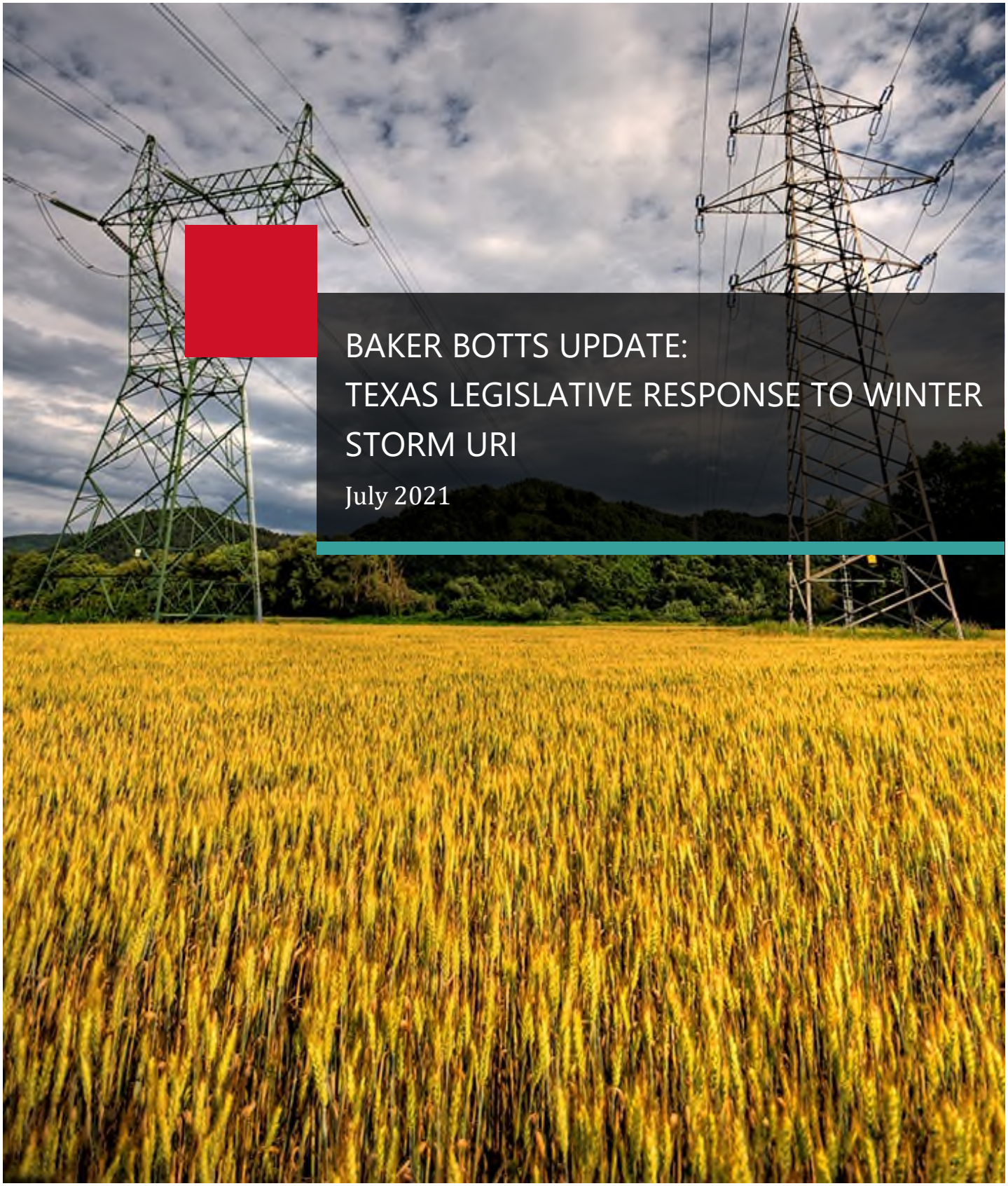

BAKER BOTTS UPDATE: TEXAS LEGISLATIVE RESPONSE TO WINTER STORM URI

July 2021

BAKER BOTTS

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INTRO

INTRODUCTION: FOUR KEY AREAS OF LEGISLATIVE FOCUS

"They're top-notch, go-to lawyers for significant legal issues - it helps me sleep at night knowing they are on my case.'"

Chambers USA, 2020

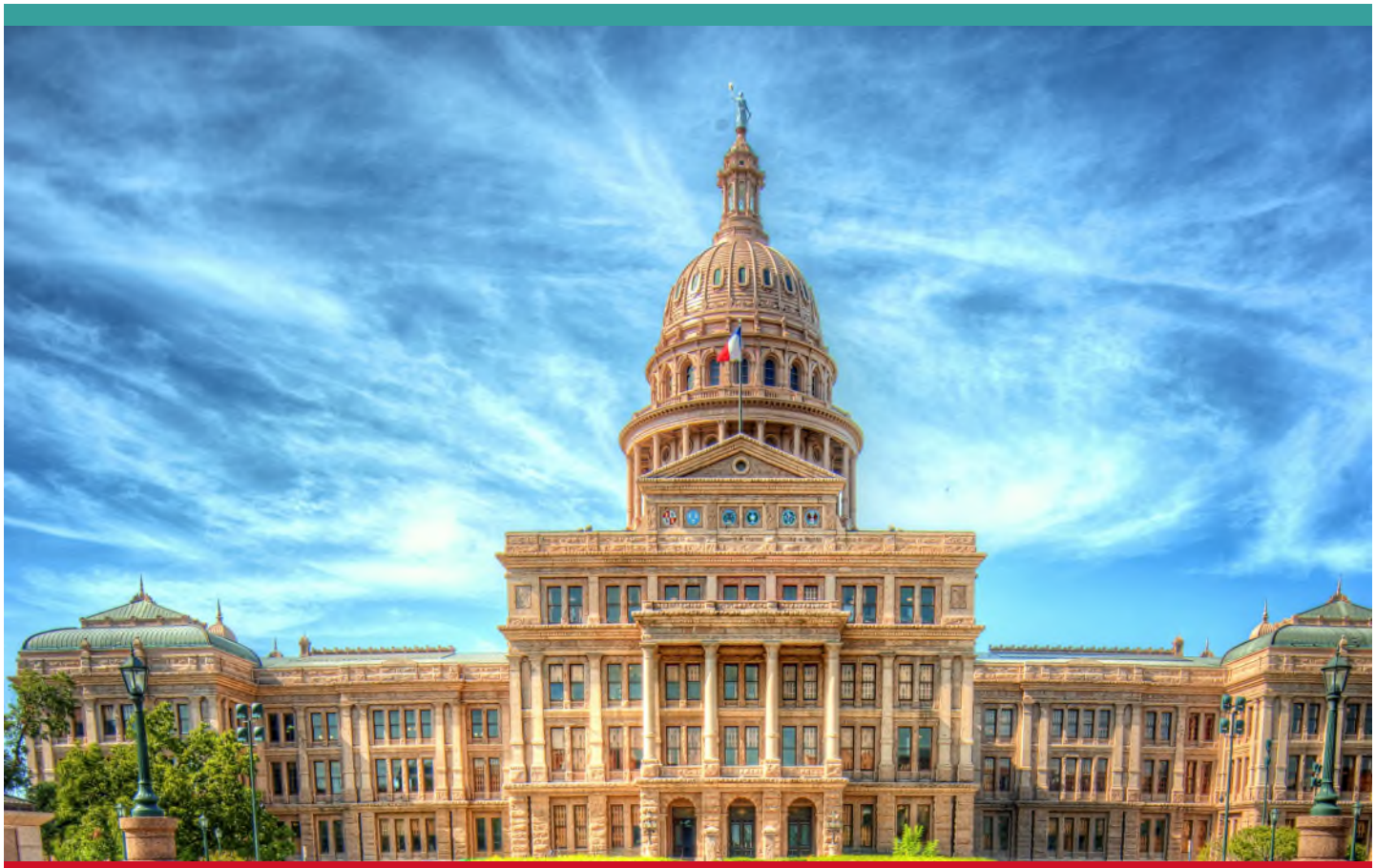
Four Key Areas of Legislative Focus

The Texas Legislature concluded its 87th regular session on May 31, 2021. The session produced a number of new laws that will affect the Texas electric power industry, both directly and indirectly. All of the new laws discussed in this alert have been signed by Governor Abbott—the last one having been signed on June 18th—and are either in effect already or will take effect on September 1, 2021. Most of the new laws amend Title 2 of the Texas Utilities Code, commonly referred to as the Public Utility Regulatory Act ("PURA"). Other new and amended provisions appear in the Texas Government Code ("TGC"), the Natural Resources Code ("NRC"), and elsewhere. The bills are targeted at the Public Utility Commission of Texas ("PUC"), Electric Reliability Council of Texas ("ERCOT"), Texas Railroad Commission ("RRC"), and Division of Emergency Management ("DEM"), but reach (and create) other agencies and groups as well. Rather than describing individual bills, and rather than describing every bill that touches the energy industry, this summary describes four key areas of legislative focus driven by the February 2021 winter storm.

- Part 1: Changes to the governance structure overseeing the electric market
- Part 2: Changes to the structure of the electric market itself
- Part 3: Changes to reduce the risk of future electric system disruptions
- Part 4: Changes to address the costs of the February 2021 winter storm

Many of the new laws addressed in this alert will require rulemakings at one or more agencies to determine the details of their implementation. The PUC has a rulemaking calendar for all rulemakings (including those required as a result of the legislation passed to address issues from the winter storm) available in Project No. 51715, which Staff periodically updates. Clients should strongly consider whether participation in any such rulemakings may be advisable to protect their interests.

Links to the bills discussed in this alert, as well as other useful documents, may be found at the end of the alert.



01 PART 1: CHANGES TO THE GOVERNANCE STRUCTURE OVERSEEING THE ELECTRIC MARKET

"The team, both in their counseling and litigation functions, provides pragmatic advice in real time. In addition to answering the question asked, they always provide me with contextual information to help me understand the broader implications of the decision before us."

Legal 500, US 2020

Part 1: Changes to the Governance Structure Overseeing the Electric Market

A primary target of legislation this session was the governance structure of both ERCOT and the PUC. The Legislature also created a number of new entities to oversee or facilitate oversight of the Texas energy markets.

OVERHAUL OF ERCOT GOVERNANCE

In SB 2, the legislature has overhauled the ERCOT governance structure with a number of changes to selection and make-up of the ERCOT board.

- *Texas Residency:* All ERCOT board members are now required to be residents of Texas.
- *ERCOT Board Selection Committee:* A newly established ERCOT board selection committee is made up of one member appointed by each of the Governor, Lieutenant Governor and Speaker of the House of Representatives. That Committee, in turn, will engage an outside consulting firm to select eight ERCOT board members.
- *ERCOT Board Changes:* The number of ERCOT board seats has been reduced from 16 to 11, with eight members (selected by the ERCOT Board Selection Committee) with executive-level experience in finance, business, engineering, trading, risk management law, or electric market design. The eight members will replace the previous board composition of six members representing market participants, one member each representing industrial consumers and large commercial consumers, and five unaffiliated members.

The politically appointed ERCOT Board Selection Committee was added to the legislation without public debate just prior to the ultimate vote on the bill. The Selection Committee construct has been criticized by some observers as favoring political connections over relevant industry experience. SB 2 became effective immediately upon the governor's signature on June 9, 2021.

CHANGES TO PUC GOVERNANCE

SB 2154 requires the revamping of the PUC. Specifically, the bill amends PURA to update eligibility requirements for Commissioners and puts new lobbying restrictions into place.

Updated Eligibility Requirements

- Expands the PUC from three commissioners to five;
- Creates a requirement that commissioners be residents of Texas;
- Removes a requirement that commissioners be "well informed and qualified in the field of public utilities and utility regulation," but creates a requirement that at least two of the five commissioners be so qualified;

- Expands the five-year professional experience requirement to include experience as a professional engineer;
- Creates a new timeline and conditions for automatic ineligibility wherein persons are ineligible for appointment if, at any time during the year preceding appointment, they:
    - Served as an officer, director, owner, employee, or legal representative of a public utility regulated by the PUC;
    - Owned or controlled more than a 10% interest in a public utility regulated by the PUC; or
    - Served as an executive officer in the Executive Department of the State of Texas, not including service as Secretary of State or as a member of the Legislature.

These are the current Commissioners and their terms.

	COMMISSIONER	TERM EXPIRES
1	Lori Cobos	September 1, 2021
2	Peter Lake, Chair	September 1, 2023
3	Will McAdams	September 1, 2025
4	*Vacant*	*To be determined*
5	*Vacant*	*To be determined*

New Lobbying Restrictions. SB 2154 also places restrictions on lobbying activities by former members of the PUC. Specifically, the law prohibits a former member of the PUC from engaging in any activity that would require registration as a lobbyist before the first anniversary of the date the member ceases to be a member of the PUC. Having received a vote of two-thirds of all members elected to each house, SB 2154 took effect immediately when signed by the Governor on June 18, 2021.

CREATION OF TEXAS ENERGY RELIABILITY COUNCIL

SB 3 creates a new Subchapter J within Chapter 418 of the Texas Government Code. New TGC § 418.301 formally establishes the Texas Energy Reliability Council ("TERC"), which was previously an informal, smaller group, "to (1) ensure that the energy and electric industries in [Texas] meet high priority human needs and address critical infrastructure concerns and (2) enhance coordination and communication in the energy and electric industries in [Texas]." Not later than November 1 of each even-numbered year (thus two months in advance of each legislative session), the TERC must submit a report to the Legislature on the reliability and stability of the electricity supply chain in Texas. The TERC comprises 25 members. A description of the membership and the individuals currently in place can be found in the Links section at the end of this alert. The TERC must meet at least twice per year.

CREATION OF TEXAS ELECTRICITY SUPPLY CHAIN SECURITY AND MAPPING COMMITTEE

SB 3 also adds a new Subchapter F to Chapter 38 of PURA. New PURA § 38.201(b) creates the Texas Electricity Supply Chain Security and Mapping Committee ("TESCSMC"). The executive director of the PUC chairs the TESCSMC. Other members are the executive director of the RRC (vice chair), the president and CEO of ERCOT, and the chief of the Texas Division of Emergency Management. The table below provides a description of the TESCSMC membership and a list of the members as of June 30, 2021.

	DESCRIPTION OF POSITION	MEMBER
1	Executive Director of PUC (*Chair*)	Thomas Gleeson
2	Executive Director of RRC (*Vice Chair*)	Wei Wang
3	President and CEO of ERCOT	Brad Jones (*Interim*)
4	Chief of Texas Division of Emergency Management	W. Nim Kidd

The TESCSMC's name provides its purpose – to ensure the reliability of the power "supply chain" by identifying critical infrastructure within the supply chain, establishing best practices to prepare such facilities such that they are able to maintain and reestablish service in an extreme weather event.

CREATION OF STATE ENERGY PLAN ADVISORY COMMITTEE

SB 3 (Section 33) creates a State Energy Plan Advisory Committee ("SEPAC"). The SEPAC comprises 12 members with 4 members appointed by each of the Governor, the Lieutenant Governor, and the Speaker of the House of Representatives. By September 1, 2022, the SEPAC must prepare a comprehensive state energy plan that evaluates barriers in the electricity and natural gas markets that prevent sound economic decisions, evaluate methods to improve the reliability, stability, and affordability of electric service in Texas, evaluate the state's electric market structure and pricing mechanisms, and make recommendations for changes to the electric and natural gas markets.

02 PART 2: CHANGES TO THE STRUCTURE OF THE ELECTRIC MARKET ITSELF

"Great honest people that are easy to work with and provide an outstanding work product in a timely manner at a fair rate."

Legal 500 US, 2020

Part 2: Changes to the Structure of the Electric Market Itself

The Legislature passed new laws changing three important aspects of the Texas electric market structure: (1) the transmission planning and approval process, (2) the procurement and pricing of wholesale energy and reliability products, and (3) the regulation of retail electricity products. Specifically, the new laws:

- expand existing exceptions to the requirement for utilities to obtain approval for new transmission lines;
- expand the reliability issues that must be addressed when considering approval of new transmission projects;
- require a reassessment of the types, quantities, and costs of ancillary services needed for ERCOT reliability;
- prescribe new parameters for emergency wholesale pricing of energy and ancillary services;
- prohibit the sale of wholesale indexed power products to residential and small commercial customers;
- limit the provision of wholesale indexed power products to other customers; and
- require retail providers to provide multiple advance notices that a fixed-rate retail plan is about to expire before moving a customer to a default plan.

CHANGES TO TRANSMISSION PLANNING AND APPROVAL

Expanded CCN Exception. SB 1281 amends PURA §37.052 to provide an expanded exception from the requirement that electric utilities obtain a certificate of convenience and necessity ("CCN") before constructing new transmission lines. The PUC's existing rules contain a CCN exemption for transmission lines that interconnect substations or end-use customers if the new line does not exceed one mile and all landowners whose property is crossed have given prior written consent. New PURA §37.052 creates a broader, statutory exception where:

1) the transmission line does not exceed three miles (for load-serving connections) or does not exceed two miles (for generation connections);
2) all "directly affected" landowners provide consent; and
3) all necessary rights-of-way have been purchased.

The reference to "directly affected" landowners introduces more uncertainty than the current administrative rule, which applies to landowners "whose property is crossed." The new law takes effect on September 1, 2021. As of June 30, 2021, the PUC had not yet opened a rulemaking to implement this bill.

Expanded Consideration of Reliability in CCN Cases. SB 1281 also made two changes to increase the consideration given to reliability issues by the PUC when reviewing proposed transmission projects. Existing PURA §37.056(c)(2) requires the PUC to consider the need for additional service when issuing a CCN, and existing PURA §37.056(d) requires that the PUC establish cost-benefit criteria for new projects that are not necessary to meet state or federal reliability standards.

Accordingly, the PUC's existing rules provide for a different need analysis depending on whether a new transmission line is considered a reliability project. Under existing PUC Rule 25.101(b)(3)(A)(i), the CCN applicant must demonstrate that the annual production cost savings from a new line will equal or exceed the project's annual revenue requirement. However, this cost-benefit requirement does not apply to a project that is "necessary to meet state or federal reliability standards, including: a transmission line needed to interconnect a transmission service customer or end-use customer; or needed due to the requirements of any federal, state, county, or municipal government body or agency for purposes including, but not limited to, highway transportation, airport construction, public safety, or air or water quality." For such reliability projects, PUC Rule 25.101(b)(3)(A)(ii) requires the PUC to consider the need for the project to support a reliable and adequate grid and to facilitate robust wholesale competition. In doing so, the PUC must give great weight to an ERCOT recommendation and/or the need for the new line to interconnect a transmission service customer or end-use customer.

The first change under the new law amends PURA §37.056 regarding the approval of new *reliability* transmission projects. SB 1281 amends §37.056 by adding a new subsection (c-1), which requires that, in the case of a reliability transmission project, the PUC must also consider historical load, forecasted load growth, and additional load seeking interconnection. We note that the PUC's standard application form for a transmission line CCN already requires a utility to provide historical load data and load projections for at least five years for any project needed to accommodate load growth.

The second change under SB 1281 amends existing PURA §37.056 regarding the required cost-benefit analysis for non-reliability transmission projects. It adds language to clarify that the costs and benefits to be considered are the costs and benefits to *consumers*. It also requires that the cost-benefit analysis consider current and future expected congestion levels and project's ability to reduce such congestion.

The new law takes effect on September 1, 2021. As of June 30, 2021, the PUC had not yet opened a rulemaking to implement this bill.

CHANGES TO THE PROCUREMENT AND PRICING OF WHOLESALE ENERGY AND RELIABILITY PRODUCTS

Reassessment of Ancillary Services and Their Costs. There were unsuccessful attempts to pass new laws that would have imposed additional ancillary service costs on renewable or non-dispatchable generation sources. However, SB 3 does amend PURA § 35.004 to require the PUC to review existing ancillary services and their costs to determine whether they continue to meet the needs of the ERCOT market and to evaluate whether additional ancillary services are necessary for reliability in ERCOT "while providing adequate incentives for dispatchable generation." Moreover, the amended PURA § 35.004 requires ERCOT (under PUC direction) to modify the design, procurement, and cost allocation of ancillary services in ERCOT "in a manner consistent with cost-causation principles and on a non-discriminatory basis. The rulemakings to implement these new provisions could shift the relative allocation of

ancillary service costs among different categories of generation. The PUC had an existing rulemaking, Project No. 51871, to review and identify potential improvements to the rules and protocols of the ERCOT wholesale electric market, with emphasis on the pricing of energy and ancillary services. Under Project No. 51871, the PUC adopted rule changes to eliminate a provision tying the low system-wide offer cap (the "LCAP") to the natural gas price index and replaced it with a provision that allows generators to recover their actual marginal costs when the LCAP is in effect. As of June 30, 2021, the PUC had not opened a new rulemaking to implement the amended PURA § 35.004.

SB 3 also adds a new PURA § 39.159 that separately requires the PUC to oversee ERCOT in (a) establishing requirements to meet ERCOT's reliability needs, (b) at least annually, determining the amount and type of ancillary or reliability services needed during extreme heat or cold events and when non-dispatchable generation is low, (c) procuring such ancillary or reliability services on a competitive basis, (d) developing qualifications for providing such services and penalties for failing to do so, and (e) sizing any such services procured to prevent prolonged rotating outages. The new law also requires the PUC to ensure that resources providing such services are dispatchable and capable of continuous service in the relevant season. Winter resources must have on-site fuel storage, dual fuel capability, or multi-day fuel supply arrangements. Summer resources must have facilities or procedures to ensure operation under drought conditions.

Emergency Wholesale Pricing. SB 3 adds a new PURA § 39.160 that requires the PUC to adopt new rules establishing an emergency pricing program for the wholesale electric market in ERCOT. The program must take effect if the high system-wide offer cap (the "HCAP") has been in effect for 12 hours in any 24-hour period after it is initially reached. The new law directs the PUC to determine the criteria for ending the emergency pricing program but dictates a number of features.

- The emergency price cap may not exceed the non-emergency HCAP.
- The PUC must establish an ancillary services cap to be in effect when emergency pricing is in effect.
- The LCAP, if any, may not exceed the HCAP (a condition that existed during the February 2021 winter storm as the result of certain price formulas in use).
- Generators must be reimbursed for reasonable, verifiable operating costs that exceed the emergency price cap (included in a new rule adopted in Project No. 51871).
- The PUC must review the emergency pricing system and consider updates at least once every five years.

As of June 30, 2021, the PUC had not opened a new rulemaking to implement the new PURA § 39.160.

CHANGES TO THE REGULATION OF RETAIL ELECTRICITY PRODUCTS

Prohibition on sale of wholesale indexed power products to residential and small commercial customers. HB 16 creates a new PURA § 39.110 that prohibits an aggregator, broker, or retail electric provider from offering wholesale indexed products to a residential or small commercial customer. Under the new law, "'wholesale indexed product' means a retail electric product in which the price a customer pays for electricity includes a direct pass-through of real-time settlement point prices determined by [ERCOT]." The prohibition takes effect on September 1, 2021.

Limitation on sale of wholesale indexed power products to other customers. Under the new PURA § 39.110 created by HB 16, providers may still enroll customers other than residential or small commercial customers in a wholesale indexed product, but only if the provider first obtains a signed statement from the customer acknowledging the potential price risk associated with wholesale indexed products. The statement must include language set out in PURA § 39.110(d). The provider *must* keep the acknowledgment in the customer's file and *may* include it as an addendum to the contract.

Notice of Fixed Rate Product Expiration. Existing law requires that a retail electric provider give a residential customer who has a fixed-rate product at least one written notice of the date on which the fixed rate product will expire. Under PURA § 39.112, "'fixed rate product' means a retail electric product with a term of at least three months for which the price for each billing period, including recurring charges, does not change throughout the term of the contract, except that the price may vary to reflect actual changes in transmission and distribution utility charges, changes to ERCOT or Texas Regional Entity administrative fees charged to loads, or changes to federal, state, or local laws that result in new or modified fees or costs that are not within the retail electric provider's control."

HB 16 amends PURA § 39.112 to increase this notice requirement. First, a retail provider must now provide *three* written notices, rather than one, specifying the date that the fixed rate product will expire. The notices must be provided during the last third of the contract period in evenly distributed intervals, when practicable. If a contract has a term of *more than four months*, the final notice of expiration must be provided at least 30 days before the date that the contract will expire. If a contract has a term of *less than four months*, the final notice of expiration must be provided at least 15 days before the date that the contract will expire. The final notice must include the pricing terms for the default renewal product.

The new law adds a requirement that the retail electric provider provide each notice by mail at the customer's billing address unless the customer has opted to receive communications electronically. An additional new provision requires that if the retail provider has access to the customer's telephone information, and the customer has agreed to receive notices by text or call, the provider may text or call the customer with additional notice of expiration. However, texts and calls are only supplementary and do not satisfy the notice requirement by themselves.

Default Renewal Products. HB 16 further amends PURA § 39.112 with regard to a retail provider's ability to move a customer to a default product when the customer's fixed rate product expires. Under new PURA § 39.112(i), a retail provider must include in each contract for service the terms of the default renewal product in which a customer will be automatically enrolled if the customer fails to select a new product before the current product expires. If a customer does not select another retail product before the expiration of the customer's contract term, the provider may automatically serve the customer through a default renewal product, but new PURA § 39.112(h) requires that the customer may cancel at any time without a fee, that the product be month-to-month (although the price may change between billing cycles), and that the product be based on terms that are designed to be easily understood by the average customer.

Failure to Notify. HB 16 also adds a new PURA § 39.112(j), providing that if a retail electric provider fails to provide notice in accordance with the new requirements and the customer does not select another retail electric product before the contract's expiration, the provider must continue to serve the customer under the prior fixed rate product until the provider gives the requisite notice or the customer selects another retail electric product.

All of the above changes to the regulation of retail electricity products become effective September 1, 2021, and the new laws will only apply to an enrollment or re-enrollment of a customer in a retail electric product that is executed on or after that date. The PUC has opened a rulemaking to implement the above changes in Project No. 51830. On June 25, 2021, the PUC published a strawman rule and comments were to be filed no later than July 6, 2021.

03 PART 3: CHANGES TO REDUCE THE RISK OF FUTURE ELECTRIC MARKET DISRUPTIONS

"Knowledgeable senior counsel who in fifteen minutes can provide what other firms charge hours of time to compile."

Legal 500 US, 2020

Part 3: Changes to Reduce the Risk of Future Electric Market Disruptions

The February 2021 winter storm occurred with more than three months remaining in the legislative session. Not surprisingly, the Legislature spent considerable time debating the causes of the resulting power outages and how to prevent future extreme weather events from having similar consequences. The session produced a number of new laws aimed at increasing preparedness for extreme weather.

BIENNIAL GRID RELIABILITY ASSESSMENT

SB 1281 creates a new PURA §39.159, which requires ERCOT to conduct a biennial assessment of the ERCOT power grid's reliability in extreme weather scenarios. Each assessment must consider the impact of different levels of thermal and renewable generation and must recommend transmission projects that will increase grid reliability. The new law takes effect on September 1, 2021.

TERC INFORMATION GATHERING AUTHORITY

SB 3 creates new TGC § 418.309 requiring that public utilities and gas providers must provide to the TERC any information requested related to a disaster. "Gas provider" is very broadly defined to include gas pipeline operators, gas well operators, and any entity that produces, treats, processes, pressurizes, stores, or transports natural gas or otherwise participates in the natural gas supply chain in Texas. Similarly, "public utility" is defined broadly to include any entity that generates, transmits, or distributes electricity to the public, and expressly includes electric cooperatives, electric utilities, municipally owned utilities, and river authorities. With some exceptions, information collected by the TERC is designated by the new law as confidential and exempt from open records requirements.

TEXAS ELECTRICITY SUPPLY CHAIN SECURITY AND MAPPING

SB 3 adds a new PURA Chapter 38, Subchapter F (PURA §§ 38.201-38.204) creating the TESCSMC (discussed further in Part 1). The new law defines the "electricity supply chain" very broadly to mean "(1) facilities and methods used for producing, treating, processing, pressurizing, storing, or transporting natural gas for delivery to electric generation facilities; and (2) critical infrastructure necessary to maintain electricity service." New PURA § 38.203 requires the TESCSMC to (a) map the Texas electricity supply chain to designate priority electric service needs during extreme weather; (b) identify sources in the electric supply chain necessary to operate critical infrastructure; (c) develop a communication system between critical infrastructure sources, the PUC, and ERCOT to ensure prioritization of electricity and natural gas supplies in the electricity supply chain during extreme weather; and (d) establish best practices to prepare the electricity supply chain to maintain service in extreme weather events. The energy supply chain map must be updated annually, and the TESCSMC is required to submit a report on the above tasks by January 1, 2022 and must complete the electricity supply chain map no later than September 1, 2022.

DESIGNATION AND REGULATION OF CRITICAL GAS SUPPLY CHAIN INFRASTRUCTURE AND CONSUMERS

Designation of Critical Facilities and Customers. SB 3 contains multiple provisions addressing, identifying, and designating critical providers and customers during weather emergencies to prioritize critical providers and customers during load shedding and power restoration. SB 3 creates a new NRC § 81.073 and a new PURA § 38.074 that, together, require the RRC and PUC to adopt rules to designate persons who own facilities or engage in operations under the TRRC's jurisdiction who must provide critical customer and critical gas supply information to ERCOT, electric utilities, municipally owned utilities, and electric cooperatives in ERCOT.

The PUC opened Project No. 51839 in March 2021 to address electric gas coordination, which will likely also have heavy overlap with a rulemaking on critical load (Project No. 51888). The PUC has not yet requested comments or provided a strawman rule.

Prioritization of Electric Service. Once designated as critical, new PURA § 38.074 requires that natural gas infrastructure be prioritized for purposes of load-shed during an energy emergency. Notably, however, each utility, cooperative, or municipal utility is granted discretion to prioritize power delivery and restoration among the critical facilities connected to its system.

Required Weatherization. Under new NRC § 81.073, only facilities that are prepared to operate during a weather emergency may be designated as critical customers. Moreover, gas supply chain operators that are included in the electricity supply chain map and designated as critical will be required by a new NRC § 86.044 to implement measures to prepare to operate during a weather emergency. The new NRC § 86.044 requires the Railroad Commission to inspect gas supply chain facilities for compliance, provide a reasonable amount of time to correct non-compliance, and report uncorrected violations to the attorney general. New NRC § 86.044 also requires the RRC to develop and implement a rule requiring a gas supply chain operator that experiences "repeated weather-related or major weather-related forced interruptions of production" to contract with a third party to assess the operator's weatherization efforts, submit the assessment to the RRC, and comply with any recommendations in the assessment if so ordered by the RRC. SB 3 amends Texas Utilities Code ("TUC") § 121.2015 to add similar provisions for operators of gas pipelines serving gas-fired generation facilities or included in the gas supply chain map. The RRC must adopt rules to implement NRC § 86.044 and TUC § 121.2015 not later than six months after the TESCSMC produces the electricity supply chain map (so, no later than March 1, 2023). New TUC § 186.008 requires the RRC to monitor and enforce emergency operations plans developed by operators in the electricity supply chain map and to submit a biennial report to the legislature on September 30 of each even numbered year.

WEATHERIZATION AND EMERGENCY PREPAREDNESS FOR ELECTRIC GENERATION

SB 3 adds a new PURA § 35.0021 that requires the PUC to craft and implement new rules requiring most providers of electric generation (municipally owned utilities, electric cooperatives, power generation companies, and exempt wholesale generators) to implement weatherization measures established by the PUC. It further requires ERCOT to inspect generation assets for compliance, to provide a reasonable time to correct the violation, and to report to the PUC any violation.

New PURA § 35.0021 also requires the PUC to develop and implement a rule requiring a provider of electric generation that experiences "repeated or major weather-related forced interruptions of service" to contract with a third party to assess the generator's weatherization efforts, submit the assessment to the PUC, and comply with any recommendations in the assessment if so ordered by the PUC. The PUC must adopt rules to implement PURA § 35.0021 not later than December 8, 2021 (six months after the June 8, 2021, effective date of SB 3). Accordingly, the PUC opened Project No. 51840 and requested comments from interested parties on June 9, 2021. Parties filed initial comments on June 23, 2021.

WEATHERIZATION AND EMERGENCY PREPAREDNESS FOR ELECTRIC UTILITIES

SB 3 adds a new PURA § 38.075 that requires the PUC to craft and implement new rules requiring electric cooperatives, municipally owned utilities, and transmission and distribution utilities in ERCOT to implement weatherization measures established by the PUC. It further requires ERCOT to inspect utility assets for compliance, to provide a reasonable time to correct the violation, and to report to the PUC continuing violations. Note that PURA § 38.075 does *not* include a provision similar to those found in NRC § 86.044 and PURA § 35.0021 requiring a third-party assessment in the event of repeated or major violations. The PUC will address these weatherization issues in Project No. 51840.

Currently, PURA allows electric utilities to securitize system restoration costs for mobilization, staging, and construction, reconstruction, replacement, or repair of facilities in response to weather-related events or natural disasters. HB 1510 (discussed in more detail in Part 4) expands the definition of system restoration costs in PURA § 36.402 to include "reasonable and necessary weatherization and storm-hardening costs" and adds a new PURA § 36.451 that authorizes and establishes a process for non-ERCOT utilities (which still own and operate generation assets) to securitize such weatherization and storm-hardening costs.

INCREASED PENALTY AUTHORITY FOR RRC AND PUC

SB 3 amends NRC § 86.222 and TUC § 121.206 (RRC), and PURA § 15.023 (PUC) to increase the penalty authority of the RRC and PUC for violation of the weatherization requirements adopted under NRC § 86.044, TUC § 121.2015, PURA § 35.0021, and PURA § 38.075. The amended laws require the RRC and PUC each to establish by rule a classification system for violations, and they provide that penalties may exceed $5,000 only if the violation is in the highest class of violations. However, for such violations, the new laws raise the maximum penalty to $1,000,000 per offense per day. That compares to prior maximum penalties of only $10,000 per offense per day (at the RRC for pollution-related offenses), $25,000 per offense per day (at the PUC), or $200,000 per offense per day (at the RRC for pipeline safety offenses).

Note a potentially significant difference between NRC § 86.044, TUC § 121.2015, and PURA § 38.075 (applicable to gas supply chain operators, gas pipelines, and utilities) and PURA § 35.0021 (applicable to electric generators). The former require reporting to the Attorney General or PUC only of a violation "that is not remedied in a reasonable period of time." In contrast, PURA § 35.0021 requires ERCOT to report to the PUC "any violation," although it authorizes penalties only for violations not remedied in a reasonable period of time. We will monitor the activity under all of these provisions to see if the reporting of violations differs in practice. As of June 30, 2021, the PUC had not yet opened a rulemaking to address this SB 3 requirement.

SB 3 also amends Texas Utilities Code ("TUC") § 105.023 to require the RRC to establish by rule a classification system for violations of the RRC's gas utility disconnection rules, and to provide that penalties may exceed $5,000 only if the violation is in the highest class of violations. However, for such violations, the new laws raise the maximum penalty from $5,000 per offense per day to a maximum of $1,000,000 per offense per day.

CLARIFICATION OF CRITICAL CUSTOMER STATUS AND PROCESS

SB 3 amends PURA § 17.002 to provide additional clarity regarding the classification of "critical care residential customers" and "critical load industrial customers." It further amends PURA § 17.003 to require that utilities provide to retail providers and retail providers provide to their customers the utility's procedures for involuntary load shedding and information on being classified as critical customers. SB 3 also amends PURA § 17.005 and 17.006 to include similar provisions for customers of municipally owned utilities and electric cooperatives, respectively. The PUC opened Project No. 51888 in March 2021 to address critical load standards, but has not yet issued a request for comments or a strawman rule.

NEW LOAD SHEDDING RULES

SB 3 adds a new PURA § 38.076 requiring the PUC to adopt new rules for allocating involuntary load shedding among electric cooperatives, municipal utilities, and transmission and distribution utilities in different seasons based on their historical peak demand. The new law further requires the PUC to adopt a rule categorizing and prioritizing critical load for power restoration and requiring such transmission service providers to submit to the PUC and ERCOT circuits designated as critical load and a plan for participating in involuntary load shedding. Following each load shedding event, the new law authorizes the PUC to investigate whether each such transmission service provider complied with its plan. New PURA § 38.077 requires the PUC and ERCOT to conduct simulated load shedding exercises, including at least one such exercise in the summer and winter of each year. The PUC must adopt rules to implement PURA § 38.075 not later than December 8, 2021 (six months after the June 8, 2021, effective date of SB 3).

04 PART 4: CHANGES TO ADDRESS THE COSTS OF THE FEBRUARY 2021 WINTER STORM

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Part 4: Changes to Address the Costs of the February 2021 Winter Storm

The February 2021 winter storm caused significant economic dislocations. Two large electric cooperatives and multiple other electric market participants defaulted on billions of dollars of payments due to ERCOT. As a result of those defaults, ERCOT has been unable to make the payments due to other electric market participants for energy and ancillary services provided during the storm. Absent legislative action, ERCOT's rules would provide for ERCOT to collect the default amounts from remaining market participants, a process known as a "default uplift." However, ERCOT's rules limit the frequency and amount of default uplifts such that recovery of the default amounts resulting from the winter storm would require decades to collect, and the uplift burden could force additional market participants into default. In addition to the defaults on amounts owed to ERCOT, disruptions in the natural gas market led to high market prices that drove up the costs of gas utilities and gas-fired electric generators throughout the state. Four bills passed by the Legislature and signed by Governor Abbott attempt to address these economic dislocations resulting from the winter storm.

The new laws rely heavily on securitization—the issuance of low-interest bonds funded by non-bypassable charges on customer bills—to raise funds to address current economic dislocations, and to spread repayment of those funds over large groups of customers and over extended time periods. The Legislature first created a securitization framework in PURA Chapter 39, Subchapter G (PURA §§ 39.301-39.313) to permit the recovery of utility stranded costs that arose in connection with the unbundling of ERCOT utilities in the early 2000s. Later, in the wake of Hurricane Ike in 2008, the 2009 Legislature added PURA Chapter 36, Subchapter I (PURA §§ 36.401-406), allowing utilities to use the Chapter 39, Subchapter G process to securitize storm restoration costs. Those existing laws offered a framework for addressing the economic dislocations occasioned by the February 2021 winter storm.

SECURITIZATION OF WEATHERIZATION, STORM HARDENING, AND SYSTEM RESTORATION COSTS FOR NON-ERCOT UTILITIES

HB 1510, effective immediately upon its signature by Governor Abbott on June 1, 2021, authorizes and establishes a process for non-ERCOT utilities—which, unlike ERCOT utilities, still own and operate generation assets—to recover the costs of weatherization, storm hardening, and system restoration costs through securitization. HB 1510 amends and expands the definition of "system restoration costs" in PURA § 36.402 to include "reasonable and necessary weatherization and storm-hardening costs incurred, as well as reasonable estimates of costs to be incurred, by the electric utility, but such estimates shall be subject to true-up and reconciliation after the actual costs are known." HB 1510 then adds a new PURA Chapter 36, Subchapter J (PURA §§ 36.451-36.457), entitled "Lower-Cost Financing Mechanism for Securitization for Recovery of System Restoration Costs. New PURA § 36.401(b) limits the purpose of the new law to electric utilities "operating solely outside of ERCOT." Subchapter J generally incorporates the securitization process codified in Chapter 39, Subchapter G and Chapter 36, Subchapter I with certain specified modifications.

Issuing Entity. Unlike prior securitization statutes, which authorize the utility itself (or a special purpose affiliate) to issue bonds, HB 1510 creates the Texas Electric Utility System Restoration Corporation ("TEUSRC") as a special purpose public corporation for that purpose. New PURA § 36.451(e) provides that the bonds are solely the obligation of the new TEUSRC. Use of the TEUSRC is intended to ensure that the bonds need not be reflected as debt on the utility's books. New PURA § 36.453 governs the creation and governance of the TEUSRC and provides in subsection (h) that it shall be governed by a board of five directors appointed by the PUC for two-year terms. At the same time, new PURA § 36.455 provides that the PUC shall regulate the TEUSRC. New PURA § 36.454 sets out the powers and duties of the TEUSRC, including the power to issue system restoration bonds consistent with a financing order from the PUC.

Qualified Costs. New PURA § 36.452(b) defines "qualified costs," which may be included in securitizations under Chapter 39, Subchapter G, to include all costs of establishing, maintaining, and operating the TEUSRC and all costs of the TEUSRC in connection with issuance and servicing of the bonds.

Determination of Amount to be Financed. Under the provisions of PURA § 36.405, incorporated by the new Subchapter J securitization framework, a utility must file an application with the PUC seeking a determination of the system restoration costs eligible for recovery and securitization. The PUC must issue an order determining such amount no later than 150 days after the utility files its application.

Financing Order. The PUC must issue a financing order as provided in Chapter 39, Subchapter G and Chapter 36, Subchapter I. The PUC must issue the financing order through a contested case to which the TEUSRC must be a party. The financing order must:

- authorize the creation of "transition property," which in this case will be the proceeds from a non-bypassable system restoration charge included on a utility's bills;
- authorize the issuance of system restoration bonds by the TEUSRC and the exchange of the bond proceeds for the transition property; and
- authorize the utility to act as collection agent for the system restoration charges and to transfer them to the TEUSRC.

The utility may file an application for a financing order before the expiration of the 150-day period for determination of the recoverable and securitizable amount. The PUC must issue a financing order within 90 days of the utility's application, but not before it determines the amount that is recoverable and securitizable.

Finding of Customer Benefit. New PURA § 36.451(d) requires that the PUC, before issuing a financing order, "ensure that customers are not harmed as a result of any financing through the [TEUSRC] and that any financial savings or other benefits are appropriately reflected in customer rates.

Non-bypassable Charges. Existing PURA §§ 36.404 and 39.306, incorporated by reference in HB 1510, require a financing order to ensure that any system restoration charges authorized by the financing order shall be non-bypassable.

Offsets and Clawbacks. Under existing PURA § 36.402(c), which is incorporated by reference into HB 1510, to the extent a utility receives insurance proceeds, government grants, or other sources of compensation for system

restoration costs, those amounts must directly offset the amounts to be securitized or, if already included in a securitization, accounted for in the utility's next rate case or a subsequent proceeding that considers system restoration costs.

Cap. HB 1510 imposes no cap on the securitization of non-ERCOT utility weatherization, storm-hardening, or storm restoration costs; but PURA § 36.403(j), incorporated by the new Subchapter J, limits the availability of the securitization process to instances in which a utility has incurred system restoration costs of $100 million or more in a single calendar year.

Term of System Restoration Charges. Existing PURA § 39.303(b), incorporated by reference in HB 1510, requires that the period over which system restoration charges are recovered may not exceed 15 years.

Period Covered. The securitization framework created by HB 1510 is not limited to system restoration costs incurred in connection with the February 2021 winter storm.

SECURITIZATION OF ELECTRIC COOPERATIVE ERCOT DEFAULT AMOUNTS

SB 1580, effective immediately upon its signature by Governor Abbott on June 18, 2021, establishes a process for electric cooperatives to use securitization financing to recover extraordinary costs and expenses incurred due to the February 2021 winter storm and owed to ERCOT. SB 1580 amends PURA Chapter 41, the primary chapter devoted to regulation of electric cooperatives, to add a new Subchapter D (PURA §§ 41.151-41.163). New PURA § 41.151 authorizes cooperatives, individually or in groups, to use securitization to raise funds that must then be paid immediately to ERCOT to satisfy outstanding cooperative obligations to ERCOT for "extraordinary costs and expenses." New PURA § 41.152(4) defines "extraordinary costs and expenses" to include (A) costs for power and energy in excess of what the cooperative would have paid for the same amount of power and energy based on its average costs during January 2021; (B) the cooperative's own costs to generate and transmit power and energy during the winter storm that would not have been incurred but for the storm; and (C) any ERCOT default uplift charges imposed on the cooperative or imposed on a power supplier to the cooperative and passed on to the cooperative.

Issuing Entity. Under new PURA § 41.153, the board of the cooperative issues (or the boards of cooperatives acting jointly issue) the bonds.

Qualified Costs. New PURA § 41.152(7) defines "qualified costs," which are eligible for recovery and securitization, to include not only (A) the cooperatives extraordinary costs and expenses and (B) its costs of issuing and servicing the bonds, but also (C) its cost of retiring and refunding its existing debt securities initially issued to finance the extraordinary costs and expenses.

Determination of Amount to be Securitized. The board of the cooperative determines the amount of qualified costs eligible for recovery and securitization. The new law includes no provision for outside review of the board's determination.

Financing Order. The board of the cooperative must issue a financing order subject to the provisions of new PURA § 41.153. The financing order must state the amount to be recovered and the period over which the non-bypassable charges are to be recovered. New PURA § 41.153(e) provides very limited appeal rights to members of the cooperative. A member may appeal for review of the financing order by a district court not later than the 15th day

after the board adopts the financing order, with direct appeal from the district court to the Texas Supreme Court. Review at both the district court and Supreme Court takes precedence over other matters, is based on the financing order and a limited record, and is limited to whether the financing order complies with the constitution and laws of Texas and the United States and is within the authority of the board under the new Subchapter D.

Finding of Customer Benefit. New PURA § 41.151(a) requires that the board of a cooperative using securitization under the new law must ensure that the securitization provides tangible and quantifiable benefits to its members, greater than would have been achieved absent the issuance of securitized bonds.

Non-bypassable Charges. New PURA § 41.156 provides that the financing order issued by the board of the electric cooperative must include terms ensuring that the collection of securitized charges authorized in the order shall be non-bypassable and apply to all customers connected to the cooperative's system assets and taking service, even if those system assets cease to be owned by the cooperative.

Offsets and Clawbacks. Under new PURA § 41.157(a), if there are reductions or refunds after the adoption of a financing order, then the financing order must be adjusted to ensure that there is not an overcollection. (Similarly, the financing order must be adjusted to avoid under-collections.)

Cap. SB 1580 imposes no cap on the securitization of a cooperative's extraordinary costs and expenses.

Term of Non-bypassable Charges. Under new PURA § 41.153(b), the period over which the non-bypassable securitized charges shall be recovered may not exceed 30 years.

Period Covered. New PURA §§ 41.151 and 41.152(8) limit this securitization tool to extraordinary costs and expenses incurred during the period of emergency, defined as February 12, 2021 through February 20, 2021.

USE OF RAINY-DAY FUNDS TO FINANCE NON-ELECTRIC COOPERATIVE ERCOT DEFAULT AMOUNTS

HB 4492, effective immediately upon signature by the Governor on June 16, 2021, directs the investment of up to $800 million from the state's economic stabilization fund (commonly known as the "Rainy Day Fund") to finance the ERCOT default balance that would otherwise be paid by all remaining market participants through ERCOT default uplift charges. The $800 million amount is (roughly) the commonly reported amount of total ERCOT defaults less the commonly reported portion of that total accounted for by electric cooperative defaults (which are financed separately under SB 1580, discussed above). The purposes of HB 4492, found in new PURA § 39.601(b) and reflected in new PURA § 39.602(1) are to (1) allow wholesale market participants that are owed money through ERCOT to be paid more quickly; (2) replenish financial revenue auction receipts temporarily used by ERCOT to reduce short payments related to the winter storm; and (3) allow the wholesale market to repay the default balance over time.

Issuing Entity. Unlike the other statutory measures described in Part 4, HB 4492 allows but does not require securitization and the issuance of bonds. Instead, through new TGC § 404.0241(b-1), HB 4492 directs the state comptroller to invest and manage a portion of the state Rainy Day Fund to finance the ERCOT default. New TGC § 404.0241(b-4) requires the comptroller to manage the investments as a separate investment portfolio, with separate accounting and reporting. New TGC § 404(b-5) gives the comptroller "any power necessary" to manage and invest the new portfolio. The use of the existing Rainy-Day Fund presumably allows the financing of the default balance more quickly than would a securitization process. The interest rate on the borrowed Rainy-Day Funds must

be set at the Municipal Market Data Municipal Electric Index ("MMDMEI"), as published by Refinitiv TM3, based on the credit rating of ERCOT, plus 2.5 percent.

In addition to the Rainy-Day Fund financing, however, new PURA § 39.604 provides that the PUC "may" (but is not required to) contract with another state agency to undertake a securitization for payment of the default balances. Such a securitization would presumably take longer than the Rainy-Day Fund financing but, when complete, would allow repayment of the Rainy-Day Fund and could produce a lower interest rate than the MMDMEI.

Qualified Costs. While HB 4492 does not reference "qualified costs" like the securitization statutes discussed in this Part 4, it does nevertheless include in the "default balance" to be financed the reasonable cost of a state agency or ERCOT to implement the financing.

Financing Order. New PURA §39.603 sets out the process for ERCOT to request and the PUC to issue a debt obligation order. On application by ERCOT, the PUC may issue an order authorizing ERCOT to establish a debt financing mechanism to finance the default balance. The PUC's order must state the default balance to be financed and the period over which non-bypassable default charges must be assessed to repay the debt obligations. The PUC must issue an order, approving or denying ERCOT's request, within 90 days of the application. As with the securitization frameworks described in this Part 4, new PURA § 39.603(h) prescribes an expedited appeal process, with no requirement for rehearing, 15-day appeal deadlines, and an expedited appellate process first at the Travis County district courts and then straight to the Texas Supreme Court.

If the PUC elects to use a securitization under new PURA § 39.604, it must issue a financing order that meets the same requirements as a debt obligation order issued under new PURA § 39.603 for the Rainy-Day Fund financing.

Finding of Customer Benefit. To issue a debt obligation order under new PURA § 39.603, the PUC must make an affirmative finding that the debt obligations are needed to preserve the integrity of the wholesale market and the public interest. The PUC must consider (1) the need to timely replenish financial revenue auction receipts previously used by ERCOT to reduce short payments; (2) the interests of wholesale market participants who are still owed payment through ERCOT; and (3) the potential effects of an ERCOT default uplift in the absence of a financing vehicle.

Non-bypassable Charges. New PURA § 39.603(d) requires ERCOT to collect from and allocate among wholesale market participants new "default charges" using the same pro rata allocation that would have been used under ERCOT's default uplift rule as of March 1, 2021. The default charges must be assessed on all market participants participating in the market, and ERCOT is permitted to base the allocation on periodically updated transaction information to prevent market participants from engaging in behavior designed to avoid the charges. New PURA § 39.605 requires that a financing order, whether or the Rainy-Day Fund financing or a securitization, include terms making the default charges non-bypassable.

Offsets and Clawbacks. Under new PURA § 39.606, a financing order must include a "true-up" mechanism requiring review at least annually to correct over-collections or under-collections over the preceding 12 months, but there is no express mention of insurance or litigation proceeds.

Cap. The amount that can be taken from the Rainy-Day Fund to finance ERCOT default amounts is capped by new PURA § 39.602(1) at $800 million. Moreover, HB 4492 adds a new PURA § 39.159 (one of several new provisions confusingly assigned that same number) that requires all market participants to fully and promptly pay all amounts

owed to ERCOT or be precluded from continuing to be a market participant, including a prohibition on ERCOT from accepting a defaulting market participant's loads or generation for scheduling until all amounts owed have been fully paid.

Lubbock Power & Light Carve Out. New PURA § 39.151(j-1) prevents ERCOT from reducing payments to or uplifting short-paid amounts to a municipally owned utility that becomes subject to ERCOT jurisdiction on or after May 29, 2021, and before December 30, 2021, related to a default by a market participant that occurred before May 29th. This provision will almost certainly apply only to Lubbock Power & Light, which transitioned from the Southwest Power Pool to ERCOT over the 2021 Memorial Day weekend.

Term of Financing. Under new TGC § 404.0241(b-1), the term of the debt obligations may not exceed 30 years.

Period Covered. HB 4492 makes clear in new PURA § 39.602(4) that it applies only to the financing of default amounts arising as a result of the emergency period of February 12 through February 20, 2021.

SECURITIZATION OF WINTER STORM UPLIFT BALANCE

HB 4492 also adds to PURA a new Subchapter N (PURA §§ 39.651-39.664), which provides for financing of the "uplift balance" owed by load serving entities (municipally owned utilities, electric cooperatives, and retail electric providers) ("LSEs"). New PURA § 39.652(4) defines the uplift balance as an amount of money of not more than $2.1 billion that was uplifted to LSEs on a load ratio share basis due to energy consumption during the winter storm for reliability deployment price adder charges and ancillary services costs in excess of the PUC's system-wide offer cap. These are amounts that ERCOT paid for power and ancillary services, at scarcity prices, that were subsequently charged out to LSEs based on their relative share of ERCOT load.

Issuing Entity. HB 4492 provides the PUC flexibility in how it may finance the uplift balance. First, new PURA § 39.653 authorizes the PUC, upon application of ERCOT, to "establish a debt financing mechanism for the payment of the uplift balance." HB 4492 (Section 6) requires ERCOT to make such a filing by July 16, 2021 (not later than the 30th day after the effective date of HB 4492). Second, new PURA § 39.654 allows, but does not require, the PUC to contract with another state agency with expertise in public financing to undertake a securitization or other form of public financing. Third, new PURA § 39.655 allows the PUC to use a financial mechanism other than the ones described in PURA §§ 39.653 and 39.654 that meets the requirements of the new PURA Subchapter N.

Qualified Costs. While HB 4492 does not reference "qualified costs" like other statutes discussed in this Part 4, new PURA § 39.652(5) defines "uplift charges" to include reasonable costs incurred by a state agency or ERCOT to implement a debt obligation order, and new PURA § 39.654 indicates that the application of funds raised through a financing is to be net of issuance costs.

Determination of Uplift Balance. New PURA § 39.653(b)(3) requires that a debt obligation order provide a process for remitting financing proceeds to participating LSEs, including a requirement for the LSEs to submit documentation of their exposure. This means that LSEs wishing to take advantage of the uplift balance financing will need to participate in the PUC proceeding to issue a debt obligation order and will need to prove up their share of the uplift balance.

Financing Order. New PURA §39.653 sets out the process for ERCOT to request and the PUC to issue a debt obligation order. On application by ERCOT, the PUC may issue an order authorizing ERCOT to establish a debt

financing mechanism for the payment of the uplift balance. The PUC's order must state the uplift balance to be financed and the period over which non-bypassable uplift charges must be assessed to repay the debt obligations. The PUC must issue an order, approving or denying ERCOT's request, within 90 days of the application. As with the other financing frameworks described in this Part 4, new PURA § 39.653(g) prescribes an expedited appeal process, with no requirement for rehearing, 15-day appeal deadlines, and an expedited appellate process first at the Travis County district courts and then straight to the Texas Supreme Court.

If the PUC elects to use a public finance mechanism under new PURA § 39.654, it must issue a financing order that meets the same requirements as a debt obligation order issued under new PURA § 39.653. If the PUC opts to exercise the flexibility offered by new PURA § 39.655, there is no similar, express requirement that an order adhere to the requirements of § 39.653.

Finding of Customer Benefit. HB 4492 includes new PURA § 39.651, which contains legislative findings that financing the uplift balance as provided in new PURA Subchapter N will allow payment of uplift amounts by LSEs over a longer period of time, "alleviating liquidity issues and reducing the risk of additional defaults in the wholesale market" and will serve the public purpose of allowing the PUC to stabilize the wholesale electricity market in ERCOT. New PURA § 39.653 requires that, before issuing a debt obligation order, the PUC must find that the proposed financing will "support the financial integrity of the wholesale market and is necessary to protect the public interest, considering the impacts on both wholesale market participants and retail customers."

Non-bypassable Charges. New PURA § 39.653(c) requires ERCOT to assess uplift charges to all LSEs on a load ratio share basis, including LSEs that enter the market after a debt obligation order is issued. New PURA § 39.656 requires that, regardless of the financing option chosen by the P C, the PUC's debt obligation order must include terms making the uplift charges non-bypassable. New PURA § 39.653(d) allows municipally owned utilities, electric cooperatives, river authorities, LSEs serving only themselves or their affiliates, and transmission service customers served by a retail electric provider to opt out of the uplift balance financing. Entities that opt out are exempt from uplift charges but may not receive any proceeds from the uplift balance financing. Under new PURA § 39.660, LSEs that receive proceeds from the uplift balance financing must pass those proceeds on to their customers who have previously paid or would otherwise be required to pay a portion of the uplift balance.

Offsets and Clawbacks. Under new PURA § 39.664, a load serving entity that has received proceeds from a financing under new Subchapter N must return an amount of the proceeds equal to any amount it receives due to litigation seeking judicial review of pricing or uplift actions by the PUC or ERCOT in connection with the winter storm. We note that the language of this provision appears to include amounts received due to litigation in which the recipient was not directly involved.

Cap. New PURA § 39.652(4) defines the "uplift balance" as an amount of "not more than $2.1 billion."

Term of Financing. Under new PURA § 39.653(b)(2), the term of the debt obligations may not exceed 30 years.

Period Covered. HB 4492 makes clear in new PURA §§ 39.651(d), 39.652(3) and (4), and 39.653(e) that the uplift balance financing applies only to the emergency period of February 12 through February 20, 2021.

SECURITIZATION OF EXTRAORDINARY GAS UTILITY COSTS

HB 1520, effective immediately upon signature by the Governor on June 16, 2021, establishes a process for gas utilities to use securitization to recover certain extraordinary costs incurred during the February 2021 winter storm. HB 1520 amends both the Texas Government Code and the portion of the Texas Utilities Code known as the Gas Utilities Regulatory Act ("GURA") (TUC §§ 101.001-105.051) to create a securitization process that relies on two existing state agencies: the Texas Public Finance Authority ("TPFA") and the RRC. In Chapter 1232 of the TGC, which creates the TPFA, HB 1520 amends TGC § 1232.002 to add a new purpose for the agency—to provide a method of financing for "customer rate relief bonds" authorized by the RRC. HB 1520 also amends GURA to add a new Subchapter I (GURA §§ 104.361-104.380) entitled "Customer Rate Relief Bonds."

Issuing Entity. To issue the securitization bonds, HB 1520 turns to the existing TPFA. Under prior law, the purpose of TGC Chapter 1232 was limited to the acquisition or construction of buildings and the purchase or lease of equipment by executive or judicial branch state agencies. With the passage of SB 7 in 1999, the bill that overhauled the ERCOT market and established retail electric competition in ERCOT, the TPFA's authority was expanded to include financing the stranded costs of a municipal power agency. Perhaps following that lead, HB 1520 now adds to the TPFA's authority the financing of customer relief bonds issued by the RRC under GURA Subchapter I. TPFA is now authorized by new TGC § 1232.1072 to create a non-profit entity, governed by three uncompensated members appointed by the TPFA, to issue bonds in accordance with a financing order from the RRC.

Qualified Costs. HB 1520 does not use the term "qualified costs," but does authorize the recovery and securitization of various financing costs in addition to a gas utility's extraordinary winter storm costs held in one or more regulatory assets. Under new GURA § 104.366(a), the RRC must first determine the total amount of extraordinary costs recoverable by *all* applying gas utilities, and then conduct a single securitization for the aggregate amount to be recovered.

Determination of Amount to be Securitized. New GURA § 104.365 requires the RRC, on application by a gas utility to recover its extraordinary winter storm costs, in the form of a regulatory asset, to determine the amount properly recoverable. Gas utilities wishing to avail themselves of this securitization tool must file an application at the RRC on or before the 60th day after the June 16th effective date of HB 1520 (meaning on or before August 15, 2021). If the RRC does not make a determination before the 151st day after a gas utility files its application, that application is deemed to have been approved as submitted. There is no rehearing, and any appeal must be made to a Travis County district court not later than the 15th day after the RRC signs its order. Appeal from the district court goes directly to the Texas Supreme Court, again with a 15-day deadline. Appeals from an RRC order under new GURA § 104.365 are given precedence over other matters before the reviewing courts.

Financing Order. New GURA § 104.366 governs the issuance by the RRC of a financing order. As noted above, the RRC must issue a single financing order, after resolution of all applications for recovery timely filed by gas utilities, covering all costs to be recovered and securitized.

Finding of Customer Benefit. New GURA § 104.366(a) requires that the RRC issue a financing order and authorize recovery and securitization of gas utility extraordinary costs only after determining that customer rate relief bond financing is the most cost-effective method of funding regulatory asset reimbursements to gas utilities. New GURA § 104.366(b) requires that the RRC may make such a determination only after considering customer affordability

and comparing the estimated monthly cost to customers of the customer rate relief bonds with the estimated monthly cost to customers of conventional recovery methods, such as using the gas utility's typical gas cost recovery mechanism.

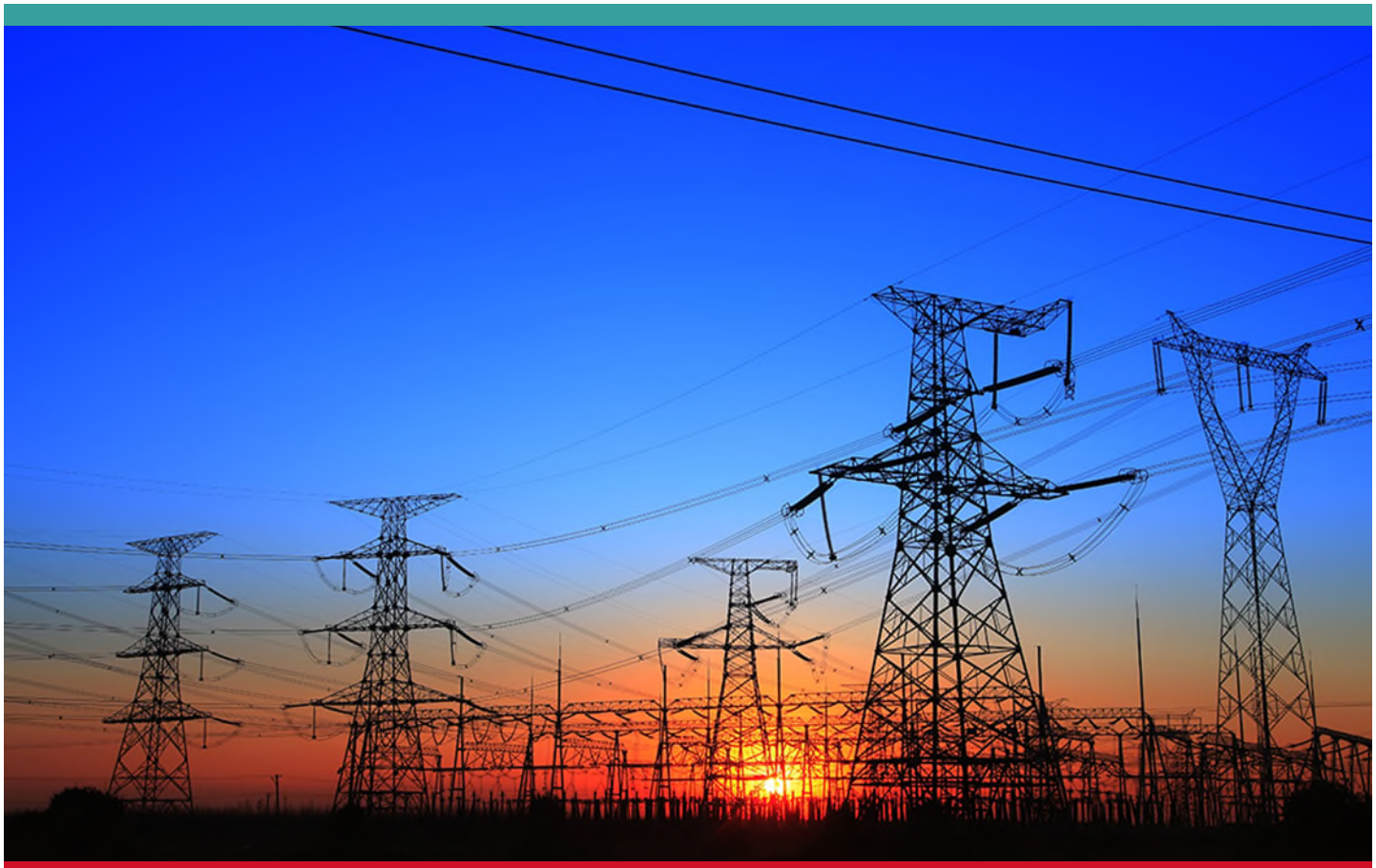
Non-bypassable Charges. HB 1520 adds new GURA § 104.362(7), defining "customer rate relief charges" as non-bypassable charges imposed on and included in customer bills of gas utilities that have received a regulatory asset determination and that are paid by all existing or future customers of such gas utilities even if customers elect to purchase gas from alternative suppliers in the future.

Offsets and Clawbacks. Under new GURA § 104.365(i), if a gas utility receives insurance proceeds, grants, or other sources of funding that compensate or indemnify the utility for extraordinary winter storm gas costs after the issuance of customer rate relief bonds, the utility "may" record those amounts in a regulatory liability for consideration in a future proceeding. Similarly, if an audit under a valid gas purchase agreement changes a gas utility's gas supply costs by more than 5% of the utility's total winter storm gas costs, the utility "may" record the change in a regulatory liability or asset for consideration in a future proceeding.

Cap. HB 1520 creates new GURA § 104.366(c)(5)(A), which caps the aggregate securitization for all utilities at $10 billion for any separate bond issue. In combination with the requirement for a single financing order covering all gas utilities and the limitation of the securitization provision to amounts incurred in connection with the February 2021 winter storm, this appears to be a hard cap. It is our understanding, however, through conversation with market participants, that this cap is expected to allow full recovery by all gas utilities that wish to participate.

Term of Non-bypassable Charges. Under new GURA § 104.366(c)(5)(A), the period over which the non-bypassable securitized charges are scheduled to be recovered may not exceed 30 years.

Period Covered. New GURA § 104.361 limits the purpose of new Subchapter I to the recovery of extraordinary costs incurred during the February 2021 winter storm and new GURA § 104.363 defines the extraordinary costs that are recoverable and securitizable as limited to those related to the February 2021 winter storm.



APPX ADDITIONAL RESOURCES

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Links and Documents

HOUSE BILLS

- HB 16
- HB 1510
- HB 1520
- HB 4492

SENATE BILLS

- SB 2
- SB 3
- SB 1281
- SB 1580
- SB 2154

PUBLIC UTILITY COMMISSION OF TEXAS RULEMAKING PROJECTS

- Project 51715 (Rulemaking Calendar)
- Project 51830 (Review of REP Customer Protection Rules)
- Project 51839 (Electric-Gas Coordination)
- Project 51840 (Electric Weatherization Standards)
- Project 51871 (Review of the ERCOT Scarcity Pricing Mechanism)
- Project 51888 (Review of Critical Load Standards and Processes)

OTHER USEFUL DOCUMENTS

- Membership of Texas Energy Reliability Council (TERC)

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