



ERCOT Finance & Audit Committee Meeting
7620 Metro Center Drive, Austin, Texas
Met Center, Conference Room 206
March 21, 2011; 12:00pm – 3:00pm*

Item #	Agenda Item Type	Description/Purpose/Action Required	Presenter	Time
1.		1a. Call to order Executive Session	C. Karnei	12:00pm
		1b. Announce proxies	C. Karnei	12:00pm
	Vote	1c. Approve executive session minutes (2/14/11)	C. Karnei	12:01pm
2.	Discussion	2a. Internal Audit status report	B. Wullenjohn	12:02pm
	Discussion	2b. Discussion of Internal Audit goals for 2011	B. Wullenjohn	12:05pm
	Discussion	2c. Review Internal Audit Department Charter	B. Wullenjohn	12:15pm
	Discussion	2d. EthicsPoint update	B. Wullenjohn	12:20pm
	Discussion	2e. Chief Audit Executive Compensation	T. Doggett	12:30pm
3.	Discussion	Personnel, Contract, Security, Compliance and Risk Management Matters	C. Karnei	12:40pm
		Recess Executive Session		
		Convene General Session		
4.	Vote	Approve general session minutes (2/14/11)	C. Karnei	1:05pm
5.	Vote	Committee approval of Internal Audit Department Charter	C. Karnei	1:06pm
6.	Vote	Review and recommend Board approval of the Finance and Audit Committee Charter	C. Karnei	1:10pm
7.	Vote	Review and recommend Board acceptance of SAS 70 Type I Audit Report	C. Moseley	1:15pm
8.	Vote	Annual review and recommendation of Board approval of (a) Investment Corporate Standard (b) Financial Corporate Standard	C. Yager / L. Swanson	1:25pm
9.	Vote	Annual review and recommendation of Board approval of Market Credit Risk Corporate Standard	C. Yager	1:35pm
10.	Vote	Committee approval of Credit Work Group Charter	T. Nikazm	1:50pm
11.	Discussion	Discuss Credit management practices and judgments (a) Specifically relating to the events of 02/02/2011 (b) Generally	C. Yager / M. Ruane	2:00pm
12.	Discussion	Periodic review of liquidity report	C. Yager	2:25pm
13.	Discussion	Review Committee briefs	M. Petterson	2:35pm
14.	Discussion	Future agenda items	M. Petterson	2:55pm
15.		Other business	M. Petterson	2:58pm
		Adjourn meeting	C. Karnei	3:00pm

** 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 Monday, April 18, 2011, at ERCOT, 7620 Metro Center Drive, Austin, Texas 78744, in Room 206.*

4. Approval of General Session Minutes Clifton Karnei

Approval of General Session Minutes

- Vote 2/14/11



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

Electric Reliability Council of Texas Inc.
7620 Metro Center Drive (Room 206) - Austin, Texas 78744
February 14, 2011

Pursuant to notice duly given and after determination by the Committee Chairman that a quorum was present, the meeting of the Finance and Audit Committee (Committee) of the Board of Directors (Board) of Electric Reliability Council of Texas, Inc. (ERCOT) convened on the above-referenced date. After meeting earlier in Executive Session, the Committee then met in General Session.

General Session Attendance

Committee Members:

Bermudez, Jorge (Vice Chair)	Unaffiliated Director	Unaffiliated Director
Crowder, Calvin	American Electric Power Service Corporation	Investor Owned Utility
Dreyfus, Mark	Austin Energy	Municipal
Espinosa, Miguel	Unaffiliated Director	Unaffiliated Director
Karnei, Clifton (Chair)	Brazos Electric Power Cooperative	Cooperative
Zlotnik, Marcie	StarTex Power	Independent Retail Electric Provider

Other Board Members and Segment Alternates:

Brown, Jeff	Shell Energy North America	Segment Alternate - Independent Power Marketer
Dalton, Andrew	Valero Services Inc.	Consumer/Industrial
Doggett, Trip	ERCOT	President and Chief Executive Officer (CEO)
Doll, Laura	Unaffiliated Director	Unaffiliated Director, Board Chairman
Gent, Michehl	Unaffiliated Director	Unaffiliated Director, Board Vice Chairman
Givens, Sheri	Office of Public Utility Counsel (OPUC)	Consumer/Residential
Hendrick, Eric	Stream Energy	Segment Alternate - Independent Retail Electric Provider
Nelson, Donna	Public Utility Commission of Texas (PUCT)	Commissioner (Alternate Representative for Barry T.



		Smitherman, Chairman)
Patton, A.D.	Unaffiliated Director	Unaffiliated Director
Prochazka, Scott	CenterPoint Houston Electric	Segment Alternate - Investor Owned Utility
Ryall, Jean	Constellation Energy	Independent Power Marketer

ERCOT Staff and Guests:

Cobos, Lori	ERCOT Associate Corporate Counsel
Cleary, Mike	ERCOT Senior Vice President and Chief Operations Officer
Leady, Vickie	ERCOT Assistant General Counsel and Assistant Corporate Secretary
Magness, Bill	ERCOT Vice President, General Counsel and Corporate Secretary
Manning, Chuck	ERCOT Vice President and Chief Compliance Officer
Morgan, Richard	ERCOT Vice President and Chief Information Officer
Nikazm, Tamila	Austin Energy – Credit Work Group Vice Chair
Petterson, Mike	ERCOT Vice President of Finance and Treasury
Saathoff, Kent	ERCOT Vice President of Grid Operations and System Planning
Wullenjohn, Bill	ERCOT Director of Internal Audit
Yager, Cheryl	ERCOT Treasurer

Chairman Karnei convened the General Session of the Committee meeting at approximately 4:27 p.m. and addressed the following Agenda Items in the order below.

Approval of General Session Minutes – January 17, 2011 (Agenda Item 4)

Chairman Karnei entertained a motion to approve the January 17, 2011 Finance and Audit (F&A) Committee General Session Meeting Minutes (Minutes). Miguel Espinosa requested the following revisions to the Minutes:

- Agenda Item 7 (Review and Assess Adequacy of Committee Charter) – add to the end of the last sentence “in accordance with the Committee Charter”.
- Agenda Item 10 (Results of F&A Committee Self Assessment) – strike last sentence – “Mr. Gent requested a focus on increased training in 2011.”

Miguel Espinosa moved to approve the Minutes with his requested revisions. Marcie Zlotnik seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Review and Recommend Board Approval of the F&A Committee Charter (Agenda Item 5)

Chairman Karnei deferred the consideration of the F&A Committee Charter to the March 2011 Committee meeting.



Review and Recommend Board Approval of Investment and Financial Corporate Standards (Agenda Items 7a and 7b)

Chairman Karnei deferred the consideration of the Investment and Financial Corporate Standards to the March 2011 Committee meeting.

Confirm Credit Work Group (CWG) Chair and Vice-Chair (Agenda Item 6)

Chairman Karnei entertained a motion to confirm Arleen Spangler, with NRG Energy, Inc., as the 2011 CWG Chair and Tamila Nikazm, with Austin Energy, as 2011 CWG Vice-Chair.

Calvin Crowder moved to approve Ms. Spangler as CWG Chair and Ms. Nikazm as CWG Vice-Chair. Miguel Espinosa seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Review Quarterly Investment Report (Agenda Item 8)

Chairman Karnei solicited questions on the Quarterly Investment Report from the Committee members, but there were none.

Review Committee Briefs (Agenda Item 9)

Chairman Karnei solicited questions on the Committee Briefs from the Committee members, but there were none.

Future Agenda Items (Agenda Item 10)

In response to Chairman Karnei's inquiry, Mike Petterson, ERCOT Vice President of Finance and Treasury, noted that the items deferred from this Committee meeting would be added to the March 2011 Committee meeting agenda.

Other Business (Agenda Item 11)

There was no other business considered at this time.

Adjournment

Chairman Karnei adjourned the meeting at approximately 4:39 p.m.

Committee materials and presentations from the meeting are available on ERCOT's website at: http://www.ercot.com/committees/board/finance_audit/

Lori Cobos
Associate Corporate Counsel

5. Committee Approval of Internal Audit Department Charter <Vote> Clifton Karnei

Annual Approval of the Internal Audit Department Charter (Proposed Charter attached as a separate document)

- **Vote**



Internal Audit Department Charter

MISSION AND SCOPE OF WORK

The mission of the Internal Audit Department is to provide independent, objective assurance and consulting services designed to add value and improve the organization's operations. It helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

The scope of work of the Internal Audit Department is to determine whether the organization's network of risk management, control, and governance processes, as designed and represented by management, is adequate and functioning in a manner to ensure:

- Risks are appropriately identified and managed.
- The systems of internal control established to ensure compliance with ERCOT's policies, plans and procedures, laws, and regulations are adequate and functioning as intended.
- Interaction with the various governance groups occurs as needed.
- Significant financial, managerial, and operating information is accurate, reliable, and timely.
- Employee's actions are in compliance with policies, standards, procedures, and applicable laws and regulations.
- Resources are acquired economically, used efficiently, and adequately protected.
- Programs, plans, and objectives are achieved.
- Quality and continuous improvement are fostered in the organization's control process.
- Significant legislative or regulatory issues impacting the organization are recognized and addressed properly.

Opportunities for improving management control, economy, and the organization's image may be identified during audits. They will be communicated to the appropriate level of management.

ACCOUNTABILITY

The Director of Internal Audit is the Chief Audit Executive at ERCOT. The Chief Audit Executive (CAE), in the discharge of his/her duties, shall be accountable to management and the Finance and Audit Committee of the Board of Directors to:

- Provide annually an assessment on the adequacy and effectiveness of the organization's processes for controlling its activities and managing its risks in the areas set forth under the mission and scope of work.
- Report significant issues related to the processes for controlling the activities of the organization and its affiliates, including potential improvements to those processes, and provide information concerning such issues through resolution.
- Provide information periodically on the status and results of the annual audit plan and the sufficiency of department resources.
- Coordinate with and provide oversight of other control and monitoring functions (risk management, compliance, security, legal, ethics, environmental, external audit).

INDEPENDENCE

To provide for the independence of the Internal Audit Department, its personnel report to the CAE, who reports administratively to the Chief Executive Officer and functionally to the Finance and Audit Committee of the Board of Directors in a manner outlined in the above section on Accountability. The Internal Audit Department will include as part of its reports to the Finance and Audit Committee, a regular report on internal audit personnel.

RESPONSIBILITY

The CAE and staff of the Internal Audit Department have responsibility to:

- Develop a flexible annual audit plan using appropriate risk-based methodology, including any risks or control concerns identified by management, and submit that plan to the Finance and Audit Committee for review and approval.
- Implement the annual audit plan, as approved, including, and as appropriate, any special tasks or projects requested by management and the Finance and Audit Committee.
- Maintain a professional audit staff with sufficient knowledge, skills, experience, and professional certifications to meet the requirements of this Charter.
- Establish a quality assurance program by which the CAE assures the operation of internal auditing activities.
- Perform consulting services, beyond Internal Audit's assurance services, to assist management in meeting its objectives. Examples may include facilitation, process design, training, and advisory services. When performing these consulting services, the Internal Audit Department will maintain and monitor its independence and objectivity.
- Evaluate and assess significant merging/consolidating functions and new or changing services, processes, operations, and control processes coincident with their development, implementation, and/or expansion.
- Issue periodic reports to the Finance and Audit Committee and management summarizing results of audit activities.
- Keep the Finance and Audit Committee informed of emerging trends and successful practices in internal auditing.

- Provide a list of significant measurement goals and results to the Finance and Audit Committee.
- Assist in the investigation of significant suspected fraudulent activities within the organization and notify management and the Finance and Audit Committee of the results.
- Consider the scope of work of the external auditors and regulators, as appropriate, for the purpose of providing optimal audit coverage to the organization at a reasonable overall cost.

AUTHORITY

The CAE and staff of the Internal Audit Department are authorized to:

- Have unrestricted access to all functions, records, property, and personnel.
- Have full and free access to the Finance and Audit Committee.
- Allocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish audit objectives.
- Obtain the necessary assistance of personnel in units of the organization where they perform audits, as well as other specialized services from within or outside the organization.
- Provide assurance services to external parties (e.g., the PUCT per Protocol 1.4.3.1.(2)).

The CAE and staff of the Internal Audit Department are not authorized to:

- Perform any operational duties for the organization or its affiliates.
- Initiate or approve accounting transactions external to the Internal Audit Department.
- Direct the activities of any organization employee not employed by the Internal Audit Department, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.
- Implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that would normally be audited.

STANDARDS OF AUDIT PRACTICE

The Internal Audit Department will govern itself by adherence to the Institute of Internal Auditors' mandatory guidance including the definition of Internal Auditing, the Code of Ethics, and the *International Standards for the Professional Practice of Internal Auditing*. This mandatory guidance constitutes statements of the fundamental requirements for the professional practice of internal auditing and for evaluating the effectiveness of the Internal Audit Department's performance and constitute an addendum to this charter.

The Institute of Internal Auditors' Practice Advisories, Practice Guides, and Position Papers will also be adhered to as applicable to guide operations. In addition, the Internal Audit Department will adhere to ERCOT's policies and procedures and Internal Audit's procedures guide.

PERIODIC ASSESSMENT

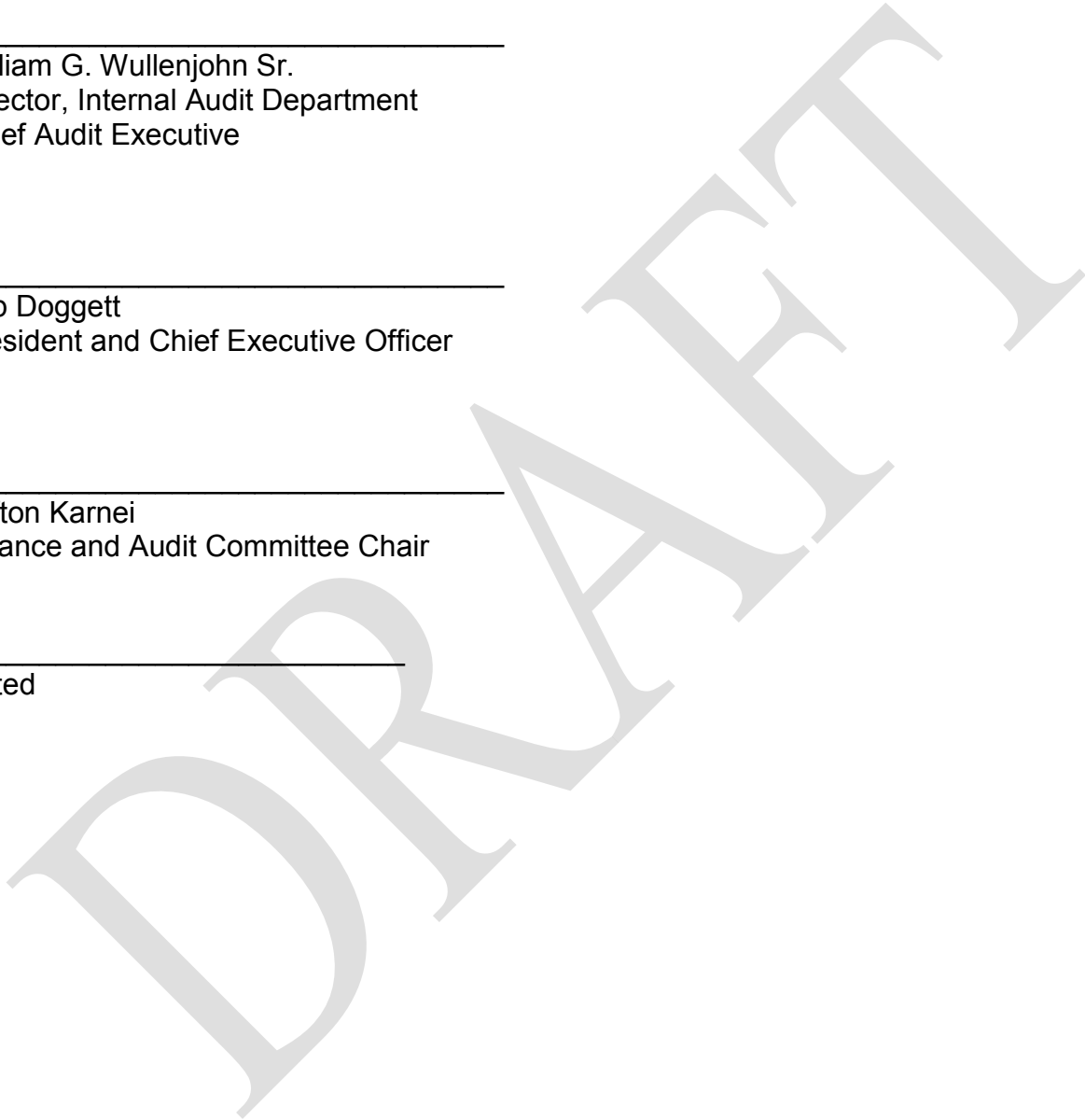
The Chief Audit Executive should at least annually assess whether the mission, responsibility, and authority, as defined in this charter, continue to be adequate to enable the Internal Audit Department to accomplish its objectives. The result of this annual assessment should be communicated to senior management and the Finance and Audit Committee.

William G. Wullenjohn Sr.
Director, Internal Audit Department
Chief Audit Executive

Trip Doggett
President and Chief Executive Officer

Clifton Karnei
Finance and Audit Committee Chair

Dated



6. Review and Recommend Board Approval of the Finance and Audit Committee Charter – Clifton Karnei

Charter is attached as a separate document

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

Purpose

The Finance and Audit Committee (the “Committee”) of the Board of Directors (“Board”) of Electric Reliability Council of Texas, Inc. (“ERCOT” or ~~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 (“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 Member 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 and Qualifications

Committee Composition; Committee Member Qualifications; and Term

The Board members shall decide from among themselves who shall participate in the Committee. [M1] 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-Unaffiliated Board members ~~of the Company~~. Each Committee Member must be able to read and understand fundamental financial statements, including the balance sheet, income statement and cash flow statement. Each Committee Member shall also meet any experience requirements as may be established from time to time by the Board. [M2] The term of the Committee and its Committee Members shall be for not more than one year. [M3]

Designation and Qualifications of Committee Financial Expert

At least one Committee 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 shall endeavor to appoint at least one Board member to the Committee as the Financial Expert. [M4]

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

Election of Committee Chair; and Chair Qualifications

The Chair of the Committee shall be selected through a majority vote of the Committee ~~m~~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.~~

[v15]

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.~~

[v16]

Authority

Power to Investigate

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 Committee 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 Committee Member or any consultants to 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.~~[v17]

Reporting Relationship and Role of Company's Chief Audit Executive

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.~~[v18]

Quorum and Action by Committee Members~~Structure~~

The presence of at least half of the ~~members of the Committee~~Committee Members for the transaction of Committee business shall constitute a quorum. [v19]At any meeting at which a quorum exists, the act of a majority of the Committee ~~M~~Members present at a meeting shall be the act of the Committee. For the purposes of voting, Committee M~~m~~embers who recuse themselves from voting on an issue shall not be counted as present for that vote.

~~The Chair, in consultation with the Vice President of Finance and Treasury 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.~~^[M10]

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 and meet the Company's liquidity needs, ~~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 and associated financing plan, ~~proposed fees, and proposed financial performance measures~~ for the following year.
4. As needed throughout the year, the Committee shall review staff's recommendations regarding specific among debt financing transactions and alternatives ~~and make recommendations~~ to the Board ~~of Directors a debt structure or facility for approval~~ 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 engaged to audit ERCOT financial statements:

1. Annually, the Committee shall recommend to the Board ~~of Directors~~ the selection and engagement of ~~the Company's independent auditor~~ a qualified independent public accounting firm to audit the financial statements of ERCOT ^[MWP11]. 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~~ Members 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. ~~T~~he independent auditor's internal quality control procedures; and
 - b. ~~A~~ll 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. ~~s~~ignificant accounting policies and practices used by the Company;
 - b. ~~A~~lternative treatments of financial information as required to be discussed by the independent auditors with the Committee; and
 - c. ~~A~~ny 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 Vice President of Finance and Treasury ~~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 [audit report](#) should be accepted.

With respect to the independent auditors engaged to perform ERCOT's annual Statement on Standards for Attestation Engagements (SSAE) 16 audit:

1. Periodically select and authorize engagement of an independent audit firm to perform annual SSAE 16 audit of ERCOT's controls related to settlement operations.
2. As necessary, before and during SSAE 16 audit fieldwork, the Committee shall discuss with management and the independent auditor the planning and execution of the audit.
3. Based on its review and discussions with management and the independent auditor, the Committee shall provide a recommendation to the Board whether the Company's SSAE 16 audit report should be accepted.

With respect to the independent auditors engaged to perform ERCOT's annual 401(k) Savings Plan audit:

1. Periodically select and authorize engagement of an independent audit firm to perform annual audit of ERCOT's 401(k) Savings Plan.
2. As necessary, before and during 401(k) Savings Plan audit fieldwork, the Committee shall discuss with management and the independent auditor the planning and execution of the audit.
3. Based on its review and discussions with management and the independent auditor, the Committee shall provide a recommendation to the Board whether the Company's 401(k) Savings Plan audit report 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~~ CEO, 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 of a Committee meeting to discuss any matters that the committee or Internal Audit believes should be discussed privately.

Meetings

Frequency of 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. The Chair, in consultation with the Vice President of Finance and Treasury, 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.^[v12]

Attendance at Open Session and Executive Session of Committee Meetings

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' Alternate Representatives.

Participation and Voting During Committee Meetings

Board members who are not Committee Members (including Segment Alternates and Alternate Representatives) may attend and participate in all Committee meetings, but may not participate in Committee voting.

[v13]

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 ~~such~~ minutes to each of the Committee Members.

Evaluation

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

7. Review and Recommend Board Acceptance of SAS 70 Type I Audit Report – Cheryl Moseley

- Internal controls for some areas normally included in the SAS 70 audit were significantly revised, and controls for a few new areas were added due to the implementation of the nodal market design.
- ERCOT Staff believes performing a Type I audit of the impacted controls was the best solution to provide market participants with information that can be relied on by their company and their auditors.
- Subsequent to F&A Committee approval in October 2010, ERCOT engaged BrightLine CPAs & Associates, Inc. (formerly SAS70 Solutions, Inc.) to perform a SAS 70 Type I audit of the controls that were revised or added.
- BrightLine performed the audit in January 2011 and worked with ERCOT staff to prepare the draft audit report dated January 21, 2011 (please refer to the draft audit report distributed with the Board meeting materials).
- ERCOT Staff respectfully requests that the F&A Committee vote to recommend to the Board of Directors to accept the Type I SAS 70 audit report.

8. Annual Review and Recommendation of Board Approval of Investment and Financial Corporate Standards (Vote) – Cheryl Yager

Standards attached as separate documents.

<Vote>

ERCOT CORPORATE STANDARD

Document Name:	Investment Corporate Standard
Document ID:	CS3.2
Effective Date:	Upon Approval by the Board of Directors
Owner:	ERCOT Board of Directors and Finance & Audit Committee
Governs:	ERCOT Personnel
Approved:	ERCOT Board of Directors

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, whether those funds arise from ERCOT operations or are held by ERCOT on behalf of the ERCOT market. All references to “ERCOT” in this Investment Corporate Standard shall be to Electric Reliability Council of Texas, Inc., unless ERCOT is used in conjunction with “market”, in which case the reference shall be to the market which ERCOT manages.

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.

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

2. 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 Executive Officer, [Vice President of Finance and Treasury](#)~~Chief Financial Officer~~ (or the Controller, in the absence of a [Vice President of Finance and Treasury](#)~~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, [Vice President of Finance and Treasury](#)~~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 to the ERCOT General Counsel in documented form to be filed with corporate 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 ~~C~~orporate ~~s~~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 a Designated Investment Officer 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 Designated Investment Officers 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 ERCOT’s policies and procedures.

Reporting. A Designated Investment Officer will provide quarterly investment reports to ERCOT’s 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)3) _____ Par value, amortized book value and market value;
- 5)4) _____ Percentage of the portfolio represented by each investment category;
- 6)5) _____ For money market mutual funds, a concentration risk report of underlying investments in the funds; and
- 7)6) _____ Statement of compliance with the Investment Corporate Standard.

Investment Losses. 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.

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 ERCOT's 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.

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 \$250,000 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; and
- 3) Has assets under management in the fund of at least \$1 billion.

APPENDIX B

**Investment Corporate Standard for
Electric Reliability Council of Texas, Inc.**

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</u> (Note 1)	<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. Repurchase agreements in which the collateral is obligations of or guaranteed by the US government. (Note 3)	Note 2	7 days or less	\$5,000,000	33% of total
3. Money market mutual funds (MMMF) invested only in obligations of or guaranteed by the US government or repurchase agreements in which the collateral is obligations of or guaranteed by the US government	Note 4	Note 4	Note 4	Note 5

Note 1: To the extent possible, ERCOT will attempt to match its investments with anticipated cash flow requirements. Some level of cash may remain uninvested to meet the liquidity needs of ERCOT 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 [Standard & Poor's](#) or A3 with Moody's [Investor Service](#). 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% [percent](#) 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% [percent](#) of middle-rated securities – A2/P2 or equivalent), 3) the SEC restriction that

no more than 5% percent 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 and given the secure investments held by the funds. However, ERCOT must diversify investments held in money market accounts across at least four different fund families to safeguard liquidity. Based on availability of funds meeting the above investment criteria, ERCOT will seek to ensure that no more than 30% percent of investable funds and ~~no more than \$100 million is maintained in any one fund through May 31, 2011, and~~ no more than \$50 million is maintained in any one fund thereafter.

ERCOT CORPORATE STANDARD

Document Name:	Financial Corporate Standard
Document ID:	CS3.1
Effective Date:	Upon Approval by Board of Directors
Owner:	Board of Directors, Finance & Audit Committee
Approved:	Board of Directors, Finance & Audit 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 and an Operating and Maintenance Budget.
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 the Federal Energy Regulatory Commission ("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.
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.

TERM	DEFINITION
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.
TCR	Transmission Congestion Rights
CRR	Congestion Revenue Rights

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 ~~Vice President of Finance and Treasury or Controller~~ ~~Chief Financial Officer or Controller~~ 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. 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 Public Utility Commission of Texas rulings. ERCOT will also collect fees on behalf of the Electric Reliability Organization as approved by FERC. 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 any overspending of the Budget or under collection of revenue, or more than a 5 percent under spending of the Budget or over collection of revenue, 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 may use a combination of equity (revenue funding) and debt to finance current year Project Budgets. In determining the combination of equity and debt to be used, ERCOT will consider the impact of the current year decision on future years, but in no event will ERCOT propose to revenue fund less than 40% percent of Project Budgets during the project development phase.

Generally, ERCOT will structure debt issues such that the average maturity of the debt does not exceed 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) to the extent ~~TCR or~~ CRR auction revenues have been utilized to fund ERCOT working capital and project expenditure needs, two months of estimated ~~TCR or~~ CRR repayment obligations expected to be paid, net of projected ~~TCR or~~ CRR auction 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 or~~ CRR 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 and [Vice President of Finance and Treasury](#)~~Chief Financial Officer~~ to ensure that this Corporate Standard is implemented appropriately and to recommend changes in the Corporate Standard as needed.

5.0 FINANCIAL STANDARD ADOPTION

ERCOT's Financial Corporate Standard was 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.

9. Annual Review and Recommendation of Board Approval of Market Credit Risk Corporate Standard (Vote) – Cheryl Yager

Standard attached as separate document

<Vote>

ERCOT CORPORATE STANDARD

Document Name:	Market Credit Risk Corporate Standard
Document ID:	CS3.6
Effective Date:	May 18, 2010 <u>March _____, 2011</u>
Owner:	Board of Directors
Governs:	ERCOT Personnel
Approved:	Board of Directors, ERCOT, Inc.

1. Purpose

This Market Credit Risk Corporate Standard provides a framework by which the ERCOT Board of Directors seeks to maintain the long-term financial integrity of the ERCOT market and to help ensure that overall market credit risk is maintained within acceptable limits.

Recognizing that a number of risk factors contribute to overall market credit risk and that it is beneficial to quantify and describe these risks, a model has been developed to help evaluate the combined impact of key market credit risk factors.

This standard and the output of the Potential ~~Future Exposure~~ Credit Risk Model do not change collateral requirements or Market Participant obligations to comply with those collateral requirements under the ERCOT Protocols. Changes to collateral requirements require a change to ERCOT Protocols through Section 21, Process for Protocol Revision.

2. Definitions

Terms & Acronyms	Definition / Description
Base Case	The Potential Credit Risk Model scenario that considers only forms and amounts of collateral required by the ERCOT Protocols.
BOD	Board of Directors
Current Case	The Potential Credit Risk Model scenario that considers forms and amounts of collateral held as of a specific point in time. This scenario may include collateral amounts above those required by the ERCOT Protocols and which may be unilaterally withdrawn at the Counter-Party's direction.
CWG	Credit Work Group
Expected Loss	The average – although not the most common – outcome across all model outcomes. It represents the loss the ERCOT market as a whole should expect to incur over time under given market conditions as a result of its portfolio credit risk.
Loss Distribution	A range of potential losses under a specific set of parameters with a given probability of occurrence

Terms & Acronyms	Definition / Description
Potential Future Exposure Credit Risk (PFPCR) Model	The financial model that ERCOT uses to measure potential credit risk. It is constructed using a standard Potential Future Exposure framework that produces a portfolio Loss Distribution of potential losses.
Potential Future Exposure Credit Risk (PFECR) Report	A report that summarizes the results from the PFECR Model together with ERCOT's analysis.
Potential Future Exposure	An estimate of potential credit risk resulting from existing counterparty relationships in light of possible future risk factors such as price volatility and volume escalation.
Probability of Default (PD)	A counter-party specific estimate of the likelihood that a specific counter-party will default over a specified time horizon
TAC	Technical Advisory Committee

3. Standards

Market Credit Risk Objective

In seeking to fulfill BOD objectives to provide for a reliable Texas electricity market, ERCOT stakeholders will

- directly consider the credit implications of operational or market decisions, and
- seek to maintain a balance of identified key credit risk factors such that the combined impact of these factors yields a market-wide credit risk profile consistent with an investment grade rating

Delegation of Authority

Responsibility for monitoring and reporting on credit risk for the market consistent with this standard is hereby delegated to the Chief Executive Officer, the [Vice President – Credit and Enterprise Risk Management](#) ~~Chief Financial Officer~~ and the Treasurer. These individuals will ensure the BOD is advised of credit risk as measured by the [PCR PFE](#) Model.

This delegation does not mean that the results of any particular model analysis will be the final determination of credit risk in the ERCOT market. Such determination rests with the BOD.

Internal Control

The Treasurer will ensure that written procedures and internal controls are established over the portfolio credit risk analysis process to ensure that results are consistent with the approved process reflected in this standard.

The Treasurer will ensure that these controls are reviewed periodically by ERCOT's Internal Audit staff to monitor compliance with control procedures. The results of Internal Audit reviews as well as underlying controls may be reviewed by the Finance and Audit Committee of the BOD upon request.

In addition, the Treasurer, in cooperation with the BOD, will seek an independent review of the [PFEPQR](#) Model prior to incorporating the [PFEPQR](#) Model into any determination of collateral requirements or within one year after Nodal market implementation and at least biennially thereafter.

Measurement

ERCOT will use a standard Potential Future Exposure framework for [estimatingmeasuring](#) credit risk. The [PFEPQR](#) Model, which was built on this framework, will be maintained within this framework.

At a minimum, ERCOT's portfolio credit risk [analysis-estimation](#) for the [NodalZonal](#) market will include the following risk factor [assumptions](#):

- [Estimated](#) Probability of Default for each QSE ~~(resulting from credit score or rating)~~,
- Forward price [analysisestimation](#),
- Price volatility [analysis-estimation for both Real Time and Day Ahead Markets as appropriate](#),
- Volume escalation behavior [analysisestimation, taking into consideration both Real Time and Day Ahead Market volume activity](#)
- [Estimated value of Congestion Revenue Rights](#), and
- Simplified collateral calculations.

~~With the implementation of the Nodal market, ERCOT's portfolio credit risk analysis for the Nodal market will include the following risk factors (in addition to those outlined above):~~

- ~~• Price volatility analysis for the Day Ahead Market,~~
- ~~• Bid and offer volume analysis in the Day Ahead Market, and~~
- ~~• Value of Congestion Revenue Rights.~~

ERCOT will recommend updates of these and other risk factors if key risk factors change.

ERCOT will update model assumptions periodically with CWG input. The [Finance and Audit Committee](#)~~BOD~~ will be informed of all model parameter changes.

At ERCOT's discretion or upon request by the BOD, TAC or CWG, ERCOT will run stress scenarios in addition to the Base Case and Current Case to quantify extreme credit risk (incorporating such things as market price events, high correlations of default, impacts of specific types of market activities and high concentration of exposures to counter-parties or types of counter-parties).

While recognizing that it is impractical to model all possible loss scenarios within the [PFEPQR](#) Model, the [PFEPQR](#) Model is a valuable tool to more effectively ~~monitor~~ [estimate](#) credit ~~risk-exposure~~ within the ERCOT market [under set assumptions](#). The model considers identified risk factors and provides an indication of potential losses; however, actual losses may be more or less than those indicated by the model.

Also, since PFE by itself does not provide a full picture of risk, ERCOT should provideutilizes other metrics to provide a broader understanding of credit risk.

It should also be recognized that multiple metrics are necessary to properly understand credit risk, so that PFE by itself does not provide a full picture of risk.

Reporting

ERCOT will maintain and run the PFEPGR Model and will prepare a summary analysis of results:

1. at least quarterly,
2. whenever ERCOT determines there have been significant changes in underlying credit risk factors-assumptions which warrant a model run, and
3. upon request of TAC or CWG when contemplating market rule changes for which significant credit implications are being evaluated.

The PFEPGR Report will, at a minimum, include:

1. the Base Case and Current Case scenarios,
2. EeExpected Loss-Loss, median loss and LlLoss DdDistributions at the 90, 95, 99 + percentiles for required and ad hoc scenarios,
3. llLarge impact stress scenarios at or above the 99th percentiles and other stress scenarios,
4. a listing of inputs used and assumptions made (specific, where possible; general when inputs are counter-party specific), and
5. ERCOT's summary analysis of the reasons for significant changes in the measurement of credit risk from the prior PCRPF Report.

A summary of the PFEPGR Report will be provided to the Finance and Audit Committee of the BOD, TAC and the CWG at least quarterly.

Market Credit Risk Corporate Standard Adoption

ERCOT's Market Credit Risk Corporate Standard was adopted by resolution of the BOD. The standard is reviewed at least annually by the Finance and Audit Committee and any modifications made thereto must be approved by the BOD.

10. Committee Approval of Credit Work Group Charter <Vote> Tamila Nikazm

- **The Credit Work Group Charter requires that** “This Charter shall be reviewed and ratified at least annually by the F&A Committee.”
 - At its February 23, 2011 meeting, the CWG voted to recommend that F&A ratify the CWG Charter with the minor edits noted.
 - See attached



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 F&A 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:

- Providing input on credit matters as requested by the F&A Committee or by TAC or TAC subcommittees

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

- 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 Employee 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 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 F&A Committee. If the Chair or Vice-Chair steps down during his or her term, the CWG will hold a special election to fill the vacant position within 60 days and the vote will be confirmed by the F&A Committee.

The CWG Chair shall report at least semi-annually to the F&A Committee regarding the state of credit policy within the ERCOT Region. In addition, the CWG Chair shall notify the F&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 Representative or proxy who may attend meetings and vote on the CWG member's behalf. Alternate 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. Alternative Representatives count toward establishing a quorum at a CWG meeting; proxies do not. If a CWG member wishes to designate an Alternate Representative or proxy, the CWG member must send to ERCOT notification of the designation of such Alternative Representative or proxy in advance of any meeting and the designation shall be valid for the time period designated by the CWG 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. 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 Committee if such dissenting party chooses to do so.

E-mail Voting: An e-mail vote is permitted provided a Notification is distributed to the CWG distribution list. 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 ERCOT 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 Representatives must meet the qualifications as identified on the attached Qualifications Guidelines for Credit Work Group Membership. The F&A Committee shall review the requirements for membership in the CWG annually.

This Charter shall be reviewed and ratified at least annually by the F&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 ~~October 20, 2009~~

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 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.

11. Discuss Credit Management Practices and Judgments: EEA Event Overview – Cheryl Yager and Mark Ruane

- **Energy Emergency Alert (EEA) event**
 - Background – average daily prices
 - Credit impact of February 2, 2011 Energy Emergency Alert (EEA)
 - ERCOT's use of discretion – considerations
 - Credit adjustments
 - Simplified example – Aggregate Incremental Liability (AIL) Impact
 - Simplified example – Average Daily Transaction Extrapolated (ADTE) impact
 - Default
 - Lessons learned
 - EEA event summary
- **General Credit management practices and judgments**
 - Use of discretion in credit decisions
 - Credit adjustment process

11. Discuss Credit Management Practices and Judgments: EEA Event Background – Average Daily Prices

The Energy Emergency Alert (EEA) beginning February 2nd was the first unique risk event encountered since 2008

DAM Daily Average Prices by Load Zone							January 2011			December 2010		
NAME	1-Feb-11	2-Feb-11	3-Feb-11	4-Feb-11	5-Feb-11	6-Feb-11	AVERAGE	LOW	HIGH	AVERAGE	LOW	HIGH
LZ_AEN	40.30	66.45	463.52	93.76	44.27	36.82	34.51	27.98	43.48	31.61	26.34	38.23
LZ_CPS	38.10	66.99	443.47	94.17	50.22	36.75	34.03	27.99	42.00	31.01	25.42	37.15
LZ_HOUSTON	39.10	66.26	444.73	89.73	42.83	36.93	33.79	28.05	42.01	31.76	26.62	37.61
LZ_LCRA	38.81	64.60	425.05	94.07	44.92	36.72	34.08	27.91	41.76	31.24	26.03	37.47
LZ_NORTH	43.00	79.02	483.55	94.09	45.50	37.20	34.11	28.17	41.88	31.69	26.62	37.90
LZ_RAYBN	43.07	74.34	476.54	92.88	45.16	37.20	34.07	28.17	41.89	31.71	26.54	37.95
LZ_SOUTH	38.14	74.54	481.06	211.19	76.25	38.42	33.80	28.24	50.77	30.67	24.97	35.95
LZ_WEST	32.29	77.34	488.37	101.09	45.15	32.01	31.37	19.66	41.18	29.50	15.29	38.67

RTM Daily Average Prices by Load Zone							January 2011			December 2010		
NAME	1-Feb-11	2-Feb-11	3-Feb-11	4-Feb-11	5-Feb-11	6-Feb-11	AVERAGE	LOW	HIGH	AVERAGE	LOW	HIGH
LZ_AEN	32.27	789.27	84.49	47.61	28.89	20.45	34.18	19.89	72.42	29.33	19.57	53.91
LZ_CPS	37.04	786.20	88.39	51.08	28.82	20.45	34.47	19.95	71.56	28.96	19.51	54.38
LZ_HOUSTON	28.71	781.15	70.91	45.78	28.97	20.45	34.05	20.16	72.68	29.45	19.68	53.89
LZ_LCRA	36.79	797.28	90.93	49.84	28.81	20.45	34.13	19.90	71.77	29.01	19.48	53.66
LZ_NORTH	100.60	797.27	79.64	47.11	29.10	20.45	34.81	19.70	73.51	29.77	19.82	53.82
LZ_RAYBN	95.32	796.76	79.43	47.08	29.12	20.45	34.36	19.70	73.62	29.86	19.85	53.85
LZ_SOUTH	31.33	803.46	696.08	56.26	53.12	20.45	39.79	21.50	146.47	28.63	19.47	53.53
LZ_WEST	31.74	781.20	82.59	42.99	24.47	20.45	31.16	-6.91	72.58	24.70	6.58	57.29

Note:

1) Data for January 2011 and December 2010 includes a) the average price for the month, b) the lowest daily average price for the month and c) the highest daily average price for the month.

11. Discuss Credit Management Practices and Judgments: EEA Event Credit Impact

- **Certain portions of the credit calculations in the ERCOT Protocols use recent history to estimate forward risk**
 - While this generally produces reasonable results, the underlying assumptions were reviewed given the atypical activity beginning February 2nd
- **After its review, ERCOT made adjustments to collateral requirements to mitigate the impact of the weather event on the estimates of forward risk**
 - The Protocols allow ERCOT flexibility to adjust exposure calculations to address unusual situations as they arise
 - ERCOT ensured that actual activity incurred (including activity on Feb 2nd) was collateralized while adjusting calculations to mitigate the impact of high prices on the estimation of forward risk

11. Discuss Credit Management Practices and Judgments: EEA Event – ERCOT’s Use of Discretion – Considerations

- **ERCOT took the following factors into consideration when determining what adjustments to make to the credit calculations**
 - Timing: The need to address changes in a rapid and timely manner since credit exposure calculation impacts the Counter-Party’s (CP’s) ability to participate in the Day Ahead Market (DAM)
 - Different from Zonal
 - Transparency: The need to be transparent so that the market understood ERCOT’s actions and could shadow the credit calculation
 - Market notices used
 - Broad market impact: The risk that the EEA impacted a broad range of market participants
 - Adjustments were made globally
 - Atypical nature of the event: The EEA beginning on February 2nd was atypical (e.g. coldest weather in 20 years, large amount of forced outages, etc)

11. Discuss Credit Management Practices and Judgments: EEA Event – Credit Adjustments

- **Collateralization:**
 - *Historical Risk:* Collateral for estimated incurred activity unchanged
 - *Forward Exposure:* Credit calculations of forward exposure adjusted due to the atypical nature of
 - Day Ahead activity on February 3rd and 4th
 - Day Ahead Market Extrapolated (DALE)
 - Real Time (RT) prices incurred on February 2nd and 3rd and
 - Aggregate Incremental Liability (AIL)
 - Average Daily Transaction Extrapolated (ADTE)
- **Impact of adjustments for February 3, 2011**
 - Total Potential Exposure (TPE) before adjustments \$ 686 million
 - Total Potential Exposure (TPE) after adjustments \$ 420 million – more representative of actual forward market risk

11. Discuss Credit Management Practices and Judgments: EEA Event – Credit Adjustments (continued)

- **CMM Core Credit Calculation**

- AIL: Applied a factor of .05 to the 150% price volatility factor to offset the impact of the \$800 average daily price from Operating Day Feb 2nd on forward week
- ADTE: Exclude operating days Feb 2nd and 3rd from the ADTE calculation
- DALE: Held DALE constant from Feb 4th through Feb 9th; began calculation again excluding DAM runs for operating days Feb 3rd and 4th

- **Day Ahead Market**

- Changed “e1” factor for 2 days. The revised “e1” was set at 70% of the prior “e1”
- “uth” percentile reduced from 90th percentile to 80th percentile beginning February 4th and rolling it back to the 90th percentile beginning February 9th

- **Additionally**

- Monitored Benchmark Report activity closely through this period
- Monitored for increased use of Real Time activity through this period

11. Discuss Credit Management Practices and Judgments: EEA Event Simplified Example – AIL Impact

Aggregate Incremental Liability (AIL) exposure for February 2nd and estimate for February 9th

Simplified example of Real Time (RT) impact

	<u>February 2nd</u> (Historical)	<u>February 9th</u> (based on Feb 2nd data) (Forward)
Average Daily Price on Feb 2	\$ 800	\$ 800
Forward day multiplier	n/a	150%
Average Daily price for collateral (before adjustment)	\$ 800	\$ 1,200
Adjustment factor applied	n/a	0.05
Average Forward Day Price used for collateral (after adjustment)	\$ 800	\$ 60
Real Time volume from February 2nd	1,000	1,000
Liability collateralized	<u>\$ 800,000</u>	<u>\$ 60,000</u>
Average Daily Price for January 2011		\$ 35.00
Forward day multiplier		150%
Estimated Forward Day Price		\$ 52.50
Round up		7.50
Estimated Forward Day Price used for collateral		<u>\$ 60.00</u>

11. Discuss Credit Management Practices and Judgments: EEA Event Simplified Example – ADTE Impact

Average Daily Transaction Extrapolated (ADTE) for weeks inclusive of February 2nd and 3rd

Simplified example of Real Time (RT) impact for a net buyer in RT

Daily settlement statements	Volume (MWh)	Price	<u>Standard Calc</u>	<u>Adjusted Calc</u>
January 21, 2011	1000	35 \$	35,000	\$ 35,000
January 22, 2011	1000	35	35,000	35,000
January 23, 2011	1000	35	35,000	35,000
January 24, 2011	1000	35	35,000	35,000
January 25, 2011	1000	35	35,000	35,000
January 26, 2011	1000	35	35,000	35,000
January 27, 2011	1000	35	35,000	35,000
January 28, 2011	1000	35	35,000	35,000
January 29, 2011	1000	35	35,000	35,000
January 30, 2011	1000	35	35,000	35,000
January 31, 2011	1000	35	35,000	35,000
February 1, 2011	1000	35	35,000	35,000
February 2, 2011	1000	800	800,000	
February 3, 2011	1000	700	700,000	
Days included in calculation			14	12
Average daily transaction			137,143	35,000
Multiplied by number of days			40	40
ADTE			<u>\$ 5,485,714</u>	<u>\$ 1,400,000</u>

Note: All Counter-Parties received the same adjustment, whether they were net buyers or net sellers into the Real Time market on February 2nd and 3rd.

11. Discuss Credit Management Practices and Judgments: EEA Event – Default

- All activity from the EEA beginning Feb 2nd has been paid other than for the one default experienced
- One default
 - QSE and LSE
 - 7,743 Retail Customers
 - Approximately 383 MWh per day of load
- Default timeline
 - Thursday, February 3rd – Collateral call
 - Monday, February 7th – Breach notice
 - Wednesday, February 9th (5:00 pm) – In Default
 - Thursday, February 10th (10:00 am) – Mass Transition Call

11. Discuss Credit Management Practices and Judgments: EEA Event – Default (continued)

- **Short payments**
 - As of March 11th, three invoices have been short paid for a total of \$731,419.61
 - As allowed per Protocols, ERCOT held back \$30,000 of collateral to pay final and true up invoices
 - Invoices that would unduly deplete the fund will be short paid
 - Any collateral not used for final and true up invoices will be used to reduce the ultimate uplift

11. Discuss Credit Management Practices and Judgments: EEA Event – Lessons Learned

- **ERCOT discussed the EEA event with the CWG and sought input on actions ERCOT took and ways ERCOT could improve response. CWG comments:**
 - Generally felt like actions were reasonable
 - No additional suggestions offered
 - Confirmed that communication using Market Notices was adequate
 - Will work with ERCOT to review AIL estimation mechanisms for ways to improve estimates
- **ERCOT encouraged members to send in any suggestions they think of later**
- **In addition, ERCOT committed to review mechanisms for adjusting exposure**
 - Possibly fine tune CMM adjustment mechanism to allow more specificity
 - Seek flexibility to adjust DAM parameters

11. Discuss Credit Management Practices and Judgments: EEA Event Summary

- **ERCOT's credit actions during the EEA event beginning February 2nd were taken with the intent to**
 - remove the impact of the high prices resulting from the EEA on forward credit calculations
 - support market liquidity during and immediately following the event
- **ERCOT believes the following factors contributed to ERCOT's ability to manage through the credit impacts of the EEA**
 - the market's conservative credit practices
 - flexibility granted ERCOT to adjust credit
 - responsiveness of the market during the period
- **ERCOT will follow up on lessons learned**
- **Note: Actions taken by ERCOT during the EEA beginning February 2nd were based on the facts at the time. Future events may be treated differently based on the facts at the time.**

11. Discuss Credit Management Practices and Judgments: ERCOT's Use of Discretion in Credit Decisions

- **The ERCOT Nodal Protocols provide that ERCOT can use judgment**

“If ERCOT, in its sole discretion, determines that the TPE for a Counter-Party calculated under paragraph (1) above ***does not adequately match the financial risk*** created by that Counter-Party’s activities under these Protocols, then ERCOT may set a different TPE for that Counter-Party (CP). ERCOT shall, to the extent practical, give to the Counter-Party the information used to determine that different TPE. ERCOT shall provide written or electronic notice to the Counter-Party of the basis for ERCOT’s assessment of the Counter-Party’s financial risk and the resulting creditworthiness requirements.”
- **From the above, ERCOT took the following guiding principles that are used when making adjustments:**
 - Adjustments are risk based – ERCOT adjusts collateral to fit the risk
 - Similar situations are treated similarly – for consistency in application
 - Notify entities when adjustments are made
 - Global adjustment – Generally a market notice
 - Entity specific adjustment – Notify the CP directly by e-mail, phone call, etc.

11. Discuss Credit Management Practices and Judgments: ERCOT's Use of Discretion in Credit Decisions (continued)

- **Examples of situations when adjustments are made**
 - Minimum collateral requirement
 - ERCOT reviews a Counter-Party's (CPs) Total Potential Exposure (TPE) relative to a Low and High Benchmark
 - For CPs that meet certain criteria (e.g. entities with less than a BB- rating, entities with negative equity, entities that have not provided financial statements, etc), ERCOT adjusts collateral requirements to help ensure that collateral is maintained at or above the Low Benchmark
 - Increases or decreases in an entity's customer base – collateral requirements may be raised or lowered accordingly
 - Emergency Interruptible Load (EIL) costs are invoiced once a quarter on one daily final invoice – collateral is adjusted to reduce forward impact
 - Change in the way a load serving CP meets its load requirement
 - Moves from Real Time to Energy Trades – may decrease forward credit component with proof of change
 - Moves from Energy Trades to Real Time – may increase forward credit component

11. Discuss Credit Management Practices and Judgments: Credit Adjustment Process – Cheryl Yager and Mark Ruane

- **A credit analyst identifies a need for an adjustment by**
 - Reviewing a CP's exposure calculation
 - Talking with a CP about their activity
 - Reviewing the Benchmark tool
- **The credit analyst reviews the issue with the Credit Manager and/or Treasurer and determines whether an adjustment is appropriate**
- **The credit analyst enters the adjustment into CMM and the Credit Manager/Treasurer approves the adjustment**
- **The credit analyst notifies the CP of the adjustment made and the reason for it**

12. Periodic Review of Liquidity Report: Overview

Cheryl Yager

- **Debt outstanding at December 31, 2010**
- **Projected debt needs for 2011 and 2012**
- **Projected debt capacity in 2011 and 2012 under current Financial Corporate Standard liquidity requirements**
- **Summary**

12. Periodic Review of Liquidity Report: Debt Outstanding at December 31, 2010 – Cheryl Yager

Facility	Counterparty	Maturity Date	As of 12/31/2010		
			Capacity	Debt Outstanding (\$ millions)	Credit Available
Senior Notes	5 Investors *	May 15, 2014	\$ 54.5	\$ 54.5	\$ -
Term Loan	JPMorgan/Wells Fargo	November 1, 2012	\$ 141.7	\$ 141.7	\$ -
Revolver	JPMorgan/Wells Fargo	August 13, 2013	\$ 100.0	\$ 65.0	\$ 35.0
Revolver	JPMorgan/Wells Fargo	June 15, 2012	\$ 75.0	\$ 75.0	\$ -
Revolver	Bank of America	August 24, 2012	\$ 50.0	\$ -	\$ 50.0
		Subtotal	\$ 421.2	\$ 336.2	\$ 85.0
		CRR Borrowings		\$ -	\$ -
		Total	\$ 421.2	\$ 336.2	\$ 85.0

* Senior Note Investors are AIG, Allstate, Hartford Financial, Prudential, TIAA-CREF

Note 1: Term Loan will be repaid one third of principal each November through 2012

Note 2: Senior Note will be repaid \$13.7 million each May through 2014.

No revolving debt capacity matures in 2011; however, \$125 million of revolving debt capacity matures in mid-2012

12. Periodic Review of Liquidity Report: Projected Debt Needs for 2011 and 2012 – Cheryl Yager

	<u>2011</u>	<u>2012</u>
	(in \$ millions)	
<u>Outstanding debt (estimated)</u>		
Beginning Balance	336.2	272.2
Capital expenditures funded with debt	69.7	18.0
Revenue available for debt reduction	<u>(133.7)</u>	<u>(142.2)</u>
Ending Balance	<u>272.2</u>	<u>148.0</u>
 <u>Capital expenditures funded with debt - Base and Nodal</u>		
Base capital expenditures	41.9	30.0
Transfer - from 2010 to 2011		
Debt Funding %	<u>0.6</u>	<u>0.6</u>
Borrowing for base capital expenditures	25.1	18.0
2010 Carry Forward	<u>19.4</u>	<u>-</u>
New borrowing - base	44.5	18.0
Nodal expenditures (excl contingency and interest)	<u>25.2</u>	<u>-</u>
Total - New Borrowing	<u>69.7</u>	<u>18.0</u>
 <u>Revenue available for debt reduction</u>		
System Administration Fee	26.2	26.2
Nodal Surcharge (excl int)	<u>107.5</u>	<u>116.0</u>
Total revenue available for debt reduction	<u>133.7</u>	<u>142.2</u>
 Net increase / (decrease) in debt	 <u>(64.0)</u>	 <u>(124.2)</u>

Assumptions

Base spend per 2011 budget / five year plan

ERCOT expects to pay down debt substantially in both 2011 and 2012.

12. Periodic Review of Liquidity Report

Cheryl Yager

Projected debt capacity in 2011 and 2012 under current Financial Corporate Standard liquidity requirements

Borrowing (\$ Millions)	As of December 31, 2010			As of December 31, 2011			As of December 31, 2012		
	Debt Capacity	Debt Outstanding	Credit Available	Debt Capacity	Debt Outstanding	Credit Available	Debt Capacity	Debt Outstanding	Credit Available
Senior Notes	\$ 54.5	\$ 54.5	\$ -	\$ 40.8	\$ 40.8	\$ -	\$ 27.1	\$ 27.1	\$ -
Term Loan	141.7	141.7	-	70.8	70.8	-	-	-	-
JPM Chase / Wachovia Revolver	100.0	65.0	35.0	100.0	85.6	14.4	100.0	120.9	(20.9)
JPM Chase / Wachovia Revolver	75.0	75.0	-	75.0	75.0	-	-	-	-
Bank of America Revolver	50.0	-	50.0	50.0	-	50.0	-	-	-
Total	\$ 421.2	\$ 336.2	\$ 85.0	\$ 336.6	\$ 272.2	\$ 64.4	\$ 127.1	\$ 148.0	\$ (20.9)
Required liquidity (estimated)			(50.0)			(50.0)			(50.0)
Excess available	\$ 421.2	\$ 336.2	\$ 35.0	\$ 336.6	\$ 272.2	\$ 14.4	\$ 127.1	\$ 148.0	\$ (70.9)

Fix	76%	66%	18%
Float	24%	34%	82%

Debt capacity is expected to be adequate through 2011 and the percentage of floating rate debt is within requirements.

In early 2012, ERCOT will need to a) replace maturing debt capacity, including b) some level of fixed rate debt.

12. Periodic Review of Liquidity Report: Summary

Cheryl Yager

- **ERCOT expects to pay down debt substantially in both 2011 and 2012**
- **Although debt levels are coming down, ERCOT will still need to address debt capacity maturing in mid- 2012**
- **ERCOT plans to include its plan to address these needs during the 2012 budget process**

13. Committee Briefs

ERCOT Market Credit Status

as of 1/31/2011

as of 2/28/2011

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		# of CPs*	Total Potential Exposure (\$)	% of TPE	Total Unsec Credit Limit / Security Posted	
Exposure in the ERCOT Market (owed to ERCOT)										
<u>QSEs that meet ERCOT Creditworthiness Standards</u>										
Ratings over BBB-	12	46,093,332	15%	491,917,949	U	14	56,032,032	18%	498,094,390	U
<u>QSEs that do not meet ERCOT Creditworthiness Standards</u>										
Ratings below BBB- or not rated										
Cash & Letters of Credit	69	174,087,168	55%	1,234,150,097	S	60	135,867,944	44%	851,354,151	S
Guarantee Agreements	25	93,625,570	30%	698,094,854	S	26	114,574,251	37%	702,694,854	S
Total Exposure	106	313,806,069	100%			100	306,474,226	100%		
Other QSEs in the ERCOT Market (ERCOT owes)										
<u>QSEs that meet ERCOT Creditworthiness Standards</u>										
Ratings over BBB-	14	(1,130,536)	-72%	362,350,846	U	12	-	0%	357,072,604	U
<u>QSEs that do not meet ERCOT Creditworthiness Standards</u>										
Ratings below BBB- or not rated										
Cash & Letters of Credit	72	(440,230)	-28%	37,630,488	S	81	(468,245)	-100%	128,236,235	S
Guarantee Agreements	8	-	0%	58,752,000	S	9	(1,652)	0%	64,727,000	S
Total	94	(1,570,766)	-100%			102	(469,897)	-100%		

Total

200

202

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.

Summary Benchmark Report as of February 28, 2011

	# of CPs	Ave Gen Vol (in MWh)	Ave Load Vol (in MWh)	% CPs	% Gen Vol	% Load Vol	CP TPE (in 000's)	Low Benchmark (in 000's)	High Benchmark (in 000's)
Between High and Low									
w/ No Load and No Generation	86						6,192	2,504	17,755
w/ Load and/or Generation	78	630,267	741,017				204,040	115,140	679,645
Total	164	630,267	741,017	81%	76%	88%	210,232	117,644	697,400
Above High									
w/ No Load and No Generation	14	-	-				17,630	143	1,343
w/ Load and/or Generation	17	160,821	46,568				72,781	11,214	56,546
Total	31	160,821	46,568	15%	19%	6%	90,411	11,356	57,888
Below Low									
w/ No Load and No Generation	3	-	-				(468)	0	-
w/ Load and/or Generation	4	39,022	50,546				5,829	8,580	68,223
Total	7	39,022	50,546	3%	5%	6%	5,361	8,580	68,223
Total	202	830,110	838,131	100%	100%	100%	306,004	137,581	823,511

Benchmark Assumptions

		Forward Risk Estimate				
		Volume Component			Price Component	
Historical Risk		Basis	# of days	Factor	Basis	Price volatility factor
Low Benchmark						
Counter-Parties - Load only	Outstanding receivable/payable - invoiced and estimated	30-day average total load volume	2	1.0	Avg real time price - floor - \$25, cap - \$50	1.0
Counter-Parties - Generation only	Outstanding receivable/payable - invoiced and estimated	30-day average total generation volume	2	0.2	Avg real time price - floor - \$25, cap - \$50	1.0
Counter-Parties - neither Load or Generation	Outstanding receivable/payable - invoiced and estimated	30-day average imbalance volume (real time activity)	2	1.0	Avg real time price - floor - \$25, cap - \$50	1.0
High Benchmark						
Counter-Parties - Load only	Outstanding receivable/payable - invoiced and estimated	Highest total load volume over past 30-days	9	1.0	Same	1.5
Counter-Parties - Generation only	Outstanding receivable/payable - invoiced and estimated	Highest total generation volume over past 30-days	9	0.2	Same	1.5
Counter-Parties - neither Load or Generation	Outstanding receivable/payable - invoiced and estimated	Highest imbalance volume over past 30-days (real time activity)	6	1.0	Same	1.5

Note 1: If an entity has both load and generation volume, the greater of the two estimates is used in the Benchmark

ERCOT
Summary of Investments
February 28, 2011

(\$ in mils)

Investment Account	Investment Type	Operating	Market	Deposit/ Restricted	Total	%
						Investments
Bank of America	<i>Treasury and Repo</i>	\$ -	\$ 2.5	\$ 11.7	\$ 14.2	5%
BlackRock 60	<i>Treasury and Repo</i>	-	2.0	\$ 3.5	\$ 5.5	2%
BlackRock 62	<i>Treasury only</i>	-	-	\$ 47.0	\$ 47.0	17%
Federated 068	<i>Treasury and Repo</i>	\$ 3.5	2.9	\$ 3.1	\$ 9.5	3%
Federated 0125	<i>Treasury only</i>	\$ -	11.6	\$ 26.0	\$ 37.6	14%
Fidelity 695	<i>Treasury and Repo</i>	\$ -	-	\$ 14.8	\$ 14.8	5%
Fidelity 680	<i>Treasury Only</i>	\$ -	-	\$ 43.6	\$ 43.6	16%
Invesco	<i>Treasury and Repo</i>	\$ -	2.0	\$ 13.4	\$ 15.4	6%
JPMorgan	<i>Treasury and Repo</i>	\$ 3.6	7.3	\$ 13.4	\$ 24.3	9%
Wells Fargo	<i>Treasury and Repo</i>	\$ -	2.6	\$ 14.4	\$ 17.0	6%
Wells Fargo	<i>Treasury only</i>	\$ -	-	\$ 48.1	\$ 48.1	17%
		<u>\$ 7.1</u>	<u>\$ 30.9</u>	<u>\$ 239.0</u>	<u>\$ 277.0</u>	<u>100%</u>

Other cash net of outstanding checks

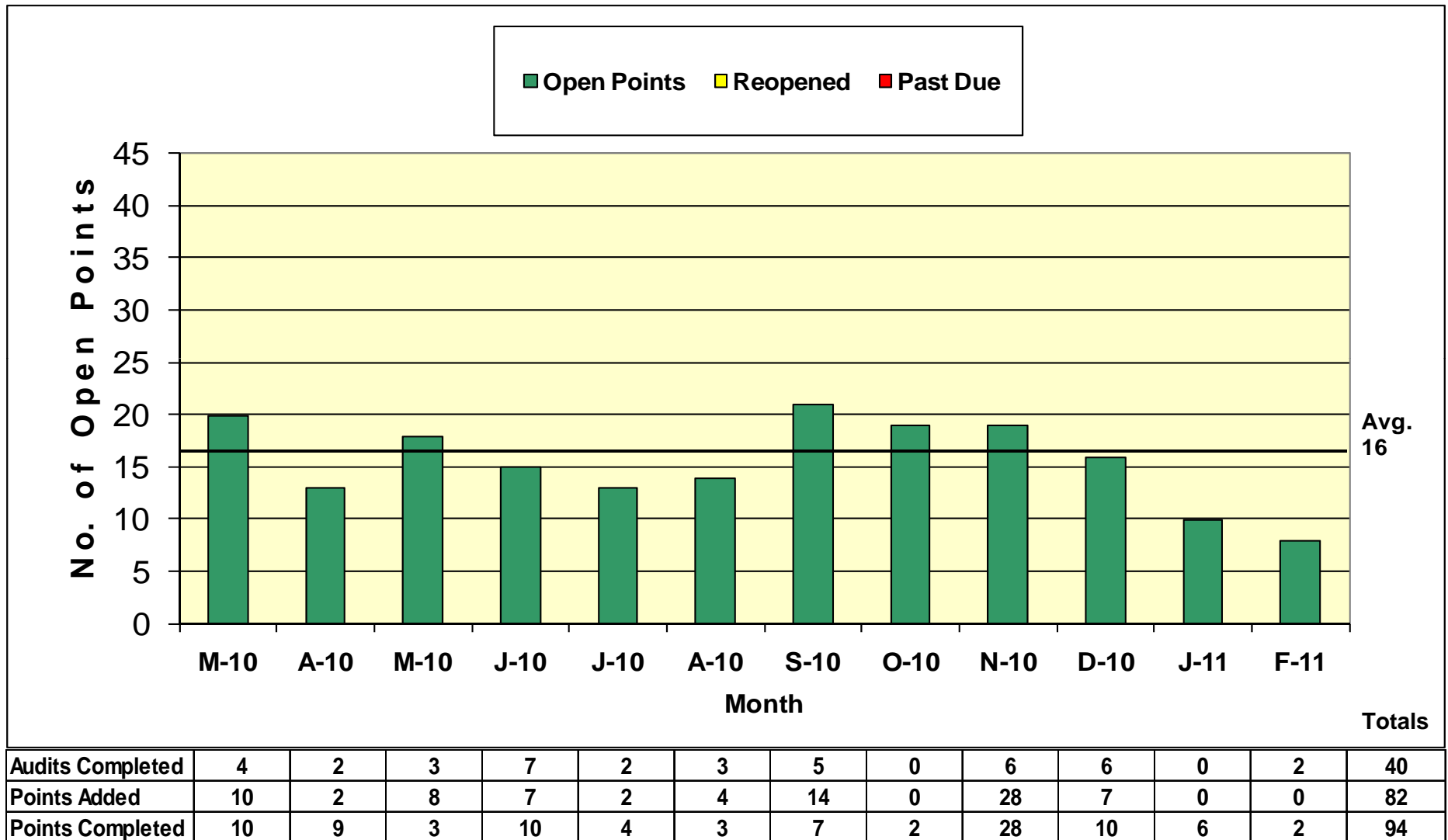
N/A

Total cash and cash equivalents

\$ 277.0

13. Committee Brief ICMP: Status of Open Audit Points

Cheryl Moseley



All audit points expected to be complete by 6/30/11.



13. Committee Brief: ICMP – Audits Cheryl Moseley

Audits Completed

(last 3 months)

Internal Audits

- Nodal Program Reporting (Special Request)
- Nodal Program Spending (Part 2 of 3)
- Outage Coordination
- Software License Mgmt. Process (Special Request)
- Nodal Program Spending (Part 3 of 3)
- FY2010 Fraud Auditing

External Audits

- 2010 Zonal SAS70 Audit (SAS70 Solutions, Inc.)
- 2011 Type I SAS70 Audit (SAS70 Solutions, Inc. (now BrightLine CPAs & Associates, Inc.))

Audits in Progress

Internal Audits

- Nodal Fixed Assets
- Governmental Grants and Contract Compliance
- Nodal Protocol 3.10(5) Required Audit – Consistent Information in Operations Models
- Nodal Protocol 17.3 Required Audit – ERCOT Market Monitoring Data Handling
- Protocol 1.4 Required Audit – Confidentiality Compliance
- ERCOT Software/System Development Lifecycle
- Protocol 1.4 Required Audit – Independence Verification
- Allegis Resource Management

External Audits

- 2010 Financial Audit (Ernst & Young, LLP)

Planned Audits

(next 3 months)

Internal Audits

- Standard for Black Start & EILS Agreements
- Employee Compensation and Benefit Plan practices – HR
- ADP (Payroll & Benefits)
- Assessment of Completed Projects
- Nodal Program Performance Bonuses
- Q1 2011 Fraud Auditing

External Audits

- 2011 Type II SSAE 16 (SAS 70) Audit (BrightLine CPAs & Associates, Inc.)



13. Committee Brief: ICMP – Security Assessments

Cheryl Moseley

Consultation/Analysis Reports Completed

(last 3 months)

Assessments

- None

Open Consultation/ Analysis Reviews

(in progress)

Assessments

- None








Planned Consultation/ Analysis Reviews

(next 3 months)

Assessments

- 1 Assessment planned


ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
RISK MANAGEMENT EVENT PROFILE MATRIX (as of March 1, 2011)

Strategic	Operational Excellence	Market Facilitation	Grid Reliability	Reporting	Legal and Regulatory Compliance
<p>Green Strategy Development</p> <p><i>Corporate objective setting adequately incorporates informed stakeholder input, market realities and management expertise.</i></p>	<p>Green Performance Monitoring</p> <p><i>Clearly defined and actively monitored performance metrics linked to mission and goals - Performance status communicated and corrective action taken.</i></p>	<p>Green Market Operations</p> <p><i>Effectively manage the evolution of the wholesale and retail markets to meet the changing business environment.</i></p>	<p>Green Grid Operations</p> <p><i>Information required to operate the grid is efficiently gathered. Appropriate tools are prudently configured to efficiently operate the system.</i></p>	<p>Green Review Practices</p> <p><i>Prudent measures are taken to insure that company disclosures are properly vetted and not misleading.</i></p>	<p>Yellow Legal & Legislative </p> <p><i>Operations are conducted in compliance with all laws and regulations. Impacts of current and proposed legislation are understood and communicated.</i></p>
					<p>Regulatory uncertainty over possible future oversight roles of CFTC / FERC on ERCOT if CRRs classified as "swaps" under Dodd-Frank legislation and potential impacts on credit policies and processes.</p>
<p>Green Mission and Goals </p> <p><i>Corporate objectives and performance standards are understood and followed.</i></p>	<p>Green Business Practices</p> <p><i>Business planning, processes and management standards are effective and efficient.</i></p>	<p>Yellow Nodal Systems Stabilization </p> <p><i>Manage the deployment and stabilization of the nodal market systems</i></p>	<p>Yellow Planning</p> <p><i>Long-range planning methods enable efficient responses to system changes that are necessary to maintain reliability standards.</i></p>	<p>Green Disclosure</p> <p><i>Reporting and other disclosures to intended parties is timely, accurate and effective.</i></p>	<p>Yellow Internal Control Compliance</p> <p><i>Internal Control Compliance processes and management standards are effective, efficient, and provide stakeholders with required assurances of quality.</i></p>
<p>Strategic Plan has been approved since July of 2010. Proposed 2011 KPIs under review by HR&G Committee.</p>		<p>ERCOT working with stakeholders to address risk of exceeding 200,000 bid limit in balance of year CRR auction and will introduce an NPRR to address additional issues caused by the dead resource node pricing logic.</p>	<p>Demand for planning studies continues to grow. ERCOT has received two awards totaling \$3.5 million to produce long-term resource and transmission planning studies in 2011. Hiring is completed. In the scoping phase of the studies. Project completion 2013.</p>		<p>A limited SAS 70 Audit was completed in January (Type I). No control issues were identified. The full suite of nodal processes are scheduled to undergo a full Type II audit later this year.</p>
<p>Yellow Reputation </p> <p><i>Positive perceptions by stakeholders lead to less cost and greater flexibility resulting in enhanced enterprise value.</i></p>	<p>Yellow Workforce </p> <p><i>Organization design, managerial and technical skills, bench strength and reward systems aligned with corporate goals.</i></p>	<p>Yellow Counterparty Credit</p> <p><i>Maintain credit risk exposure for overall market within acceptable limits.</i></p>	<p>Yellow Bulk System Resources</p> <p><i>Market Participants construct and make available adequate bulk electric grid resources.</i></p>	<p>Yellow Communication </p> <p><i>Internal & external communications are timely and effective.</i></p>	<p>Yellow Industry Standards</p> <p><i>Business and operational activities in compliance with all applicable regulatory, financial & accounting requirements, standards, & directives.</i></p>
<p>Reassessed reputation risk as a result of February cold weather event.</p>	<p>Employee retention risk likely to increase as economy continues to improve.</p>	<p>Color remains yellow pending the review of risk factors in the Nodal market requested by F&A. CMM successfully launched. Market participant credit quality continues to be monitored on an ongoing basis.</p>	<p>The December update of the CDR report forecasts reserve margins in 2013 and 2016 falling below the 13.75% target reserve margin. ERCOT is evaluating the potential impact of EPA regulations and nodal pricing on future reserve margins.</p>	<p>February cold weather event revealed need for ERCOT to reassess its communication procedures for issuing Energy Emergency Alert (EEA) notifications.</p>	<p>Still waiting for the final 2009 NERC audit report for the Critical Infrastructure Protection (CIP) portion. For 2010 NERC Audit, ERCOT was found to be fully compliant on the 693 (O/P) standards. CIP status is not determined at this point</p>
<p>Green Fiscal Management</p> <p><i>ISO design requires competent, prudent and cost effective provision of services.</i></p>	<p>Green Technology Infrastructure</p> <p><i>Information systems, supporting facilities and data are effectively managed and are reliable.</i></p>	<p>Green Administration, Settlement & Billing</p> <p><i>Market rules fairly applied to all participants. Accounting is timely and accurately reflects electricity production and delivery.</i></p>	<p>Yellow Operational Responsibility </p> <p><i>Market participant conduct their operations in a manner which facilitates consistent grid reliability.</i></p>	<p>Green Adequacy and Integrity</p> <p><i>Robust processes exist to support management assertions embodied within financial reports.</i></p>	<p>Green Regulatory Filings</p> <p><i>Evidence, testimony and other supporting materials are compelling and successful.</i></p>
			<p>Operational impacts of increasing amounts of intermittent renewable generation on the system is uncertain. ERCOT has established a Resource Integration department devoted to analyzing and proposing solutions to defined issues. Questions have arisen regarding adequacy of power plant winterization plans. We are reassessing interdependence between gas and electric markets. Plans to address these issues going forward are being developed.</p>		

Notes:

Changes to Risk Categories / Descriptions shown in **Green**

Elevated risk level indicated by 

Reduced risk level indicated by downward green arrow ()

13. Committee Briefs: Quarterly Committee Education on Accounting Developments – Rebecca Beckham

- **Update on newly proposed accounting standards and reporting requirements:**

Lease Accounting

The FASB and IASB have initiated changes to their proposed model for lease accounting based on comments that indicate it is overly complex and costly to implement.

- The Boards have tentatively agreed to revise their definition of lease term and the treatment of variable lease payments.
- To prepare ERCOT for the impact of the standard, the accounting group will establish a catalog of all leases in 2011 and assess the potential impact to the financial statements and debt agreements. The impact is expected to be immaterial.

1099 Reporting

The Senate and House of Representatives have passed a measure repealing the increased reporting requirements for IRS Form 1099 information returns.

FASB- Financial Accounting Standards Board
IRS- Internal Revenue Service

IASB- International Accounting Standards Board

13. Committee Briefs: Quarterly Committee Education on Accounting Developments – Rebecca Beckham

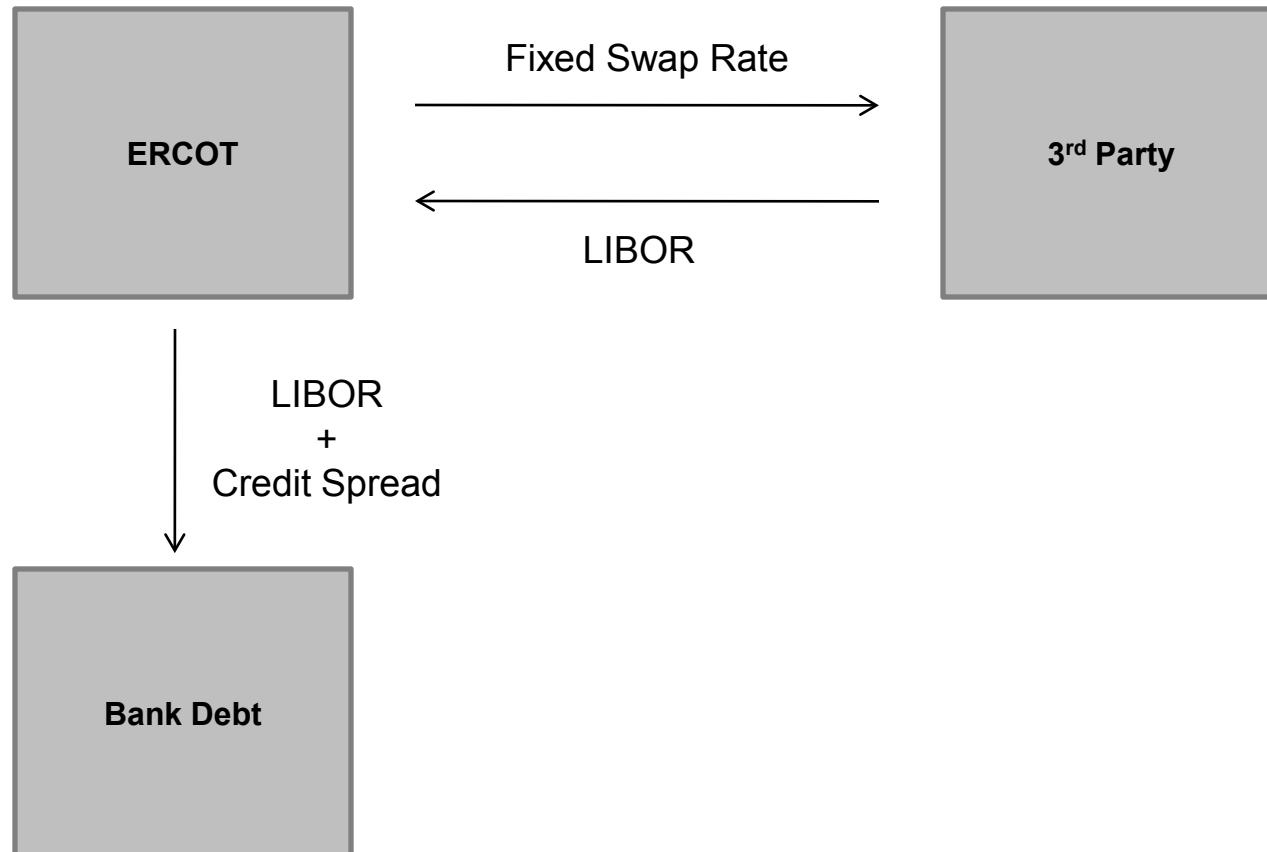
- **Discussion of a key area of audit emphasis:**

The external audit of ERCOT's 2010 financial statements is currently in progress. One area of emphasis remains ERCOT's use and accounting treatment of derivatives.

- ERCOT's Financial Corporate Standard requires unhedged, variable rate debt to not exceed 40 percent of total debt outstanding.
- ERCOT uses interest rate swaps to limit the variable rate debt, protect ERCOT from interest rate volatility, and provide more certainty of interest rates for budgeting purposes.
- ERCOT uses plain vanilla swaps to fix the floating benchmark (LIBOR) for a portion of underlying debt.

13. Committee Briefs: Quarterly Committee Education on Accounting Developments – Rebecca Beckham

- Through an interest rate swap, ERCOT pays a 3rd party a fixed rate amount and in return receives a payment based on the LIBOR rate. The payment received approximates the LIBOR floating rate ERCOT must pay on its variable rate debt.



13. Committee Briefs: Quarterly Committee Education on Accounting Developments – Rebecca Beckham

ERCOT's Interest Rate Swaps at December 31, 2010:

Counterparty	Maturity Date	Notional	Fixed Rate	Fair Value
JPMorgan	Nov-2011	\$50M	5.549%	(\$2.6M)
JPMorgan	Jun-2012	\$40M	2.522%	(\$1.2M)
B of A	Jun-2012	\$40M	2.422%	(\$1.2M)
JPMorgan	Nov-2012	\$30M	5.655%	(\$3.0M)
JPMorgan	Nov-2012	\$40M	3.213%	(\$1.8M)
TOTAL		\$200M		(\$9.8M)

13. Committee Briefs: Quarterly Committee Education on Accounting Developments – Rebecca Beckham



13. Committee Briefs: Quarterly Committee Education on Accounting Developments – Rebecca Beckham

Accounting Treatment of Interest Rate Swaps

- As a not-for-profit company, ERCOT does not qualify for hedge accounting treatment. As such, all derivatives are marked-to-market on the Statement of Activities.
- The fair value is recognized on the Statement of Financial Position as a “Derivative liability” and is classified in Long-term liabilities.
- The change in fair value is recognized on the Statement of Activities as a “Change in valuation of interest rate swaps” and is classified as Other income (expense).
- Actual fixed rate payments (net of variable rate receipts) from the interest rate swap are recognized on the Statement of Activities as “Interest expense” and are classified as Other income (expense).
- A third-party valuation firm (DerivActiv) determines the fair value quarterly.
- Although not applicable to not-for-profit entities, the FASB and IASB have recently issued proposed changes to hedge accounting to reduce the complexity, make it more accessible to companies, and enable investors to better understand company’s risk management activities.

13. Committee Briefs: Financial Institutions That Are Market Participants – Cheryl Yager

<u>Market Participant</u>	<u>Financial Institution</u>	<u>Services Provided</u>
Bank of America, N.A. (also their subsidiary, Merrill Lynch)	Bank of America, N.A. or affiliate	Lender, bank account, money market funds
JPMorgan Ventures Energy Corporation	JPMorgan Chase, N.A. or affiliate	Lender, bank accounts, money market funds, purchasing card
<p><i>Note: ERCOT's 401(k) has mutual fund options that may include securities from these or other market participants.</i></p>		

13. Committee Briefs: Discussion of ERCOT's IRS Form 990 Filing

Mike Petterson

- ERCOT's 2010 IRS Form 990 is expected to be filed on August 15, 2011
- Preparation and filing of the informational tax return requires ERCOT Board members and some employees to complete a questionnaire
 - The questionnaire has been distributed as part of the March board materials
 - Completed questionnaires are due on April 19, 2011
- The Board will be given an opportunity to review the final draft of the 2010 IRS Form 990 at the July 19, 2011 meeting of the ERCOT Board of Directors

13. Committee Briefs: Handling of Complaints Regarding Financial Matters – Mike Petterson

- The Committee shall establish procedures for:
 - The receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters; and
 - The confidential, anonymous submission by the Company's employees of concerns regarding accounting or auditing matters
- Complaints regarding financial matters may be received through a variety of sources – direct, indirect, and anonymous alternatives are available
 - Employees receive training to ensure they are aware of these options
- Complaints are investigated as appropriate and reported to the Finance and Audit Committee or Board of Directors until resolved
- Evidence of complaints is retained in meeting minutes, investigative work papers, and systematically (e.g. the Ethics Point system) when possible

13. Committee Briefs: Hiring Former Employees of the Independent Auditor – Mike Petterson

- With respect to the independent auditors:
 - The Committee shall establish the Company’s hiring policies for employees who are former employees of the Company’s independent auditors.
- ERCOT will obtain Finance and Audit Committee approval before hiring a former employee of the Company’s independent auditor if -
 - The candidate was employed by the independent auditor for some time over the last twelve months, and
 - The former employee of the independent auditor was assigned to the ERCOT audit engagement for more than one month over the last twelve months, or
 - The former employee of the independent auditor will have responsibility for the work performed by the independent auditor after joining ERCOT

ERCOT

Finance and Audit Committee

2011 Annual Meeting Planner and Future Agenda Items

Task Description	Charter Page #	Month											
		J	F	M	A	M	J	J	A	S	O	N	D
1 Elect Committee officers and designate a secretary	2 & 7	A											
2 Review and assess adequacy of Committee charter	6	A	A										
3 Review and recommend investment standard	3			A									
4 Review and recommend financial standard	3			A									
5 Handling of complaints regarding financial matters	5			A									
6 Hiring former employees of the independent auditor	4			A									
7 Review and recommend credit standard	3			A									
8 Receive periodic report on Credit Work Group activity	na												
9 Approve Credit Work Group Charter	na			A									
10 Appoint Credit Work Group Chair and Vice Chair	na		A										
11 Review risk policies and risk management practices	6												
12 Undertake annual self-evaluation	8	A											
13 Periodic meeting with senior management	6												
14 Review and approve internal audit charter	6			A									
15 Periodic meeting with Chief Audit Executive	6 & 7	A	A	A									
16 Review internal audit reports	6	A	A	A									
17 Review Ethics Point issues	na	A	A	A									
18 Review effectiveness of internal audit functions	6												
19 Review and approve annual internal audit plan	6												
20 Review performance of the Chief Audit Executive	7												
21 Recommend selection of independent auditor	4												
22 Receive independence report from independent auditor	4												
23 Periodic meeting with independent auditor	5												
24 Discuss audited financial statements	5												
25 Review and accept financial statement audit	5												
26 Review and recommend proposed budget	3												
27 Review and recommend debt structure	3												
28 Review insurance coverage	na												
29 Review IRS Form 990	na												
30 Review and accept 401(k) audit report	6												
31 Review and accept SSAE 16 audit report	5			A									
32 Review Committee briefs	na	A	A	A									
33 Receive periodic investment report	na		A										
34 Receive periodic liquidity report	na			A									
35 Review major changes to accounting principles	5			A									
36 Review financial institutions - market participants	6			A									
37 Receive periodic Potential Future Exposure report	na												
38 Preapprove non-audit services	4	Performed on as-needed basis											
39 Review any report by independent auditor	4	Performed on as-needed basis											
40 Review effect of regulatory accounting initiatives	5	Performed on as-needed basis											
41 Review complaints regarding financial statements	5	Performed on as-needed basis											
42 Review press stories regarding financial statements	5	Performed on as-needed basis											
43 Periodic meeting with 401(k) auditor	na	Performed on as-needed basis											
44 Periodic meeting with SSAE 16 auditor	na	Performed on as-needed basis											
45 Review proposed audit of the nodal program	na		A										
46 Review credit procedures, practices, and judgments	na		A	A									

15. Other Business

Mike Petterson
