

ERCOT Finance & Audit Committee Meeting
7620 Metro Center Drive, Austin, Texas
Met Center, Conference Room 206
October 17, 2011; 12:30pm – 3:00pm*

Item #	Agenda Item Type	Description/Purpose/Action Required	Presenter	Time
		Call Open Session to order and announce proxies	Clifton Karnei	12:30pm
1.	Vote	Approve general session minutes (09/19/11)	Clifton Karnei	
2.	Discussion	Update on Commodities Exchange Act exemption	Mark Ruane	
3.	Vote	Recommend Board approval of revisions to ERCOT's Creditworthiness Standard	Cheryl Yager	
4.	Discussion	Receive report on auditor independence from Ernst & Young regarding the financial statement audit	Rebecca Beckham Ernst & Young	
5.	Discussion	Review and approve Finance and Audit Committee self-assessment questionnaire	Mike Petterson	
6.	Discussion	Review Committee briefs a. Credit statistics b. Exposure benchmark report c. Investment summary d. Risk stoplight report e. Audit activity	Mike Petterson	
7.	Discussion	Future agenda items a. Review December 2011 meeting matrix b. Review preliminary 2012 meeting matrix	Mike Petterson	
8.		Other business	Mike Petterson	
		Convene to Executive Session	Clifton Karnei	
9.	Vote	Approve executive session minutes (09/19/11)	Clifton Karnei	
10.	Vote	Contract, personnel, security, compliance, risk management, litigation and regulatory matters	Rebecca Beckham Leslie Wiley	
11.	Discussion	Chief Audit Executive status report	Bill Wullenjohn	
		Reconvene to Open Session	Clifton Karnei	
		Adjourn meeting	Clifton 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, December 12, 2011, at ERCOT, 7620 Metro Center Drive, Austin, Texas 78744, in Room 206.*

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

7620 Metro Center Drive, Room 206
Austin, Texas 78744
September 19, 2011 at 10:00 a.m.

Pursuant to notice duly given and after determination that a quorum was present, the meeting of the Finance and Audit (F&A) Committee of the Board of Directors (Board) of Electric Reliability Council of Texas, Inc. (ERCOT) convened on the above-referenced date.

Meeting Attendance:

Committee Members:

Director	Affiliation	Segment
Bermudez, Jorge (Vice Chairman)	Unaffiliated	Unaffiliated Director; Proxy for Calvin Crowder during Agenda Items 1-3
Crowder, Calvin	AEP Service Corp.	Investor Owned Utility (except for Call to Order, Agenda Items 1-3)
Dreyfus, Mark	Austin Energy	Municipal; Proxy for Clifton Karnei
Espinosa, Miguel	Unaffiliated	Unaffiliated Director
Hendrick, Eric	Stream Energy	Independent Retail Electric Provider (REP)

Guest Board Members and Segment Alternates:

Director	Affiliation	Segment
Bowling, Shannon	Cirro Energy	Independent REP Segment Alternate
Doll, Laura	Unaffiliated	Unaffiliated Director
Gent, Michehl	Unaffiliated	Unaffiliated Director

Other Guests:

Anderson, Kenneth	Commissioner, Public Utility Commission of Texas (except for Call to Order and Agenda Item 1)
Beckham, Rebecca	ERCOT Manager of Financial Reporting
Cleary, Mike	ERCOT Senior Vice President and Chief Operating Officer
Day, Betty	ERCOT Vice President of Business Integration
Dreyer, Jerry	ERCOT Vice President and Chief Information Officer
Ledy, Vickie	ERCOT Assistant General Counsel and Assistant Corporate Secretary
Magness, Bill	ERCOT Vice President, General Counsel and Corporate Secretary
Manning, Chuck	ERCOT Vice President of Human Resources and Chief Compliance

	Officer
Nikazm, Tamila	Austin Energy – Vice Chair of Credit Work Group
Petterson, Mike	ERCOT Vice President and Chief Financial Officer
Ruane, Mark	ERCOT Vice President of Credit and Enterprise Risk Management
Wullenjohn, Bill	ERCOT Director of Internal Audit
Yager, Cheryl	ERCOT Director of Credit

Call Open Session to Order and Announce Proxies

Jorge Bermudez, Committee Vice Chairman, acted as Chairman for this Committee meeting in Committee Chairman Clifton Karnei’s absence. Chairman Bermudez determined that a quorum was present and called the Committee meeting to order at approximately 10:09 a.m. Chairman Bermudez announced that he was holding a proxy for Calvin Crowder and that Mark Dreyfus was holding a proxy for Mr. Karnei.

Approval of August 15, 2011 Meeting Minutes (Agenda Item 1)

Chairman Bermudez entertained a motion to approve the August 15, 2011 Committee General Session Meeting Minutes (Minutes).

Mr. Dreyfus moved to approve the Minutes as presented. Eric Hendrick seconded the motion. The motion passed by unanimous voice vote with no abstentions.

Periodic Credit Work Group (CWG) Report (Agenda Item 2)

Tamila Nikazm provided a report from the CWG regarding an update on 2012 goals to the Committee members and responded to comments and questions from the Committee members.

ERCOT Credit Update (including discussion of ERCOT Recommendations regarding Point-to-Point (PTP) Obligations in the Upcoming Annual Congestion Revenue Rights (CRR) Auctions) (Agenda Item 3)

Cheryl Yager provided an update on ERCOT Credit to the Committee members and responded to comments and questions from the Committee members.

Update on Commodities Exchange Act Exemption (Agenda Item 4)

Mark Ruane provided an update on the Commodities Exchange Act Exemption to the Committee members. Mr. Ruane and Bill Magness responded to comments and questions from the Committee members.

Quarterly Committee Education on Accounting Developments (Agenda Item 5)

Rebecca Beckham provided a quarterly update on current accounting developments to the Committee members. Ms. Beckham and Bill Wullenjohn responded to comments and questions from the Committee members.

Review Committee Briefs (Agenda Item 6)

Mike Petterson reviewed the Committee briefs for the Committee members. No comments or questions were voiced by the Committee members.

Future Agenda Items (Agenda Item 7)

Mike Petterson reviewed the future agenda items for the Committee members. No comments or questions were voiced by the Committee members.

Other Business (Agenda Item 8)

No other business was discussed at this time.

Executive Session (Agenda Items 9 - 11)

Chairman Bermudez adjourned the meeting into Executive Session at approximately 11:30 a.m. and reconvened the Open Session at approximately 12:05 p.m.

Adjourn

Chairman Bermudez announced that the Committee had no other business to consider and adjourned the Committee meeting at approximately 12:07 p.m.

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

Vickie G. Leady
Assistant Corporate Secretary



Commodity Exchange Act Exemption Status

Mark Ruane

ERCOT Vice President of Credit and Enterprise Risk Management

Bill Magness

ERCOT Vice President, General Counsel and Corporate Secretary

Finance & Audit Committee Meeting

October 17th 2011

2. Commodity Exchange Act Exemption Summary

ERCOT is in the process of preparing an application for a Commodity Exchange Act exemption with the CFTC.

- ERCOT is continuing discussions with the CFTC with respect to the scope and terms of an exemption.
 - The filing date is not yet known.

2. Commodity Exchange Act Exemption

Expected CFTC Conditions for CEA Exemption

	Item	Status
1.	Two-day limit to cure collateral calls	No action necessary.
2.	Elimination of unsecured credit in CRR market	NPRR 400 filed (October Board review).
3.	Disallowance of netting between CRR and non-CRR markets	
4.	Reduce settlement timeline	<ul style="list-style-type: none"> • NPRR 347 combines invoices for day-ahead and real time markets (approved by Board in August). • NPRR 391 shortens settlement cycle by one day and eliminates Automated Clearing House (ACH) payments (October Board review).
5.	\$50m limitation on unsecured credit	Revision to Creditworthiness Standard approved by CWG on August 4 th . Requesting Board action at October Board meeting.
6.	Criteria for market participation	NPRR to be drafted as scope finalized.
7.	Become a central counterparty (CCP)	Request for IRS letter ruling to confirm tax-exempt status of CCP is pending.

2. Commodity Exchange Act Exemption Market Participant Risk Management Capability Verification

- **Participants and ISO/RTOs have expressed interest in developing common risk management standards and processes for use in all markets.**
 - ERCOT supports harmonization but this will depend on the outcomes of stakeholder processes.
- **ERCOT staff have met with counterparts at other ISO/RTOS to assess areas of commonality in the approach.**
- **ERCOT staff are providing input to the CCRO work group that is planning to put forward standards for risk management capabilities.**

2. Commodity Exchange Act Exemption Market Participant Risk Management Capability Verification

- **ERCOT staff support a ‘principles-based’ framework for capability assessment,**
 - Focus on general risk management best practices addressing sufficiency in areas such as governance, segregation of duties, reporting, etc.
 - Not specific methodologies, capabilities and reports,
- **Some participants have proposed standards that would differ depending on various Counter-Party characteristics, e.g.**
 - Hedger v speculator
 - Sophisticated v unsophisticated
 - Generator v integrated energy company

ERCOT staff believe that such distinctions may be difficult to define and manage and therefore recommends minimization of discrimination among Counter-Parties.

2. Commodity Exchange Act Exemption Market Participant Risk Management Capability Verification

- **Most ISOs have expressed interest in contracting the verification process out to third parties. Nevertheless, ERCOT will maintain ‘ownership’ of the results.**
- **Verification will likely be mandatory for some Market Participants above a risk threshold with some sampling of others below the threshold.**
- **Both the content of risk management standards and the process by which verification will take place are still being defined. The immediate priority is development of risk management standards.**
- **Stakeholders are encouraged to provide input to the CCRO standard development working group, although the CCRO report will not be binding on ERCOT.**

2. Commodity Exchange Act Exemption Central Counterparty Update

- **As previously noted to the Committee, ERCOT expects to seek Central Counterparty (CCP) status.**
- **ERCOT external counsel has indicated that, in their opinion, establishment of a CCP would be the cleanest way to ensure set-off across Day Ahead and Real Time markets in the event of bankruptcy.**
 - While ERCOT and its external counsel believe becoming a CCP will enhance its position in bankruptcy, no ISO has yet tested this in bankruptcy court

2. Commodity Exchange Act Exemption Central Counterparty Update

- **Considering the potential risks and alternatives, ERCOT staff does not believe that becoming a CCP will significantly increase risk to ERCOT, Inc. or its Market Participants.**
- **A subgroup of the CWG continues to explore the potential benefit to Market Participants of using a 3rd party as a CCP**



Recommend Revisions to the Creditworthiness Standard

Cheryl Yager

3. Recommend revisions to the Creditworthiness Standard Credit Work Group Recommendation

- **In conjunction with ERCOT seeking an exemption from CFTC regulations, the CWG reviewed the maximum credit limit allowed under ERCOT's Creditworthiness Standards.**
 - Current limit per ERCOT Creditworthiness Standard - \$100 million
 - ERCOT imposed limit - \$75 million
 - Other ISOs (as required by FERC Order 741d) - \$50 million
- **CWG voted to recommend that ERCOT reduce the maximum credit limit to \$50 million to:**
 - Reduce the overall credit risk in the ERCOT market
 - Make ERCOT credit policy more consistent with that of other ISOs
 - Meet CFTC expectations as we seek exemption from CFTC regulation

3. Recommend revisions to the Creditworthiness Standard

Anticipated impact of proposed revisions

As of August 31, 2011	<u>With \$75 million cap</u>		<u>With \$50 million cap</u>	
	Count	\$	Count	\$
Unsecured Credit	28	844,439,283	28	657,084,283
Guarantees	40	937,485,597	40	811,792,363
Total	68	1,781,924,880	68	1,468,876,646
Net reduction				313,048,234

3. Recommend revisions to the Creditworthiness Standard F&A Recommendation

- **ERCOT staff respectfully recommends that the Board approve the proposed change to the ERCOT Creditworthiness Standards as recommended by the CWG**
 - ERCOT recommends an implementation date of December 31, 2011 to allow Counter-Parties time to
 - obtain collateral, if needed, to replace unsecured credit or Guarantees and
 - execute new Guarantee documents.

<Vote>

Creditworthiness Standards for Cooperative and Municipal Systems

IF YOUR ENTITY HAS	AND	AND	AND	THEN
Minimum Equity (Patronage Capital)	Minimum Times Interest Earnings Ratio (TIER)	Minimum Debt Service Coverage (DSC)	Minimum Equity to Assets	Maximum unsecured line as a percentage of Unencumbered Assets*
\$25,000,000	1.05	1.00	0.15	0.00% to 5.00%

* Unsecured line not to exceed \$~~100~~50 million.

Unencumbered Assets is defined as Total Assets minus Total Secured Debt.

Note 1: Cooperatives shall apply these standards consistent with RUS [CFR Sec. 1717.656 (3)]. Municipals shall apply these standards annually.

Note 2: A Cooperative or Municipal must use "Rated Entity" standards for qualification if that entity is publicly rated by Fitch, S&P or Moody's and has greater than \$100 million in equity.

Note 3: The amount of unsecured line established within the range above is at the discretion of ERCOT if the above criteria are met.

Creditworthiness Standards for Rated Entities

IF YOUR ENTITY HAS		AND	THEN			
Long-Term or Issuer Rating		Tangible Net Worth greater than	Maximum unsecured line as a percentage of Tangible Net Worth*			
<u>Fitch or S&P</u>	<u>Moody's</u>					
AAA	Aaa	\$ 100,000,000	0.00%	to	3.00%	
AA+	Aa1	\$ 100,000,000	0.00%	to	2.95%	
AA	Aa2	\$ 100,000,000	0.00%	to	2.85%	
AA-	Aa3	\$ 100,000,000	0.00%	to	2.70%	
A+	A1	\$ 100,000,000	0.00%	to	2.55%	
A	A2	\$ 100,000,000	0.00%	to	2.35%	
A-	A3	\$ 100,000,000	0.00%	to	2.10%	
BBB+	Baa1	\$ 100,000,000	0.00%	to	1.80%	
BBB	Baa2	\$ 100,000,000	0.00%	to	1.40%	
BBB-	Baa3	\$ 100,000,000	0.00%	to	0.70%	
Below BBB-	Below Baa3	Requires Security				

* Unsecured line not to exceed \$~~100~~50 million

Tangible Net Worth is defined as Total Shareholder's Equity less Goodwill or other intangible assets.

Note 1: If a Market Participant's or Guarantor's debt is rated by more than one of the rating agencies and all ratings fall within rating categories which are functional equivalents, ERCOT shall assign unsecured credit or allow a guarantee for amounts within the range for that rating.

If a Market Participant's or Guarantor's debt is rated by more than one of the rating agencies and the ratings fall within different rating categories which are not functional equivalents, ERCOT shall assign unsecured credit or allow a guarantee for amounts as follows:

- If there are 3 ratings and 2 of the 3 are functional equivalents, within the range where 2 of the 3 ratings apply
- If there are 3 ratings and all 3 are different, within the range where the average of the 3 ratings apply (rounded down)
- If there are 2 ratings and the two are different, within the range of the lower of the two

Note 2: ERCOT has the discretion to reasonably request any entity to provide updated financial information and may adjust credit limits as required.

Note 3: The amount of unsecured line established within the range above is at the discretion of ERCOT if the above criteria are met.

Creditworthiness Standards for Privately-Held Entities

IF YOUR ENTITY HAS	AND	AND	AND	THEN
Tangible Net Worth		Minimum Current Ratio	Maximum Debt to Total Capitalization Ratio	Minimum EBITDA to Interest and CMLTD
100,000,000		1.0	0.60	2.0
				Maximum unsecured line as a percentage of Tangible Net Worth*
				0.00% to 1.80%

*Unsecured line not to exceed \$~~400~~ 50 million

Tangible Net Worth is defined as Total Shareholders' Equity less Goodwill or other intangible assets.

Debt to Total Capitalization Ratio is defined as Long-Term Debt (including all current borrowings) divided by Total Shareholders' Equity plus Long-Term Debt.

Note 1: An unsecured limit will be set for privately-held entities which do not have a long-term rating based on the above criteria, subject to the entity providing ERCOT with the most recent audited financial statements, and subsequent quarterly unaudited interim financial statements.

Note 2: ERCOT has the discretion to reasonably request any entity to provide updated financial information and may adjust credit limits as required.

Note 3: The amount of unsecured line established within the range above is at the discretion of ERCOT if the above criteria are met.

Entities not meeting the requirements established by the Protocols must provide one (or a combination) of the following forms of financial security for the benefit of ERCOT, as defined in the Protocols. Acceptance of financial security is subject to the review and approval of ERCOT.

1. **Cash Deposit** - standard form n/a

2. **Letter of Credit**

- a. Must be issued by a bank with a minimum rating of A- with Fitch or S&P or A3 with Moody's
- b. Must be issued on the Standard Form document approved by the Board of Directors

3. **Corporate Guarantee**

- a. Guarantor must meet applicable credit standards as stated in the ERCOT Protocols
- b. Guarantee must be on the Standard Form document approved by the Board of Directors

4. **Foreign Guarantee**

- a. Guarantor must meet applicable credit standards as stated in the ERCOT Protocols, as well as the standards listed below
- b. The country of domicile for the foreign guarantor must:
 - i. Maintain a sovereign rating greater than or equal to AA with Fitch or S&P or Aa2 with Moody's
 - ii. If the ratings are below those in (i) above, but greater than or equal to A with Fitch or S&P or A2 with Moody's, then the sovereign rating would qualify if the country had a ceiling rating of AAA with Fitch or S&P or Aaa with Moody's
 - iii. Must have reciprocity agreements with the U.S. regarding enforcement and collection of guarantee agreements
- c. The foreign guarantor must:
 - i. Provide to ERCOT annual audited financial statements, prepared in accordance with U.S. generally accepted accounting principles or international accounting standards and quarterly unaudited financial statements
 - ii. If the foreign guarantor does not provide quarterly financial statements, the assigned credit limit will be reduced based on their credit rating by:
 - 1. A- (Fitch or S&P) or A3 (Moody's) and above: 20%
 - 2. BBB+ (Fitch or S&P) or Baa1 (Moody's) or below: 50%
 - iii. Provide a guarantee in the form of the ERCOT Board approved standard form guarantee Agreement for foreign Entities
 - iv. Reimburse ERCOT the cost of obtaining an opinion of counsel affirming that the guarantee agreement is enforceable in the U.S. and in the jurisdiction of the corporate guarantor's domicile
 - v. Maintain a registered Texas Registration Agent

5. **Surety Bond**

- a. Must be issued by an insurance company with a minimum rating of A- with Fitch or S&P or A3 with Moody's
- b. Subject to a limit of \$10 million per QSE per insurer and an overall limit of \$100 million per insurer for all ERCOT QSEs

Revisions to the Creditworthiness Standards shall be reviewed by the Credit Work Group and the Finance and Audit Committee and approved by the ERCOT Board.

4. Review of External Auditor Independence and Financial Statement Audit Plan- Rebecca Beckham

- **The F&A Charter states that “at least annually, the Committee shall obtain and review a report by the independent auditor describing (a) the independent auditor’s internal quality control procedures and (b) all relationships between the independent auditor and the Company, in order to assess the auditor’s independence.”**
- **In Executive session, agenda item 10, management recommends that the Committee appoint Ernst & Young LLP as the independent audit firm for the 2011 financial statement audit.**
- **Accordingly, Ernst & Young LLP will present their 2011 financial statement audit plan and provide an update on their independence.**



Electric Reliability Council of Texas

2011 financial statement audit plan





October 5, 2011

The Finance and Audit Committee

Electric Reliability Council of Texas

Dear Members of the Finance and Audit Committee,

On October 17, 2011, we are meeting with you to discuss our audit approach and current year audit plan for ERCOT. We will outline the scope of our services, that will serve you and present some key considerations that will affect the 2011 audit. We are providing the enclosed materials so you can familiarize yourselves with them prior to our meeting.

Our audit is designed to express an opinion on the 2011 consolidated financial statements as of December 31, 2011. We are currently completing the planning phase of our audit. We will consider ERCOT's current and emerging business risks, assess those that could materially affect the financial statements and align our procedures accordingly. The plan will be responsive to your needs and will maximize audit effectiveness so we can deliver the high quality audit you expect.

We appreciate the opportunity to serve ERCOT for the 2011 audit. Our commitment to quality will be reflected in every aspect of our work.

A handwritten signature in black ink, appearing to read 'Philip J. Gunn'.

Philip J. Gunn

Partner

Agenda

Deliverables

Key areas of audit emphasis

Fraud considerations and the risk of management override

Appendix A - PCAOB updates

Appendix B - Independence

Appendix C - Timing of required communications

Deliverables

Audit deliverables	
Opinion	▶ Express an opinion on the consolidated financial statements of ERCOT
Internal control communications	▶ Issue a written communication to management and the audit committee describing significant deficiencies and material weaknesses , if any, identified during our audit ▶ Issue a management letter, if appropriate, that provides our recommendations regarding internal controls and opportunities for improvement or efficiency, based on observations made during the course of our audit

Note: Fees for the 2011 audit engagement were previously agreed upon in August 2009 as part of a three year fee arrangement. Fees for 2011 audit are anticipated to range from \$93,500 to \$110,500 based on a composite rate of \$170 per hour.

Key areas of audit emphasis

Key areas of audit emphasis include:

- Revenue recognition - EY to test Entity's revenue recognition procedures, incorporating Service Organization Report (SOC)
- Cash - EY to test cash and restricted cash accounts associated with significant increase in balances (higher market participant exposure under Nodal).
- Nodal- EY will test Nodal as a depreciating asset, including reviewing proper depreciable lives.
- Long-term debt (including LOC and interest rate swaps)
- Regulatory liabilities

Fraud considerations and the risk of management override

We are responsible for planning and performing the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or by fraud (SAS No. 99, *Consideration of Fraud in a Financial Statement Audit*).

Our audit procedures will encompass the requirements of SAS 99: brainstorming, gathering information to facilitate the identification of and response to fraud risks and performing mandatory procedures to address the risk of management override (including examining journal entries, reviewing accounting estimates and evaluating the business rationale of significant unusual transactions).

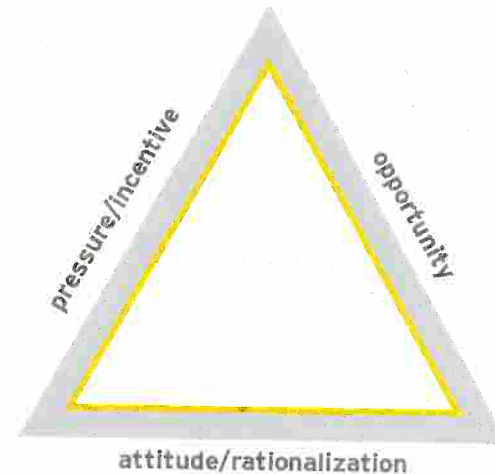
We evaluate the risk of fraud, including the risk of management override, using the fraud triangle and consider the actions management has taken to respond to those risks.

We consider, among other things:

- Code of conduct/ethics
- Effective and independent oversight by audit committee
- Process for dealing with whistle-blower allegations
- Adequacy of internal audit oversight of activity
- Entity's risk assessment processes

Role and oversight responsibilities of the audit committee:

- Management's assessment of the risks of fraud
- Programs and controls to mitigate the risk of fraud
- Process for monitoring multiple locations for fraud
- Management communication to employees on its views on business practices and ethical behavior



Occupational Fraud and Abuse, by Joseph T. Wells, CPA, CFR
(Obsidian Publishing Co, 1997);
Fraud Examination, by W. Steve Albrecht (Thomson South-Western Publishing, 2003)

Appendix A

PCAOB Updates

PCAOB developments

In recent months, the PCAOB has signaled that it is intensifying its focus on auditor oversight. The ideas expressed by the PCAOB have important implications to the audit profession, audit committees and to the issuers themselves. Following is a summary of key PCAOB developments and our observations.

PCAOB consideration	Observations
Auditor's Reporting Model	
<ul style="list-style-type: none"> ▸ The PCAOB has been evaluating whether changes are needed to the auditor's report to provide investors with additional information. Ideas being considered include: <ul style="list-style-type: none"> ▸ Inclusion of auditor's discussion and analysis (AD&A) ▸ Expanded use of emphasis paragraphs ▸ Report on information outside of the financial statements ▸ Clarification of certain language in current reports 	<ul style="list-style-type: none"> ▸ The Center for Audit Quality (CAQ) - representing the US auditing profession - wrote to the PCAOB to suggest enhancements to the auditor's report. ▸ We support the principles of the CAQ's letter, including that auditors should not be the original source of disclosure about the company and changes to the reporting model should narrow - or at least not expand - the expectations gap. ▸ We are concerned with the subjective nature of a number of the potential topics that could be included in an AD&A and the potential for such disclosures to compete with information provided by the Company. ▸ We are also concerned with the potential effect various alternatives may have on the auditor's relationship with management and the audit committee.
Mandatory Audit Firm Rotation	
<ul style="list-style-type: none"> ▸ The PCAOB has stated "the payment model is an inherent challenge to independence and objectivity as the auditor is hired and fired by the Company itself." On 16 August 2011, the PCAOB issued a concept release seeking comment on mandatory audit firm rotation. 	<ul style="list-style-type: none"> ▸ We believe audit committees and boards, representing the interests of shareholders, should be free to appoint the audit firm that best meets their needs at the time they believe appropriate. ▸ We do not believe mandatory audit rotation will improve audit quality. In fact, it could threaten audit quality because it erases the cumulative knowledge an audit firm builds over time and diminishes the resources and industry knowledge available to the auditor. ▸ Existing audit partner rotation rules and independence requirements, as well as natural personnel turnover, keep relationships between the audit firm and the audit client fresh and appropriately independent.

PCAOB developments cont.

PCAOB consideration	Observations
Auditor Independence and Professional Skepticism - Non-audit Services	
<ul style="list-style-type: none"> The PCAOB has expressed concern that auditors too often fail to exercise an effective level of skepticism in the audit. The PCAOB has noted that the pressure auditors face both from within the firm and from companies may contribute to failures to exercise the required level of skepticism. In its concept release on mandatory audit firm rotation, the PCAOB is seeking comment on whether such a requirement would help insulate auditors from these pressures. 	<ul style="list-style-type: none"> For a variety of reasons, including the rigorous oversight of the profession, we do not believe that there is a pervasive weakness across the profession related to the exercise of an appropriate level of professional skepticism. We believe confidence in the audit profession is built on independence and audit committees are best situated to provide oversight to auditor independence. We do not believe the provision of non-audit services by the auditor should be prohibited. We believe that delivering the most complete range of permissible services increases a firm's knowledge of the company and its risks and processes, all of which contribute to audit quality.
Transparency of the Audit	
<ul style="list-style-type: none"> The PCAOB is looking for ways to enhance audit committees' and investors' understanding of the audit. In addition to the concepts proposed related to the auditor's reporting model, it is exploring ways to increase the transparency of the participants in the audit to assist investors and audit committees in making more informed decisions about how to use the audit report. As such, the PCAOB has suggested enhanced transparency of the partner in charge of the audit as well as information regarding how cross-border audits are conducted. 	<ul style="list-style-type: none"> While the partner in charge of the audit is ultimately responsible for the decisions made in the audit process, the audit itself is conducted by a team of professionals who are subject to the firm's system of quality control, which includes processes for training, staffing, independence and audit methodology - all of which the partner in charge relies upon in order to perform the audit. Given the audit committee's oversight role and the significant role a firm's system of quality control contributes to the quality of an audit, we do not believe that identifying the partner in charge of the audit in the auditor's report or elsewhere in the company's filing with the SEC, provides useful information to investors. The profession has proposed to include in the audit report, where applicable, a description of the accounting firm's network structure involved in the execution of the audit and the extent (in terms of the percentages of consolidated assets, revenues and income) of such member firms' participation.

PCAOB developments cont.

PCAOB consideration	Observations
Communication with audit committees on PCAOB Inspection Findings	
<ul style="list-style-type: none">▶ The PCAOB has expressed concern that some accounting firms may not be fairly portraying the results of audit inspections. To address this concern, the PCAOB is exploring ways to better inform audit committees about the inspection process and results.	<ul style="list-style-type: none">▶ We support efforts by the PCAOB to better inform audit committees about the PCAOB's inspection process. At the same time, we believe it is important that inspection findings are presented in a balanced manner and include the appropriate context.▶ We provide audit committees with a summary of the public portion of each annual inspection report we receive from the PCAOB and frequently share the full public portion of the report.▶ In situations where specific engagements have been included in the PCAOB's report available to the public and we agree with the PCAOB's findings, we remediate such engagements.
Recent Inspection Experiences	
<ul style="list-style-type: none">▶ We undergo rigorous annual inspections from the PCAOB. As a result of the inspections we often enhance our policies and procedures to respond to expressed concerns and recommendations of PCAOB staff. Typically, such activities include additional training, additional mandated audit procedures, changes to our guidance or revisions to our tools or enablers.	<ul style="list-style-type: none">▶ We are supportive of efforts that improve audit quality▶ Areas of recent inspection focus include:<ul style="list-style-type: none">▶ Internal control testing and level of precision of controls▶ Reserves, such as sales returns and promotional allowances▶ Investments▶ Business combinations and impairments▶ Strength of internal audit functions and reliance thereon▶ Some of these areas have recently resulted in changes to our guidance that are responsive to the PCAOB's interpretations of professional standards. Additional changes will likely result during the year, which will generally require additional audit effort.▶ There may be implications on certain issuers from inspections

Appendix B

Independence

The independence landscape

Auditor independence rules are founded on four general principles - that auditors and their clients engage in no relationship or provision of service that, in either fact or appearance:

- Creates a mutual or conflicting interest between the auditor and the audit client
- Places the auditor in the position of auditing his or her own work
- Results in the auditor acting as management or an employee of the audit client
- Places the auditor in a position of being an advocate for the audit client

Based on these general principles, independence rules can be summarized within two categories: Relationships and Services

Relationships

- ▶ *Financial Relationships* - prohibits auditors and certain family members from investments in, and other types of financial relationships with, an audit client
- ▶ *Employment Relationships* - prohibits auditors and certain family members, and retired partners, from entering into certain employment or directorship arrangements with an audit client
- ▶ *Business Relationships* - prohibits auditors from having business relationships with an audit client, or any person associated with the audit client in a decision-making capacity, unless the relationship is for the provision of professional services or the auditor is a consumer in the ordinary course of business

Services

- ▶ *Non-Audit Services* - prohibits auditors from providing certain non-audit services to audit clients
- ▶ *Contingent Fees* - prohibits auditors from charging audit clients a contingent fee or a commission for any service
- ▶ *Partner Compensation* - prohibits audit partner compensation to be based on selling non-audit services to audit clients

We are not presently aware of any relationships or services with ERCOT that may reasonably be thought to bear on our independence. We will complete our independence procedures near the completion of our audit in March, 2012

Ernst & Young's focus on independence

Independence is fundamental to EY, our audit clients, and the public interest. Our approach to maintaining independence includes implementing policies, processes and systems with both "prevent" and "detect" type controls to provide reasonable assurance that a breach of independence will not occur and, in the event one does, will not go undetected nor unremediated. We proactively reexamine, monitor and test our policies, processes and systems so that they are current, thorough and effective. We reinforce our policies, processes and systems through continuous independence training of our professionals. We continually reinforce to all our people that compliance with our independence policies is essential, and that non-compliance has consequences.

Independence Organization

- ▶ Global network of independence leaders in every country where we operate
- ▶ Independence specialists support the global network
- ▶ Clear accountability - centralized independence functions report to Global Managing Partner - Quality and Risk Management (Q&RM) and Americas Vice Chair - Q&RM

Independence Processes and Systems

- ▶ Monitoring of compliance with our firm's independence requirements relating to matters such as investment holdings, lending relationships and family employment relationships, which are periodically confirmed by our professionals
- ▶ Monitoring business relationships between EY and our audit clients and their officers, directors, and substantial shareholders
- ▶ Maintaining and periodic updating of audit client subsidiary and affiliate information
- ▶ Detailed programs and procedures to assert independence in connection with client acceptance, IPOs and issuance of independence letters under PCAOB Rule 3526
- ▶ Consultation processes and documented conclusions

Independence Policies

- ▶ EY Global independence policies based on International Federation of Accountants (IFAC) and SEC rules
- ▶ Issued a comprehensive independence manual with rules all in one place
- ▶ A Code of Conduct that highlights the importance of maintaining our objectivity and independence and with which our personnel are required to confirm their compliance annually

Independence Training and Compliance

- ▶ Mandatory, continuous independence training for all professionals globally
- ▶ Independence content is included in many other core learning and industry related programs
- ▶ Conducting ongoing compliance audits of partners and other professionals regarding personal independence
- ▶ Global Independence Compliance Team focused on scope of services and business relationships

Appendix C

Timing of required communications

Timing of required communications

	Communicate when event occurs	Communicate on a timely basis, at least annually
Our responsibility under generally accepted auditing standards, including (in our Audit Results Template) discussion of the type of opinion we are issuing		X
Overview of planned scope and timing		X
Other information in documents containing audited financial statements		X
Our views about the qualitative aspects of the Company's significant accounting practices, including:		
• The appropriateness of accounting policies to the particular circumstances of the Company including, the adoption of, or a change in, an accounting policy	X	
• The effect of significant accounting policies in controversial or emerging areas	X	
• Significant accounting estimates		X
• Financial statement disclosures and related matters		X
Significant difficulties encountered in dealing with management when performing the audit	X	
Uncorrected misstatements		X
Material corrected misstatements		X
Disagreements with management	X	
Representations we are requesting from management		X

Timing of required communications

	Communicate when event occurs	Communicate on a timely basis, at least annually
Management's consultations with other accountants	X	
Significant issues, if any, arising from the audit that were discussed, or the subject of correspondence, with management	X	
Communication of independence matters	X	
Fraud and illegal acts involving senior management and fraud and illegal acts that cause a material misstatement of the financial statements	X	
Significant deficiencies and material weaknesses in internal control		X
AICPA ethics ruling regarding third-party service providers		X
Other findings or issues regarding the oversight of the financial reporting process	X	

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5. 2011 Committee member self-evaluation survey

Mike Petterson

- **Finance and Audit Committee charter requires members to undertake an annual self-evaluation of the Committee's activity and effectiveness**
- **Self-evaluation will be conducted through web-based survey questions to be distributed soon after the October meeting of the Committee**
- **Seeking Finance and Audit Committee confirmation that the survey questions detailed on the following pages are acceptable.**

	ERCOT Finance & Audit Committee Self-Evaluation 2011	Yes	No	Not Sure	Comments
1.	Does the committee have the appropriate number of members? The committee should not be so large that: <ul style="list-style-type: none"> ▪ its ability to operate efficiently and effectively is reduced ▪ members' ability to raise issues is hampered ▪ it is difficult to get a quorum when a time-sensitive issue arises 				
2.	Committee members demonstrate their objectivity during meetings through behaviors such as driving agendas, rigorous probing of issues, consulting with other parties, and hiring experts, as necessary.				
3.	Differences of opinion on issues are resolved to the satisfaction of the committee.				
4.	Committee members challenge the Chair as appropriate.				
5.	The committee charter is used as a document to guide the committee in its efforts, and to help guide the committee's agenda.				
6.	6.1 Committee members are financially literate, and the committee has determined that it has adequate financial expertise in accordance with its charter.				
	6.2 Committee members participate in some form of continuing education to stay abreast of changes in the financial accounting and reporting, regulatory and ethics areas.				
	6.3 The committee understands how the organization's performance compares with its budgetary targets and its peers, and how management plans to address any unfavorable variances.				
	6.4 The committee discusses the initial selection of or changes in significant accounting policies used in developing the financial statements, the reason for and impact of any changes in policy, and reasons alternative treatments were not adopted.				

	ERCOT Finance & Audit Committee Self-Evaluation 2011	Yes	No	Not Sure	Comments
	6.5 The committee discusses significant, complex, or unusual transactions with management and the external auditors.				
	6.6 The committee understands which areas represent high risk for material misstatement of the financial statements, and discusses assumptions and approaches used with management and the external auditors.				
	6.7 The committee forms its own view of the risk of material misstatement due to fraud, discusses with management and the external auditors their views on the risk of material misstatement due to fraud, and is comfortable that any differences in views can be reconciled.				
	6.8 The committee fully understands significant changes in financial statements from prior years and from budget, and is provided with sufficient, reliable evidence to support variances.				
	6.9 The committee commits sufficient time to review, discuss, and consider the financial statements.				
	6.10 The committee makes optimum use of the meeting time allotted.				
	6.11 The committee meets with financial management to discuss results reported before finalization.				
7.	Committee members have a clear understanding of ERCOT's debt structure and cash management practices.				
8.	Committee members receive sufficient details regarding long-term financial planning.				
9.	The Committee makes appropriate use of workgroups or task forces to investigate issues defined by the Committee.				
10.	The committee engages outside experts as appropriate.				
11.	11.1 The organization's financial reporting processes are stronger as a result of management's interactions with the committee.				

	ERCOT Finance & Audit Committee Self-Evaluation 2011	Yes	No	Not Sure	Comments
	11.2 The committee understands and agrees with the board on which categories of internal control it oversees. Categories include: <ul style="list-style-type: none"> ▪ Integrity of financial reporting ▪ Compliance with laws and regulations ▪ Operational efficiency and effectiveness 				
	11.3 The committee and the board concur with any changes to the committee's internal control oversight mandate.				
	11.4 The committee understands the current high-risk areas - including information technology and computer systems - in the categories of controls it oversees, as well as how management addresses those areas.				
12.	The committee is cognizant of the line between oversight and management, and endeavors to respect that line.				
13.	The committee conducts executive sessions in a manner that offers a "safe haven" to the individual, while at the same time asking tough and necessary questions, evaluating the answers, and pursuing issues that might arise to a satisfactory resolution.				
14.	14.1 The committee does its part to ensure the objectivity of the internal audit team.				
	14.2 The committee provides constructive feedback to the chief audit executive at least annually.				
	14.3 The committee receives sufficient detail regarding material issues and complaints brought forward which relate to the company's fraud, ethics or accounting practices.				

	ERCOT Finance & Audit Committee Self-Evaluation December 2007	Yes	No	Not Sure	Comments
	14.4 The committee has developed the scope of work to be done by the independent auditor and by the internal audit department based upon a reasoned review of the risks or exposures to the company.				
15.	The committee communicates at an appropriate level of detail when informing the Board of its actions.				
16.	Committee members receive clear and succinct agendas and supporting written material sufficiently prior to scheduled meetings.				
17.	Committee members have adequate opportunities to discuss issues and ask questions.				
18.	The frequency of committee meetings is appropriate for the responsibilities assigned to the committee.				
19.	Meeting facilities and presentation materials are effective for the conduct of committee activities.				
20.	The committee is efficient and value adding.				
21.	Please add additional comments, questions and suggestions here.				

6. Committee Brief: Market Credit Statistics

Cheryl Yager

ERCOT Market Credit Status

as of 8/31/2011					as of 9/30/2011					
	# of CPs*	Total Potential Exposure (\$)	% of TPE	Total Credit Limit		# of CPs*	Total Potential Exposure (\$)	% of TPE	Total Credit Limit	
Exposure in the ERCOT Market (owed to ERCOT)										
<u><i>QSEs that meet ERCOT Creditworthiness Standards</i></u>										
Ratings over BBB-	9	60,791,282	4%	581,394,409	U	11	114,553,308	9%	540,318,948	U
<u><i>QSEs that do not meet ERCOT Creditworthiness Standards</i></u>										
Ratings below BBB- or not rated										
Cash & Letters of Credit	77	1,075,230,733	73%	2,111,279,463	S	81	836,673,826	67%	1,598,544,179	S
Guarantee Agreements	27	347,050,637	23%	815,138,034	S	29	289,264,126	23%	884,154,486	S
Total Exposure	113	1,483,072,652	100%	3,507,811,906		121	1,240,491,260	100%	3,023,017,613	
Other QSEs in the ERCOT Market (ERCOT owes)										
<u><i>QSEs that meet ERCOT Creditworthiness Standards</i></u>										
Ratings over BBB-	19	(1,108,799)	-5%	263,044,874	U	17	(249,650)	-16%	290,350,602	U
<u><i>QSEs that do not meet ERCOT Creditworthiness Standards</i></u>										
Ratings below BBB- or not rated										
Cash & Letters of Credit	87	(21,752,414)	-95%	83,761,021	S	86	(1,281,391)	-84%	59,308,487	S
Guarantee Agreements	13	-	0%	122,347,563	S	10	-	0%	70,497,563	S
Total	119	(22,861,214)	-100%	469,153,458		113	(1,531,040)	-100%	420,156,652	
Total	232	1,460,211,438		3,976,965,364		234	1,238,960,220		3,443,174,265	

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 a QSE's collateral requirements by entities that do not meet ERCOT's Creditworthiness Standards are not included on this schedule.

Note 2: As a result of the high prices in August 2011, TPE increased by approximately \$0.8 billion, more than double the TPE at July 31, 2011. To cover this exposure, Counter-Parties increased collateral by approximately \$1.2 billion. Both TPE and collateral levels have come down in September and are expected to continue to moderate in October / November as August activity rolls out of the ADTE calculation.

6. Committee Brief: Summary Exposure Benchmark Report Cheryl Yager

Summary Benchmark Report as of September 30, 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	94	-	-				3,590	3,537	5,994
w/ Load and/or Generation	55	536,170	478,650				145,372	49,843	345,966
Total	149	536,170	478,650	64%	54%	47%	148,962	53,380	351,960
Above High									
w/ No Load and No Generation	34	-	-				94,320	7,661	9,334
w/ Load and/or Generation	45	443,622	508,807				995,173	94,719	424,661
Total	79	443,622	508,807	34%	44%	50%	1,089,492	102,380	433,995
Below Low									
w/ No Load and No Generation	2	-	-				(311)	-	-
w/ Load and/or Generation	4	21,068	21,310				817	2,731	37,921
Total	6	21,068	21,310	3%	2%	2%	506	2,731	37,921
Total as of September 30, 2011	234	1,000,860	1,008,768	100%	100%	100%	1,238,960	158,491	823,877
Total as of August 31, 2011	232	1,220,806	1,232,801				1,460,211	474,532	2,537,824

6. Committee Brief: Summary Exposure Benchmark Report

Cheryl Yager

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 - \$150	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 - \$150	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 - \$150	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	Avg real time price - floor - \$25, cap - \$150	1.5
Counter-Parties - Generation only	Outstanding receivable/payable - invoiced and estimated	Highest total generation volume over past 30-days	6	0.2	Avg real time price - floor - \$25, cap - \$150	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	Avg real time price - floor - \$25, cap - \$150	1.5
		Highest DAM sales volume over past 30-days	2	1.0	Avg real time price - floor - \$25, cap - \$150	1.5


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

6. Committee Brief: Investment Report Leslie Wiley

Summary of Investments 9/31/2011

<u>Counter Party</u>	<u>Treasury</u>	<u>Treasury and Treasury Repo</u>	<u>Total Invested</u>	<u>Percentage of Investments</u>
	<small>\$ millions</small>			
Goldman Sachs	\$ 50.0		\$ 50.0	10%
Western Asset	50.0		50.0	10%
Fidelity	49.0	1.0	50.0	10%
Wells Fargo	44.0	6.0	50.0	10%
Morgan Stanley		50.0	50.0	10%
Federated	29.1	20.8	49.9	10%
BlackRock	34.0	15.9	49.9	10%
Invesco		49.7	49.7	10%
SSgA	49.4		49.4	10%
JPMorgan		49.4	49.4	10%
Bank of America		1.0	1.0	0%
UBS		0.2	0.2	0%
Total	\$ 305.5	\$ 194.0	\$ 499.5	100%

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

Strategic	Operational Excellence	Market Facilitation	Grid Reliability	Reporting	Legal and Regulatory Compliance
<p>1 Strategy Development</p> <p><i>Corporate objective setting adequately incorporates informed stakeholder input, market realities and management expertise.</i></p>	<p>1 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>1 Market Operations</p> <p><i>Effectively manage the evolution of the wholesale and retail markets to meet the changing business environment.</i></p>	<p>1 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>1 Review Practices</p> <p><i>Prudent measures are taken to insure that company disclosures are properly vetted and not misleading.</i></p>	<p>3 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>1 Mission and Goals</p> <p><i>Corporate objectives and performance standards are understood and followed.</i></p> <p>Strategic Plan has been approved since July of 2010 . Proposed 2011 KPIs under review by HR&G Committee.</p>	<p>1 Business Practices</p> <p><i>Business planning, processes and management standards are effective and efficient.</i></p>	<p>2 Nodal Systems Stabilization</p> <p><i>Manage the deployment and stabilization of the nodal market systems</i></p>	<p>2 Planning</p> <p><i>Long-range planning methods enable efficient responses to system changes that are necessary to maintain reliability standards.</i></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>1 Disclosure</p> <p><i>Reporting and other disclosures to intended parties is timely, accurate and effective.</i></p>	<p>3 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>A limited SAS 70 Audit was completed in January (Type I). No control issues were identified. Testing for the SSAE16 audit is underway. No issues have been identified to date.</p>
<p>3 Reputation</p> <p><i>Positive perceptions by stakeholders lead to less cost and greater flexibility resulting in enhanced enterprise value.</i></p> <p>Increased visibility of ERCOT during recent series of EEA events.</p>	<p>3 Workforce</p> <p><i>Organization design, managerial and technical skills, bench strength and reward systems aligned with corporate goals.</i></p> <p>Employee retention risk likely to increase if economy continues to improve.</p>	<p>3 Counterparty Credit </p> <p><i>Maintain credit risk exposure for overall market within acceptable limits.</i></p> <p>Work is proceeding on the CFTC application for the CEA exemption. Reduced level due to credit impact of reversion to lower prices.</p>	<p>4 Bulk System Resources</p> <p><i>Market Participants construct and make available adequate bulk electric grid resources.</i></p> <p>Elevated due to ongoing impact of drought and potential impact of EPA Cross-State Air Pollution Rule.</p>	<p>2 Communication</p> <p><i>Internal & external communications are timely and effective.</i></p> <p>An updated external communications plan has been issued following the February Energy Emergency Alert.</p>	<p>3 Industry Standards</p> <p><i>Business and operational activities in compliance with all applicable regulatory, financial & accounting requirements, standards, & directives.</i></p> <p>Compliance is believed to be on target for 'spot checks' of CIP compliance later in 2011.</p>
<p>1 Fiscal Management</p> <p><i>ISO design requires competent, prudent and cost effective provision of services.</i></p>	<p>1 Technology Infrastructure</p> <p><i>Information systems, supporting facilities and data are effectively managed and are reliable.</i></p>	<p>1 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>3 Operational Responsibility</p> <p><i>Market participant conduct their operations in a manner which facilitates consistent grid reliability.</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 the issues.</p>	<p>1 Adequacy and Integrity</p> <p><i>Robust processes exist to support management assertions embodied within financial reports.</i></p>	<p>1 Regulatory Filings</p> <p><i>Evidence, testimony and other supporting materials are compelling and successful.</i></p>

Notes:

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

Elevated risk level indicated by (↑). Reduced risk level indicated by downward green arrow (↓).

Numbers correspond to colors as follows:

Red - 5

Red-Yellow - 4

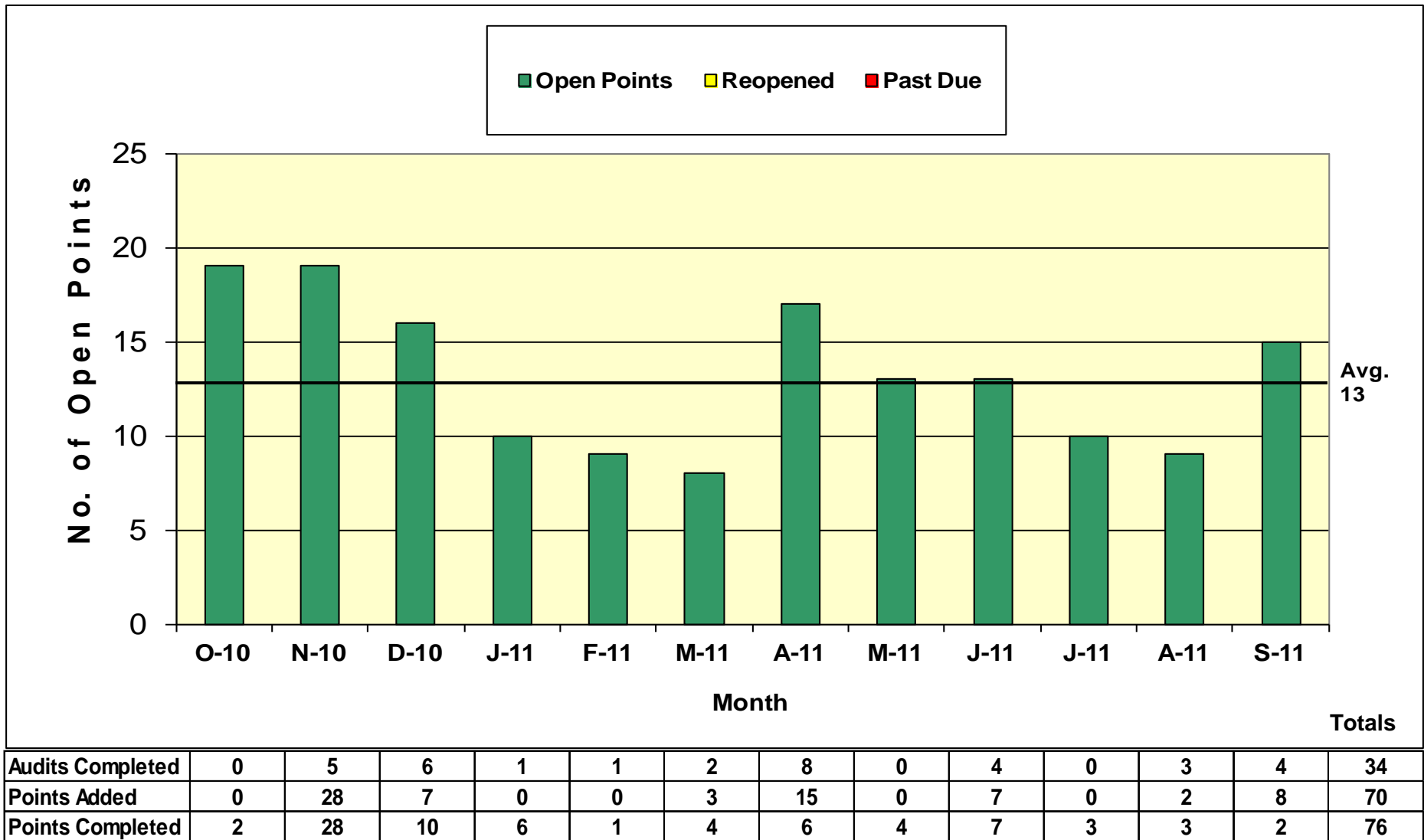
Yellow - 3

Yellow - Green - 2

Green - 1

6. Committee Brief: Status of Open Audit Points

Cheryl Moseley



Audits Completed	0	5	6	1	1	2	8	0	4	0	3	4	34
Points Added	0	28	7	0	0	3	15	0	7	0	2	8	70
Points Completed	2	28	10	6	1	4	6	4	7	3	3	2	76

All audit points except three expected to be complete by 1/31/12.

6. Committee Brief: Audit Activity

Cheryl Moseley

Audits Completed

(last 3 months)

Internal Audits

- Q2 Fraud Auditing
- Nodal Program Bonus Procedures (Special Request)
- ControlPath System
- WAN Management Fee Proposal (Special Request)
- Data Center Procurement
- Internal Control Self Assessment Process
- Assessment of Completed Projects
- Cash and Investments

External Audits

- 401K Benefit Plan (Maxwell, Locke & Ritter)

Audits in Progress

Internal Audits

- Business Continuity Plan and Disaster Recovery
- Storage and Capacity Planning
- Nodal Program Bonus Payments (Special Request)
- Q3 Fraud Auditing
- Enterprise Risk Management (Consulting/Advisory)
- Business Integration Testing

External Audits

- 2011 Type 2 SSAE 16 (SAS 70) Audit (BrightLine CPAs & Associates, Inc.)
- Nodal Program Audit (Navigant Consulting, LLC)

Planned Audits

(next 3 months)

Internal Audits

- Protocol 1.4 Required Audit – Ethics (Employee & Contractor Ethics)
- Market Credit

External Audits

- None

6. Committee Brief: 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

- None

6. Committee Briefs: NPRRs with Credit Implications

- **Two NPRRs with credit implications will be at the October 2011 BOD meeting for approval**
 - Additional background information is provided in the following slides for
 - NPRR 391 - Shortening RTM Settlement and Payment Timeline and Eliminate ACH as a Mode of Payment
 - NPRR 400 - Eliminate Unsecured Credit for CRR Auctions and for Future Credit Exposure (FCE) and Eliminate Netting of FCE with CCE
- **Both ERCOT staff and CWG endorsed the above NPRRs**

6. Committee Briefs: NPRRs with Credit Implications

- **NPRR 391 - Shortening RTM Settlement and Payment Timeline and Eliminate ACH as a Mode of Payment**

1. Reduces RTM settlement timeline from 10 to 9 days
2. Reduces payment timeline from 3 to 2 bank business days for daily DAM and RT invoices

IMPACT: With the above two changes (in addition to the changes in NPRR 347), ERCOT anticipates (based on 2011 calendar) that approximately 88% of operating days will be settled within 14 days and the weighted average days to settle will be approximately 13.5 days

3. Eliminates ACH as a Mode of Payment (may only pay by immediately available funds)

IMPACT: Approximately 1% of dollar volume is ACH. Fewer than 10 CPs (or 4%) use ACH.

Impact of this NPRR is manageable

6. Committee Briefs: NPRRs with Credit Implications

- **NPRR 400 - Eliminate Unsecured Credit for CRR Auctions and for Future Credit Exposure (FCE) and Eliminate Netting of FCE with CCE**
 - Eliminates Unsecured Credit for CRR Auctions and the FCE component of the credit exposure calculation
 - IMPACT (as of September 30, 2011)
 - 67 counterparties have unsecured credit available, either directly or indirectly through guarantees.
 - 27 counterparties (or 40%) do not have any exposure collateralized.
 - 40 counterparties have exposure that requires collateral, of which 20 entities also have CRR activity that would require collateral (remaining 20 have no CRR activity or credits from CRR activity)
 - Elimination of unsecured credit in the CRR market would have increased collateral requirements by approximately \$16.7 million for CRR FCE (as of September 30, 2011) or approximately 1.3% of total exposure of \$1.2 billion
 - Impact will likely grow when there are 12 or 24 months of exposure rather than 3 months for CRRs outstanding
 - Expected to have a significant impact on CP's pre-posting requirements for CRR Auctions as well
 - Operational risk entailed by this change is manageable

6. Committee Briefs: NPRRs with Credit Implications

- **NPRR 400 - Eliminate Unsecured Credit for CRR Auctions and for Future Credit Exposure (FCE) and Eliminate Netting of FCE with CCE (Cont.)**
 - Eliminates netting of the calculated credit exposure for CRR forward risk
 - Currently netting between CRR and non-CRR markets is restricted to counterparties a) from whom ERCOT has a first priority security interest, or b) who are either an Electric Cooperative or an Entity created under TWC § 222.001.

IMPACT: As of September 30th, only 11 Counter-Parties or approximately 5% of CPs are allowed to net between CRR and non-CRR markets.

Impact is manageable

ERCOT

Finance and Audit Committee

2011 Annual Meeting Planner and Future Agenda Items - NOVEMBER MEETING CANCELLED

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					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	A								A	←		
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					A							
12 Undertake annual self-evaluation	8	A									A	→	
13 Periodic meeting with senior management	6							A					
14 Review and approve internal audit charter	6			A									
15 Periodic meeting with Chief Audit Executive	6 & 7	A	A	A	A	A	A	A	A	A	A	→	
16 Review internal audit reports	6	A	A	A	A	A	A	A	A	A	A	→	
17 Review Ethics Point issues	na	A	A	A	A	A	A	A	A	A	A	→	
18 Review effectiveness of internal audit functions	6												
19 Review and approve annual internal audit plan	6									A	←		
20 Review performance of the Chief Audit Executive	7												→
21 Recommend selection of independent auditor	4										A		
22 Receive independence report from independent auditor	4										A		
23 Periodic meeting with independent auditor	5				A						A		
24 Discuss audited financial statements	5				A								
25 Review and accept financial statement audit	5				A								
26 Review and recommend proposed budget	3					A	A	A	A				
27 Review and recommend debt structure	3						A	A	A				
28 Review IRS Form 990	na							A					
29 Review and accept 401(k) audit report	5								A				
30 Review and accept SSAE 16 audit report	5			A									
31 Review Committee briefs	na	A	A	A	A	A	A	A	A	A	A	→	
32 Receive periodic investment report	na		A			A			A			→	
33 Receive periodic liquidity report	na			A									
34 Quarterly Committee education on accounting developments	5			A			A			A			
35 Review financial institutions - market participants	6			A						A			
36 Receive periodic Potential Future Exposure report	na												→
37 Preapprove non-audit services	4				A								
38 Review any report by independent auditor	4	Performed on as-needed basis											
39 Review effect of regulatory accounting initiatives	5	Performed on as-needed basis											
40 Review complaints regarding financial statements	5			A	A								
41 Review press stories regarding financial statements	5	Performed on as-needed basis											
42 Periodic meeting with 401(k) auditor	na	Performed on as-needed basis											
43 Periodic meeting with SSAE 16 auditor	na	Performed on as-needed basis											
44 Review proposed audit of the nodal program	na		A										
45 Review credit procedures, practices, and judgments	na		A	A	A	A							
46 Commodity Exchange Act exemption	na				A	A	A	A	A	A	A		
47 Generation interconnection fee	na				A		A						

ERCOT

Finance and Audit Committee

2012 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												
2 Review and assess adequacy of Committee charter	6		█										
3 Review and recommend investment standard	3		█										
4 Review and recommend financial standard	3		█										
5 Handling of complaints regarding financial matters	5		█										
6 Hiring former employees of the independent auditor	4		█										
7 Review and recommend credit standard	3												
8 Receive periodic report on Credit Work Group activity	na										█		
9 Approve Credit Work Group Charter	na		█										
10 Appoint Credit Work Group Chair and Vice Chair	na		█										
11 Commodity Exchange Act exemption	na		█										
12 Review risk policies and risk management practices	6				█				█				█
13 Undertake annual self-evaluation	8										█		█
14 Periodic meeting with senior management	6		█						█				
15 Review and approve internal audit charter	6		█										
16 Periodic meeting with Chief Audit Executive	6 & 7		█		█		█		█		█		█
17 Review internal audit reports	6		█		█		█		█		█		█
18 Review Ethics Point issues	na		█		█		█		█		█		█
19 Review effectiveness of internal audit functions	6												
20 Review and approve annual internal audit plan	6										█		█
21 Review performance of the Chief Audit Executive	7												█
22 Recommend selection of independent auditor	4										█		
23 Receive independence report from independent auditor	4										█		
24 Periodic meeting with independent auditor	5				█						█		
25 Discuss audited financial statements	5				█								
26 Review and accept financial statement audit	5				█								
27 Review and recommend proposed budget	3						█		█				
28 Review and recommend debt structure	3		█		█		█		█				
29 Review IRS Form 990	na								█				
30 Review and accept 401(k) audit report	5								█				
31 Review and accept SSAE 16 audit report	5								█				█
32 Review Committee briefs	na		█		█		█		█		█		█
33 Quarterly Committee education on accounting developments	5				█				█				█
34 Review financial institutions - market participants	6				█						█		
35 Receive periodic Potential Future Exposure report	na		█				█				█		
36 Preapprove non-audit services	4	Performed on as-needed basis											
37 Review any report by independent auditor	4	Performed on as-needed basis											
38 Review effect of regulatory accounting initiatives	5	Performed on as-needed basis											
39 Review complaints regarding financial statements	5	Performed on as-needed basis											
40 Review press stories regarding financial statements	5	Performed on as-needed basis											
41 Periodic meeting with 401(k) auditor	na	Performed on as-needed basis											
42 Periodic meeting with SSAE 16 auditor	na	Performed on as-needed basis											