Date: July 12, 2011
To: Board of Directors
From: Clifton Karnei, Chair, Finance & Audit (F&A) Committee
Subject: Approval of Modifications to Standard Forms of Letter of Credit and Market Participant (MP) Guarantee Agreements

Issue for the ERCOT Board of Directors

ERCOT Board of Directors Meeting Date: July 19, 2011
Agenda Item No.: 9a

Issue:
The F&A Committee of the ERCOT Board of Directors (Board) requests that the Board approve revised versions of the standard forms of Letter of Credit, MP Guarantee Agreement and Foreign MP Guarantee Agreement (collectively, MP Guarantee Agreements).

Background/History:
Available Means of Financial Security Pursuant to Protocol Section 16.11.3
Pursuant to Protocol Section 16.11.3, *Alternative Means of Satisfying ERCOT Creditworthiness Requirements*, if a Counter-Party is required to provide Financial Security, then it may do so through one or more of the following means: (1) guarantee; (2) an unconditional, irrevocable letter of credit; (3) surety bond; and (4) cash. Items 1 – 3 are standard forms approved by the Board.

Recent History of Review of Standard Forms of Letter of Credit and MP Guarantee Agreements
Last year, the F&A Committee asked ERCOT staff to work with ERCOT's outside counsel on a regular basis in reviewing and, if necessary, proposing changes to MP Guarantee Agreements with the intent of adequately protecting ERCOT's interests. The F&A Committee also asked that the Credit Work Group (CWG) participate in the review process to allow for comments in furtherance of protecting MPs' interests. ERCOT staff included the standard form Letter of Credit in the review process since the last version was approved by the Board in October 2007. After working with MPs and consulting with ERCOT's outside counsel for several months, ERCOT staff submitted proposed redline drafts of the Letter of Credit and MP Guarantee Agreements to the CWG on May 25, 2011 for approval. Through an email vote which concluded on June 3, 2011, the CWG approved the revised versions of the standard forms of the Letter of Credit and MP Guarantee Agreements.

The modifications to the standard forms of the Letter of Credit and MP Guarantee Agreements were scheduled for discussion and vote at the June 2011 F&A Committee and Board meetings; however, these discussions and votes were deferred to the July 2011 F&A Committee and Board meetings to address additional questions by Board members. Since the June 2011 F&A Committee and Board meetings, ERCOT staff has answered the questions of the Investor Owned Utility Segment. ERCOT staff is scheduled to discuss questions of the Independent Generator Segment prior to the July 2011 F&A Committee and Board meetings. It is expected that the F&A Committee will recommend modifications to the standard forms of the Letter of Credit and MP Guarantee Agreements at its July 18, 2011 meeting.

Proposed Standard Form Agreements

The proposed standard forms of Letter of Credit and MP Guarantee Agreements are attached hereto, in red-lined format with changes identified, as follows:

- **Attachment A:** Letter of Credit;
- **Attachment B:** ERCOT Market Participant Guarantee Agreement (General Use);
- **Attachment C:** ERCOT Market Participant Guarantee Agreement (3rd Party);
- **Attachment D:** ERCOT Foreign Market Participant Guarantee Agreement (General Use); and
- **Attachment E:** ERCOT Foreign Market Participant Guarantee Agreement (3rd Party).

Proposed Primary Changes to the Standard Form of Letter of Credit

The primary substantive changes for the standard form Letter of Credit include the following: (1) broader demand and presentation language; (2) additional time for Beneficiary to present when Issuing Bank is not open for business on expiration/termination date; (3) addition of an evergreen provision; (4) addition of a corporate debt rating provision; and (5) addition of a termination provision. Other formatting and non-substantive changes were recommended as well.

Proposed Primary Changes to the Standard Form of MP Guarantee Agreements

The primary substantive changes for the standard form MP Guarantee Agreements include the following: (1) clarified additional Guarantor expressed waiver provisions; (2) addition of an evergreen provision; (3) addition of a Substitute Collateral provision; (4) added additional Guarantor representations and warranties; (5) added additional Guarantor covenant to provide financial information when requested; and (6) clarified assignment rights. Other formatting and non-substantive changes were recommended as well.

Key Factors Influencing Issue:

Although the current Board-approved versions of the standard forms of the Letter of Credit and MP Guarantee Agreements are adequate, these revised versions are recommended by ERCOT staff and CWG to provide MPs more flexibility in managing their financial security without weakening ERCOT's position. Overall, ERCOT staff believes that the new versions improve the current Board-approved versions of standard forms of the Letter of Credit and MP Guarantee Agreements.

Alternatives:

1. Accept the F&A Committee's expected recommendation, that is, to approve the proposed revised versions of the Letter of Credit and MP Guarantee Agreements as recommended by the F&A Committee.
2. Take no action and continue to use the current Board-approved Letter of Credit and MP Guarantee Agreements.
3. Instruct ERCOT staff to further revise the standard forms of the Letter of Credit and MP Guarantee Agreements based upon any additional directives from the Board.

Conclusion/Recommendation:

Accept the F&A Committee's expected recommendation, that is, to approve the proposed revised versions of the Letter of Credit and MP Guarantee Agreements as recommended by the F&A Committee.

ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.
BOARD OF DIRECTORS RESOLUTION

WHEREAS, after due consideration of the alternatives, the Board of Directors (Board) of Electric Reliability Council of Texas, Inc. (ERCOT) deems it desirable and in the best interest of ERCOT to approve revisions to the standard forms of the Letter of Credit and Market Participant Guarantee Agreements for US company Guarantors and Foreign company Guarantors.

THEREFORE, BE IT RESOLVED, that that the standard form Letter of Credit, which is attached hereto as Attachment A, is hereby authorized and approved in each and every respect to be accepted by ERCOT in accordance with the ERCOT Protocols.

RESOLVED FURTHER, that the Market Participant Guarantee Agreement (General Use Version), which is attached hereto as Attachment B, is hereby authorized and approved in each and every aspect to be accepted by ERCOT as the standard form guarantee agreement for qualified US company Guarantors in accordance with the ERCOT Protocols.

RESOLVED FURTHER, that the Market Participant Guarantee Agreement (3rd Party Version), which is attached hereto as Attachment C, is hereby authorized and approved in each and every aspect to be accepted by ERCOT as the standard form guarantee agreement for qualified US company Guarantors in accordance with the ERCOT Protocols.

RESOLVED FURTHER, that the Foreign Market Participant Guarantee Agreement (General Use Version), which is attached hereto as Attachment D, is hereby authorized and approved in each and every aspect to be accepted by ERCOT as the standard form guarantee agreement for qualified Foreign company Guarantors in accordance with the ERCOT Protocols.

RESOLVED FURTHER, that the Foreign Market Participant Guarantee Agreement (3rd Party Version), which is attached hereto as Attachment E, is hereby authorized and approved in each and every aspect to be accepted by ERCOT as the standard form guarantee agreement for qualified Foreign company Guarantors in accordance with the ERCOT Protocols.

CORPORATE SECRETARY'S CERTIFICATE

I, Bill Magness, Corporate Secretary of ERCOT, do hereby certify that, at its July 19, 2011 meeting, the ERCOT Board passed a motion approving the above Resolution by _____.

IN WITNESS WHEREOF, I have hereunto set my hand this ___ day of July, 2011.

_____
Bill Magness
Corporate Secretary