



**Date:** March 12, 2013  
**To:** Board of Directors  
**From:** Mark Ruane, Vice President, Credit & Enterprise Risk Management  
**Subject:** ERCOT Creditworthiness Standards

**Issue for the ERCOT Board of Directors**

**ERCOT Board of Directors Meeting Date:** March 19, 2013

**Item No.:** 12.3

**Issue:**

Approval of revisions to the ERCOT Creditworthiness Standards, which revisions are endorsed by the Credit Work Group (CWG) and recommended by ERCOT staff.

**Background/History:**

Protocol Section 16.11.2, “Requirements for Setting a Counter-Party’s Unsecured Credit Limit,” requires the ERCOT Board of Directors (Board) to approve ERCOT Creditworthiness Standards that define how ERCOT will grant unsecured credit to Counter-Parties and Guarantors.

The ERCOT Creditworthiness Standards (Standards) require that “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.” The Standards were last approved by the Board in October 2011.

By electronic vote, in November 2012, the Credit Work Group voted to endorse a number of proposed revisions to the Standards. The revisions include:

- Cash deposits to be made into an ERCOT-designated account.
- No modifications allowed to standard guarantee form.
- Corporate guarantees subject to a limit of \$50 million per Counter-Party and an overall limit of \$50 million per guarantor.
- Elimination of the reduction in credit limits for foreign guarantors who do not provide quarterly financial statements, however, foreign guarantors must provide ERCOT a legal opinion that the guarantee is enforceable in the US.
- Surety bonds must be on a standard form document approved by the ERCOT Board of Directors. (The current surety bond template was approved by the Board in April 2012.)

The proposed revisions to the Standards are reflected in *Attachment A*.

The Finance and Audit (F&A) Committee is expected to recommend whether the Board adopt, reject or amend the Standards at its March 18, 2013 meeting.



**Key Factors Influencing Issue:**

1. Improved controls over cash deposits.
2. Better protection to ERCOT by standardization of guarantees and surety bonds.
3. Improved transparency with respect to the value of foreign guarantees.
4. Reduced exposure from single guarantors.

**Conclusion/Recommendation:**

ERCOT staff respectfully recommends approval of the proposed revisions to the Standards, which have been endorsed by the CWG. The F&A Committee is expected to recommend to the Board whether any revisions should be made to the Standards at its March 18, 2013 meeting, and whether they should become effective upon approval by the Board.



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

WHEREAS, Section 16.11.2, *Requirements for Setting a Counter-Party's Unsecured Credit Limit*, of the Nodal Protocols requires the Board of Directors (Board) of Electric Reliability Council of Texas, Inc. (ERCOT) to approve ERCOT Creditworthiness Standards that define how ERCOT will grant unsecured credit to Counter-Parties and Guarantors; and

WHEREAS, after due consideration of the alternatives, the ERCOT Board deems it desirable and in the best interests of ERCOT to approve the proposed changes to the ERCOT Creditworthiness Standards as endorsed by the Credit Work Group (CWG) and recommended by ERCOT staff and as reflected in *Attachment A*, with immediate effect; and

THEREFORE, BE IT RESOLVED, that the ERCOT Creditworthiness Standards as endorsed by CWG and recommended by ERCOT staff, as described in *Attachment A*, are hereby authorized and approved with immediate effect.

**CORPORATE SECRETARY'S CERTIFICATE**

I, Vickie G. Leady, Assistant Corporate Secretary of ERCOT, do hereby certify that, at its March 19, 2013 meeting, the ERCOT Board passed a motion approving the above Resolution by \_\_\_\_\_.

IN WITNESS WHEREOF, I have hereunto set my hand this \_\_\_\_ day of March, 2013.

\_\_\_\_\_  
Vickie G. Leady  
Assistant Corporate Secretary

## Electric Reliability Council of Texas, Inc.

### Creditworthiness Standards

Referenced in Section 16.11 of the Nodal Protocols

### Creditworthiness Standards for Cooperative and Municipal Systems

IF YOUR ENTITY HAS	<u>AND</u>	<u>AND</u>	<u>AND</u>	<u>THEN</u>
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*
<b>\$25,000,000</b>	<b>1.05</b>	<b>1.00</b>	<b>0.15</b>	<b>0.00% to 5.00%</b>
* Unsecured line not to exceed \$ 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.

# Electric Reliability Council of Texas, Inc.

## Creditworthiness Standards

Referenced in Section 16.11 of the Nodal Protocols

### 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&amp;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 \$ 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.

# Electric Reliability Council of Texas, Inc.

## Creditworthiness Standards

Referenced in Section 16.11 of the Nodal Protocols

### Creditworthiness Standards for Privately-Held Entities

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

\*Unsecured line not to exceed \$ 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.

# Electric Reliability Council of Texas, Inc.

## Creditworthiness Standards

Referenced in Section 16.11 of the Nodal Protocols

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

1. ~~Cash Deposit - standard form n/a~~ Deposited in an account designated by ERCOT.

2. Letter of Credit (LC)

a. Must be issued by a bank with a minimum rating of A- with Fitch or S&P or A3 with Moody's. Must be issued on the Sstandard Form document approved by the ERCOT Board of Directors; no modifications are permitted.

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3. Corporate Guarantee

a. Guarantor must meet applicable credit standards as stated in ~~the ERCOT Protocols.~~

b. Guarantee must be on the Sstandard Fform document approved by the ERCOT Board of Directors; no modifications are permitted

c. Subject to a limit of \$50 million of guarantees per Counter-Party and an overall limit of \$50 million per guarantor for all ERCOT Counter-Parties.

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 semi-annual/quarterly unaudited financial statements.

~~ii. However, if the foreign guarantor does not provide quarterly financial statements, the assigned credit limit will be reduced for the relevant quarters 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 one of the standard form documents approved by the ERCOT Board of Directors - approved standard form guarantee Agreement for foreign Entities; no modifications are permitted.~~

~~— Provide Reimburse ERCOT the cost of obtaining an opinion letter from a law firm unaffiliated with the Counter-Party or guarantor of counsel affirming that the guarantee agreement is enforceable in the U.S. and in the jurisdiction of the corporate guarantor's domicile. Maintain a registered Texas Registration Agent~~

# Electric Reliability Council of Texas, Inc.

## Creditworthiness Standards

Referenced in Section 16.11 of the Nodal Protocols

~~iv.~~

### 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.
- ~~a.b.~~ Surety Bond must be on the standard form document approved by the ERCOT Board of Directors; no modifications are permitted.
- ~~b.c.~~ Subject to a limit of \$10 million per Counter-PartyQSE per insurer and an overall limit of \$100 million per insurer for all ERCOT Counter-PartiesQSEs.

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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.