

Securitization: What Is It and How Did It Happen?

Friday, February 12, 2021, ERCOT advised of possible rotating outages for the upcoming weekend and following week. At 5:03 that evening, PenTex Energy posted the following message on their website and social media: "Please conserve energy in the coming days as it is possible, we could experience ERCOT rolling outages. Due to high energy demands, ERCOT required load shed may cause rotating outages throughout the PenTex Energy system."

At 2:40 AM on Monday, February 15th, PenTex received notice that the predicted mandated rolling outages must begin. While we realized these outages were a great inconvenience to our membership, once the ERCOT mandate was enacted, it was beyond the control of PenTex, or any distribution provider. For simplicity, many providers chose to meet their required load shed by turning off a circuit for many hours at a time and then moving on to another circuit. I experienced this firsthand! Unfortunately, my home is not located in PenTex Energy's service area, and I experienced extended periods of being without power (a 15-hour period initially). Trying to keep pipes from freezing and the temperature in our home livable was next to impossible. PenTex Energy's team devised a plan that met the load shed requirement while not leaving members without power for an extended period. This was very time intensive and more work for our employees, but we felt it was worth it for our membership.

Over the next several days across the state of Texas, roughly 34,000 megawatts of generation failed due to the extreme record setting freezing weather. Over 4.5 million people were without power, over 200 people perished, and twelve million people were issued boil notices due to broken water pipes. During this time, solar production declined dramatically due to snow and ice, and wind production was almost non-existent due to icing on turbine blades. Additionally, gas-powered generation was down due to equipment failures from the extreme temperatures and the inability to procure fuel to run.

The freezing rain, snow, wind gusts and relentless cold caused damage to poles, wires, and equipment across the state of Texas, including PenTex Energy's system. Normally co-ops from across the state assist one another by providing hundreds of crews who can help. Because the damage was statewide and travel was dangerous, the movement of crews was limited.

On Monday, February 15th, even with the mandated load shed across the state, the electric grid came within four ½ minutes of complete failure. Had the grid completely failed, it would have taken weeks to restore, leaving Texas totally without power. The mandated rolling outages continued until 1:00 a.m. on 2/18/21, when ERCOT lifted the mandate. However, ERCOT kept the Energy Emergency Alert at EEA3, which kept the door open for mandated rolling outages to be required again at any time. ERCOT requested continued conservation as work continued to stabilize the grid. It was not until Friday, February 19th that ERCOT changed the EEA3 status to "normal operations". It was later revealed that sufficient generation and reserves existed 33 hours prior to ERCOT returning the EEA status to "normal". There was a pricing mechanism in place that allowed prices to rise to a cap of \$9,000/MWH (\$9.00/KWH) during the EEA3 status, which was over 375 times typical pricing. So, you see, the emergency operations status is not merely for energy conservation reasons but also the economic piece of it. After a lot of push back, that cap has since been lowered to \$5,000/MWH (\$5.00/KWH), which is still exorbitant!

Brazos Electric Cooperative, PenTex Energy's power provider was slapped with a \$1.9 billion bill for power procurement during Uri. Brazos, rated AAA prior to Uri, did not have the liquidity available to pay ERCOT within the required amount of time to stay in the market, leaving them no choice but to file for Chapter 11 bankruptcy.

PenTex Energy's board and staff were notified that effective March 1, 2021, Brazos would be filing for bankruptcy. While we knew this was a bleak time, the full impact became reality when the February power bill from Brazos Electric to PenTex Energy was received. A bill that typically would have been \$3,450,000 totaled \$82,000,000. The bill included a \$79 million "Temporary Affordability Adjustment" (TAA), providing temporary but not long-term relief. This TAA was PenTex Energy's share of Brazos's \$1.9 billion due from Winter Storm Uri.

State legislators came together to address this financial crisis. The Texas House passed HB 4492 which created a mechanism for the Public Utility Commission of Texas to authorize the securitization of ERCOT market uplift charges related to the winter weather event. Another blow came to cooperatives when we were made aware that an amendment was made to HB 4492 at the last hour by State Representative Chris Paddie, which excluded electric cooperatives from participating in this legislation. In lieu of HB 4492, SB 1580 was enacted, which is a mechanism that allowed electric cooperatives to finance their Uri costs and extraordinary expenses (off balance sheet) at a lesser cost than otherwise would have occurred.

As all the above was unfolding, the Brazos bankruptcy proceedings slowly moved forward. The initial hope was that the \$1.9 billion due to ERCOT from Brazos would be significantly reduced through the bankruptcy process. As the hearings commenced, it became clear that was not to be the case. ERCOT maintained they are only a clearinghouse through which the power purchases passed, and the gas providers had long since been paid. After a year of weekly calls, meetings and correspondence, the Brazos bankruptcy trial was scheduled to be held in February, 2022. Several days into the trial, the presiding judge ordered the proceeding into mediation with another judge. The mediation process continued over the next several months and it became evident there would be no great reduction in the amount to be paid to ERCOT. Additionally, with mounting attorney and professional fees, reaching a mediated settlement was in the best interest of Brazos Electric and their members. Without the mediated settlement, there was a good chance of an appeal to the Supreme Court and years of continued legal fees. The Uri charges incurred during the last 33 hours, that ERCOT maintained emergency status and the \$9,000/MWH (\$9.00/KWH) pricing, were mitigated through the settlement.

The Brazos bankruptcy reorganization plan required them to sell their generation plants. The plan also included a \$140 Million allotment to a Hardship Fund available to qualifying members, specifically for securitization charges. The bankruptcy plan also allowed members of Brazos Electric to retain their patronage, which in turn is assigned and disbursed as G & T patronage to our members.

At the end of the day, PenTex Energy had \$65,325,775 in Uri costs to deal with. After months of deliberation, the PenTex Energy board of directors, with the recommendation of PenTex senior staff, determined that participating in the Brazos led securitization, along with nine other Brazos Electric member cooperatives, was the best solution. While not ideal, securitization ensures PenTex Energy's financial stability and our ability to best serve our membership, at the lowest possible cost, moving forward. The securitization finances the Uri costs for 27.75 years.

Professionals and attorneys specializing in the securitization process were procured by Brazos Electric. PenTex Energy staff devoted countless hours throughout this process. For complete transparency, PenTex Energy made the decision to list the Securitization Cost Recovery Factor (SCRF) as a separate line item on member bills. The per kwh charge initially provided to us was .01298. Correspondence was mailed to our membership stating this amount in mid-December. A few days later another meeting was called, and we were informed that ten months of estimated securitization cost must be collected in the first six months. Thus, a second letter was mailed to our members, notifying them that the SCRF would be .02146 per kWh. The per kWh charge will be re-calculated by the Master Servicer every six months

and updated accordingly. Looking forward, growth in the PenTex Energy service territory will reduce the cost per kWh of the securitization charge (The charge is fixed, so as the number of meters and kWh sales increase, the cost per kWh to each member will decrease). Please keep in mind that none of the securitization charges billed and collected remain at PenTex Energy. Within two days of the due date of billed securitization charges, payment must be made by PenTex Energy to the Master Servicer.

Beginning March 1st, PenTex Energy will procure all our own power supply. Since this power procurement will meet the needs of PenTex Energy's specific load shape, this should be advantageous for pricing going forward. Any savings in power cost will be passed on to our members through the Power Cost Recovery Factor (PCRF).

The last two years have been a grueling and humbling process that we hope and pray PenTex Energy employees and membership never have to experience again.

Sincerely,

Neil Hesse
General Manager