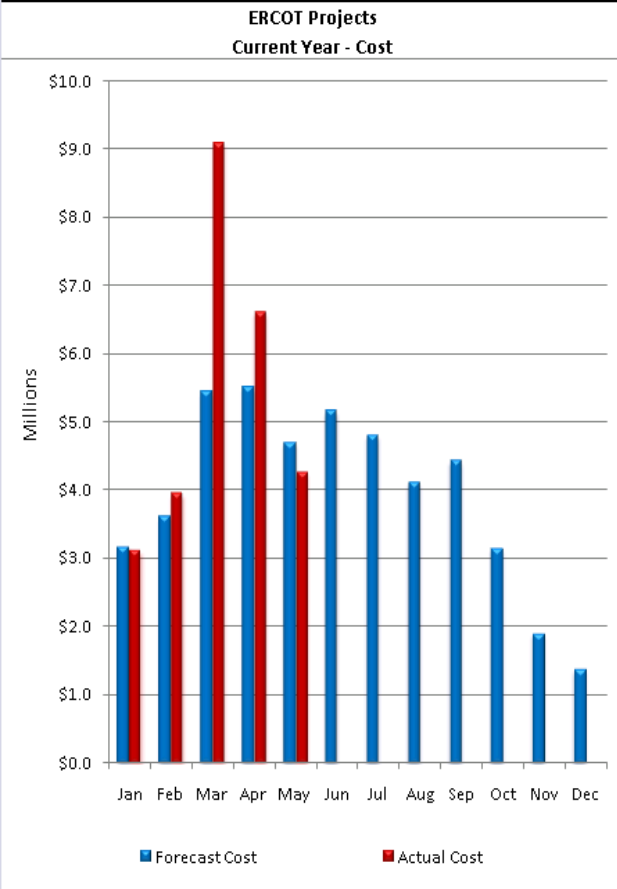
Reduced Risk Level

(New Risk Categories / Descriptions Indicated in Green)

# 10. Committee Brief: PMO David Troxtell

## ERCOT Enterprise Projects Summary Report

ERCOT		Overall Projects Report					Reporting Period: 5/31/2010	
Projects in Ercot's Portfolio							Portfolio Performance	
Deferred	Concept	On Hold	Initiation	Planning	Execution	Closing	Schedule	Budget
0	1	1	4	6	13	3	Green	Green
			Closed	Total Active		27		
			Cancelled	Projects Not Started		0	Current Year Funded Budget: \$52,200,000	



Includes \$5.9M carry-over funds from 2009 for MET Center.  
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**ERCOT**  
**Summary of Investments**  
**May 31, 2010**

<u>Investment Account</u>	<u>Chase</u>	<u>Federated 068</u>	<u>Federated 0125</u>	<u>Evergreen 497</u>	<u>Invesco</u>	<u>BlackRock</u>	<u>Subtotal</u>
	<i>Treasury and Repo</i>	<i>Treasury and Repo</i>	<i>Treasury only</i>	<i>Treasury and Repo</i>	<i>Treasury and Repo</i>	<i>Treasury and Repo</i>	
Operating	\$ 6,895	\$ 5	\$ -	\$ -	\$ -	\$ -	\$ <b>6,900</b>
TRE	2,054	1,267	-	-	-	-	\$ <b>3,321</b>
Market	489	19	15	6	15	5	\$ <b>548</b>
Deposit/Restricted	35,212	23,613	11,001	32,310	31,009	30,540	\$ <b>163,685</b>
<b>Total</b>	<b><u>\$ 44,650</u></b>	<b><u>\$ 24,904</u></b>	<b><u>\$ 11,016</u></b>	<b><u>\$ 32,316</u></b>	<b><u>\$ 31,024</u></b>	<b><u>\$ 30,545</u></b>	<b><u>\$ 174,455</u></b>
% Investments:	26%	14%	6%	19%	18%	18%	100%
Other cash net of outstanding checks							<b><u>\$ (1,646)</u></b>
Total cash and cash equivalents							<b><u>\$ 172,809</u></b>

- **Internal Audit recently completed audit of ERCOT's procurement card program.**
- **Internal Audit concluded the procurement card program -**
  - continues to grow in usage, compliance, and efficiency
  - would benefit from several minor improvements
  - may be more efficient and potentially gain wider acceptance if transactional spending limits were increased
- **After addressing minor improvement recommendations made by Internal Audit staff, Procurement intends to raise the current spending limit from \$1,000 per transaction to \$5,000 per transaction.**
  - The planned increase in transaction dollar limits will allow a greater number of items to be procured through more efficient processes with only slight increase in organizational financial risk.



## **Future Agenda Items – July 2010**

- **Standing Internal Audit agenda items**
- **Discussion of IRS form 990 filing**
- **Update on annual operating budget**
- **Credit briefing – Potential Future Risk (YE 2009)**
- **Review of investment strategy**
- **Committee briefs**
- **Future agenda items**

# 11. Future Agenda Items: F&A 2010 Yearly Schedule

## Mike Petterson

### Quarter 1

- √ •Elect officers and confirm financial qualifications
- √ •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 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
- √•Review the Market Credit Risk Corporate Standard

### Quarter 3

- Appoint the independent auditors for upcoming year
- Approval of independent auditor fees for upcoming year
- Review of committee charter
- 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

### 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 Corporate Standards
- 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 the Company's dealings with any financial institutions that are also market participants
- Review scope of annual financial audit
- Review of external auditor quality control procedures and independence

### 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

# 12. Other Business

## Mike Petterson

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