



## **Item 8.3: Review of Audited Financial Statements – REVISED**

*Sean Taylor*

Vice President and Chief Financial Officer

Finance and Audit Committee Meeting

ERCOT Public

April 27, 2022

Revised 4/26/2022



# Consolidated Financial Statements

Electric Reliability Council of Texas, Inc.  
Years ended December 31, 2021 and 2020  
With Independent Auditors' Report

April 2022

Electric Reliability Council of Texas, Inc.

Consolidated Financial Statements

As of and for the Years Ended  
December 31, 2021 and 2020

**Contents**

Independent Auditors' Report.....	1
-----------------------------------	---

Financial Statements

Consolidated Statements of Financial Position .....	3
Consolidated Statements of Activities and Net Assets .....	5
Consolidated Statements of Cash Flows.....	6
Notes to Consolidated Financial Statements .....	8

Supplementary Information

Consolidating Statements of Financial Position Information .....	44
Consolidating Statements of Activities and Net Assets Information .....	46
Consolidating Statements of Cash Flow Information.....	47

## **Independent Auditors' Report**

The Board of Directors and the Finance and Audit Committee of  
Electric Reliability Council of Texas, Inc.

### ***Opinion***

We have audited the accompanying consolidated financial statements of Electric Reliability Council of Texas, Inc. ("ERCOT"), which comprise the consolidated statements of financial position as of December 31, 2021 and 2020, and the related consolidated statements of activities and net assets and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of ERCOT as of December 31, 2021 and 2020, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Basis for Opinion***

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are required to be independent of the Organization and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Emphasis of Matter***

As discussed in Note 12 to the consolidated financial statements, ERCOT has been impacted by legislative, regulatory, legal and market participant responses resulting from Winter Storm Uri in February 2021. Our opinion is not modified with respect to this matter.

### ***Responsibilities of Management for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about ERCOT's ability to continue as a going concern within one year after the date that the consolidated financial statements are available to be issued.

## ***Auditors' Responsibilities for the Audit of the Consolidated Financial Statements***

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of ERCOT's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about ERCOT's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings and certain internal control-related matters that we identified during the audit.

### ***Supplementary Information***

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information as identified in the Table of Contents is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, changes in net assets and cash flows of the individual organizations, and it is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Minneapolis, Minnesota

**Date of Report**



Electric Reliability Council of Texas, Inc.  
Consolidated Statements of Financial Position

	December 31	
	2021	2020
	(In Thousands)	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 1,099,267	\$ 996,337
Accounts receivable	18,975	5,023
Unbilled revenue	9,132	2,607
Restricted cash and cash equivalents	1,135,962	658,559
Short-term investments	-	102,965
Prepaid expenses and other current assets	25,382	26,788
Total current assets	2,288,718	1,792,279
Property and equipment, net	115,632	109,356
Systems under development	40,209	27,522
Default charges receivable, non-current	784,181	-
Other long-term assets	867	1,042
Total assets	<u>\$3,229,607</u>	<u>\$1,930,199</u>

See accompanying notes to the consolidated financial statements

Electric Reliability Council of Texas, Inc.

Consolidated Statements of Financial Position (continued)

	December 31	
	2021	2020
	(In Thousands)	
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable	\$ 3,108	\$ 3,472
Accrued liabilities	29,266	18,230
Finance lease liabilities current	12,642	-
Deferred revenue	1,072	960
Market settlement liabilities	586,884	689,383
Security deposits and reserves	1,135,962	658,559
Debt payable, current portion	8,244	4,000
Total current liabilities	1,777,178	1,374,604
Debt payable, less current portion:		
Principal	834,756	43,000
Less unamortized debt issuance costs	2,055	173
Debt payable, less current portion and unamortized debt issuance costs	832,701	42,827
Long-term CRR liabilities	488,594	377,047
Other long-term liabilities	659	597
Total liabilities	3,099,132	1,795,075
Net assets without donor restrictions	130,475	135,124
Total liabilities and net assets	<u>\$3,229,607</u>	<u>\$1,930,199</u>

See accompanying notes to the consolidated financial statements

Electric Reliability Council of Texas, Inc.

Consolidated Statements of Activities and Net Assets

	Year Ended December 31	
	2021	2020
	<i>(In Thousands)</i>	
<b>Operating revenues:</b>		
System administration fees	\$ 218,339	\$ 212,185
Other services revenue	11,283	6,866
Default charges fees	3,273	-
Total operating revenues	232,895	219,051
<b>Operating expenses:</b>		
Salaries and related benefits	123,635	119,099
Hardware and software maintenance and licensing	32,808	29,712
Outside services	27,060	16,586
Facility and equipment costs	10,860	9,472
Depreciation	27,902	30,142
Other	11,020	6,701
Total operating expenses	233,285	211,712
(Loss) income from operations	(390)	7,339
<b>Other income (expense):</b>		
Investment return, net	200	4,298
Interest expense	(4,461)	(1,576)
Non-operating income	2	23
Change in net assets without donor restrictions	(4,649)	10,084
Net assets without donor restrictions, beginning of year	135,124	125,040
Net assets without donor restrictions, end of year	<u>\$ 130,475</u>	<u>\$ 135,124</u>

See accompanying notes to the consolidated financial statements



Electric Reliability Council of Texas, Inc.

Consolidated Statements of Cash Flows

	Year Ended December 31	
	2021	2020
	(In Thousands)	
<b>Operating activities</b>		
Change in net assets without donor restrictions	\$ (4,649)	\$ 10,084
Adjustments to reconcile change in net assets without donor restrictions to net cash provided by operating activities:		
Depreciation/amortization of assets	27,902	30,142
Amortization of debt issuance costs	26	17
Interest expense accrual on finance lease liabilities	5	-
Amortization of bond premium (discount)	290	(100)
Net gain on property, equipment and systems under development	(1)	-
Changes in operating assets and liabilities:		
Accounts receivable	(13,952)	833
Unbilled revenue	(6,525)	(90)
Prepaid expenses and other current assets	1,406	2,807
Default charges receivable, non-current	(784,181)	-
Other long-term assets	175	(1,042)
Other long-term liabilities	62	238
Accounts payable	(247)	1,282
Accrued liabilities	10,028	2,118
Deferred revenue	112	117
Security deposits and reserves	477,403	154,750
Market settlement liabilities	(102,499)	(2,531)
Long-term CRR liabilities	111,547	17,702
Net cash (used in) provided by operating activities	(283,098)	216,327
<b>Investing activities</b>		
Purchase of investments	(27,830)	(310,466)
Proceeds from investments	130,505	309,698
Capital expenditures for property and equipment and systems under development	(33,338)	(33,502)
Proceeds from sale of property and equipment	2	-
Net cash provided by (used in) investing activities	69,339	(34,270)

See accompanying notes to the consolidated financial statements

Electric Reliability Council of Texas, Inc.

Consolidated Statements of Cash Flows (continued)

	Year Ended December 31	
	2021	2020
	<i>(In Thousands)</i>	
<b>Financing activities</b>		
Proceeds from debt issuance	800,000	-
Repayment of debt payable	(4,000)	(4,000)
Payment of debt issuance costs	(1,908)	(20)
Net cash provided by (used in) financing activities	794,092	(4,020)
Net increase in cash, cash equivalents, and restricted cash and cash equivalents	580,333	178,037
Cash, cash equivalents, and restricted cash and cash equivalents, beginning of year	1,654,896	1,476,859
Cash, cash equivalents, and restricted cash and cash equivalents, end of year	\$2,235,229	\$1,654,896
<b>Supplemental information</b>		
Cash paid for interest	\$ 1,517	\$ 1,638
<b>Supplemental disclosures of non-cash investing and financing activities</b>		
Change in accrued capital expenditures	\$ 891	\$ 147
Capitalized interest	\$ 766	\$ 503
Right of use assets obtained for financing lease liabilities	\$ 12,637	\$ -

See accompanying notes to the consolidated financial statements

# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

### 1. Organization and Operations

The consolidated financial statements include the accounts of Electric Reliability Council of Texas, Inc. (ERCOT) and Texas Electric Market Stabilization Funding M LLC (TEMSFM) because ERCOT has both control and an economic interest in TEMSFM.

#### **Electric Reliability Council of Texas, Inc. (ERCOT)**

ERCOT is a Texas, non-profit corporation. ERCOT functions as the independent system operator for its reliability region, which comprises about 90% of the electrical load in Texas. The ERCOT region has more than 86,000 megawatts of available capacity for the summer peak demand period.

The Public Utility Commission of Texas (PUCT) has primary jurisdictional authority over ERCOT, which is responsible for ensuring the adequacy and reliability of electricity across the state's main interconnected power grid and for operating and settling the electricity markets it administers. ERCOT's market rules and operations are carried out in accordance with its Protocols filed with the PUCT. The ERCOT electric service region is contained completely within the borders of Texas, and it has only a few direct current ties across state lines to import or export power with neighboring reliability regions. ERCOT has no synchronous connections (alternating current) across state lines. As a result, ERCOT is considered "intrastate" and does not fall under the jurisdiction of the Federal Energy Regulatory Commission except for reliability issues under the provisions of the Federal Energy Policy Act of 2005.

ERCOT is governed by a Board of Directors, the membership of which is established by Texas statute, that is, the Public Utility Regulatory Act (PURA). In 2021, the portion of PURA governing the composition of the ERCOT Board of Directors was amended by Texas Senate Bill 2. Prior to implementation of Senate Bill 2, the Board of Directors was composed of 16 directors (15 voting and one non-voting). Six of the voting directors represented segments of industry in the ERCOT electricity market, that is, cooperative, independent generator, independent power marketer, independent retail electric provider, investor-owned utility, and municipal. The remaining ten seats on the board were filled by

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 1. Organization and Operations (continued)

##### Electric Reliability Council of Texas, Inc. (ERCOT) (continued)

two consumer directors (large commercial and industrial), five independent directors, and three ex officio directors, that is, the Public Counsel as a third consumer director (residential and small consumer), the non-voting Chair of the PUCT, and ERCOT's Chief Executive Officer. The six "market segment directors" and two of the consumer directors (large commercial and industrial) each had an elected alternate (segment alternate) who could attend meetings and vote in the absence of the market segment director.

Beginning with implementation of the Senate Bill 2 amendment on October 12, 2021, the Board of Directors is composed of 11 directors (nine voting and two non-voting). Eight of the voting directors are independent directors. The remaining voting director is the ex-officio Public Counsel Director. The two non-voting directors are also ex officio directors, that is, Chair of the PUCT and ERCOT's Chief Executive Officer (which was previously a voting director position but is now non-voting).

As a result of the February 2021 extreme winter weather event, extraordinary prices in the wholesale electricity market caused some wholesale market participants to default on their payment obligations to ERCOT for power under the ERCOT Nodal Protocols. As a result of these payment defaults, ERCOT was unable to fully settle obligations to certain wholesale market participants who were due payments from ERCOT for the power they produced during the storm. To address these problems, the Texas Legislature during the 87th legislative session enacted two bills that authorized financing mechanisms to provide funds to pay market participants who were previously short-paid and provide liquidity to market participants. One of these bills, House Bill 4492, added subchapters M and N to chapter 39 of PURA and each provided authority for a financing mechanism to address different aspects of the extraordinary costs incurred due to the February 2021 extreme winter weather event, with Subchapter M authorizing up to \$800,000 and Subchapter N authorizing up to \$2,100,000, plus reasonable costs.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 1. Organization and Operations (continued)

##### Electric Reliability Council of Texas, Inc. (ERCOT) (continued)

On October 14, 2021, the PUCT approved ERCOT's application for a Debt Obligation Order (The Order) under PURA §39.603 (Subchapter M) and issued The Order. The Order approves the default balance in an aggregate amount of up to \$800,000; approves the assessment of default charges to all wholesale market participants except those expressly exempted by PURA, in an amount sufficient to ensure the recovery of amounts expected to be necessary to timely provide all payments of debt service and other required amounts and charges in connection with the issuance of debt obligations; authorizes the issuance of Texas Stabilization M bonds in one or more series in an aggregate amount of up to \$800,000 for the payment of the default balance; and approves the financing or securitization of default charges and the creation of default property.

On October 13, 2021, the PUCT approved ERCOT's application for a separate Debt Obligation Order under PURA §39.653 (Subchapter N) and issued the order. The order approves the uplift balance up to \$2,100,000, plus reasonable costs; approves bonds to be issued through a special purpose entity to finance the uplift balance; and approves the securitization of uplift charges and the creation of uplift property. The bonds will not be issued until year 2022.

##### Texas Electric Market Stabilization Funding M LLC (TEMSFM)

TEMSFM is a Delaware limited liability company with ERCOT as its sole member, and a disregarded entity for tax purposes. It was incorporated on October 27, 2021, for the limited purpose of (a) imposing, collecting, and receiving default charges and acquiring default property and related assets to support its obligations under the Texas Stabilization M bonds, (b) issuing Texas Stabilization M bonds in one or more series, and (c) performing other activities relating thereto or otherwise authorized by The Order. On November 12, 2021, TEMSFM issued \$800,000 of Texas Electric Stabilization M Bonds, Series 2021, pursuant to The Order, which were sold to the Texas Treasury Safekeeping Trust Company, which was incorporated by the Texas Comptroller of Public Accounts (see Note 7). ERCOT is the servicer and administrator of the Texas Stabilization M bonds, Series 2021.

# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

### 2. Summary of Significant Accounting Policies

#### Principles of Consolidation

The consolidated financial statements include the accounts of ERCOT and TEMSFM because ERCOT has both control and an economic interest in TEMSFM. All significant intercompany accounts and transactions have been eliminated in consolidation. Unless otherwise noted, these consolidated entities are hereinafter referred to as the Company.

#### Method of Accounting

The accompanying consolidated financial statements have been prepared on an accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

#### Net Assets Without Donor Restrictions

Net assets without donor restrictions are those that are not subject to donor restrictions or stipulations and that may be expendable for any purpose in performing the Company's objectives. Accordingly, net assets of the Company and changes therein are classified and reported as net assets without donor restrictions.

#### Use of Estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities of the consolidated financial statements and reported amounts of revenues, expenses, and capital expenditures during the reporting period. Actual results could differ from those estimates.



## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Cash and Cash Equivalents

Cash and cash equivalents consist of deposits in banks and money market investment accounts with original maturities of 90 days or less. Cash and cash equivalents consist primarily of amounts held by ERCOT on behalf of market participants for congestion management funds and payments of settlement obligations (as described in Note 2 – Market Settlement Liabilities).

##### Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents consist of deposits in banks and money market investment accounts with original maturities of 90 days or less. ERCOT's restricted cash and cash equivalents primarily represent amounts received for security deposits from ERCOT's market participants. TEMSFM's restricted cash consists of security deposits from ERCOT's market participants subject to subchapter M, and partial proceeds from \$800,000 Texas Stabilization M Bonds, Series 2021 issuance that are reserved for retiring or refunding ERCOT existing debt, and debt service.

As of December 31, restricted cash and cash equivalents consist of below:

	2021		
	ERCOT	TEMSFM	Total
Security Deposits	\$ 1,075,543	\$ 6,419	\$ 1,081,962
Reserve for retiring or refunding ERCOT existing debt		50,000	50,000
Reserve for debt service	-	4,000	4,000
Total	\$ 1,075,543	\$ 60,419	\$ 1,135,962

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Restricted Cash and Cash Equivalents (continued)

	2020
	ERCOT
Security Deposits	\$ 658,559

##### Custodial Credit Risk

The Company maintains cash balances at financial institutions, which, at times, may exceed Federal Deposit Insurance Corporation (FDIC) limits and are exposed to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Company's deposits may not be returned. The Company has not experienced, nor does it anticipate, any losses with respect to such cash deposits.

##### Accounts Receivable and Revenue Recognition

Revenue is measured based on a consideration specified in a contract with a customer, and excludes amounts collected on behalf of third parties. The Company recognizes revenue when it satisfies a performance obligation by transferring control over a service to a customer.

##### A. Performance Obligations

*System administration services* - As the independent system operator for the region, ERCOT provides a variety of services to Texas electricity market participants. ERCOT schedules power on an electric grid that connects more than 52,700 miles of transmission lines and 1,030+ generation units, performs financial settlement for the competitive wholesale bulk-power market, and administers retail switching for nearly 8 million premises in competitive choice areas. These services are performed to fulfill ERCOT's

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Accounts Receivable and Revenue Recognition (continued)

primary responsibilities which are maintaining system reliability, facilitating competitive wholesale and retail markets, and ensuring open access to transmission. ERCOT identifies a single performance obligation from these services which are considered a series of distinct services under the revenue standard. Revenue from system administration services, called the system administration fee (SAF) is recognized when services are performed over time. SAF is collected from electric service providers operating within the ERCOT region. This fee is charged pursuant to the ERCOT protocols and as approved by both the ERCOT board of directors and the PUCT. It is based on actual volume consumption. Services are billed each business day and are generally due 2 business days after the invoice date. Amounts not yet billed are accrued and presented as unbilled revenue on the consolidated statements of financial position. The SAF was 55.5 cents per megawatt hour of adjusted metered load in both 2021 and 2020. It is structured to provide funding for ERCOT's core operations and related services.

*Other services* - ERCOT offers or is required to provide its participants other services, including wide-area network usage (WAN) connectivity to ERCOT's grid, weatherization inspection, training for market participants, membership, and other miscellaneous services.

- 1) *WAN* - ERCOT provides, in accordance with its reasonable discretion and control, the design, engineering, procurement, and installation of the equipment and facilities necessary to interconnect market participant's data transfer system to ERCOT's data network and facilities for the sole purpose of transferring data between ERCOT and the market participant. Revenue is recognized when services are provided over time. Market participants are billed monthly based on actual cost incurred that are the responsibility of them, but were incurred by ERCOT. Payment term is net 30 days.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Accounts Receivable and Revenue Recognition (continued)

- 2) *Connectivity to ERCOT's grid* – Entities who propose new or updated generation resources to connect into the ERCOT grid are required to submit Generation Resource Interconnection or Change Request (GINR) to ERCOT. ERCOT coordinates studies on the request with relevant Transmission Service Providers and the entity. Study fees are paid together with the requests and are deferred in the consolidated statements of financial position, and are recognized as revenue when studies are completed.
- 3) *Weatherization Inspection* – Pursuant to Senate Bill 3 (SB3) and PUC Substantive Rule 25.55, Weather Emergency Preparedness, ERCOT is required to perform new weatherization tasks, including conducting inspections of generation resources and transmission facilities. Costs relating to the SB3 weatherization inspections for the 2021-2022 winter weather season are recovered by weatherization inspection fees revenue which is recognized when inspection services are provided.
- 4) *Training for market participants* – ERCOT offers Operator Training and Black Start Training to market participants. Training fees are received during training registration and are recognized as revenue when trainings are completed.
- 5) *Membership* – Applicants pay annual membership dues to apply for ERCOT membership. Membership dues are deferred, and revenue is recognized over the membership period.
- 6) *Other miscellaneous services* – ERCOT provides other miscellaneous services such as studies of operational issues, development of certain revisions to market rules and associated changes to IT systems. Revenue related to these services is recognized as the services are performed over time.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Accounts Receivable and Revenue Recognition (continued)

7) *Default charges fees* – As described in Note 1 Organization and Operations, TEMSFM is established to finance the default balance under The Order through Texas Market Stabilization M bonds, Series 2021. TEMSFM has the rights to impose, collect, and receive default charges along with the other rights arising under The Order. As the issuer of Texas Market Stabilization M bonds, Series 2021, TEMSFM has the performance obligations to maintain and service the bonds. Ongoing expenses associated with the performance obligations are recovered through default charges fees revenue. Wholesale market participants, except those expressly exempted by PURA, are billed and payments are collected monthly on a pro rata basis in amounts sufficient to ensure the recovery of default charges receivable and ongoing expenses. Revenue is recognized over time when related services are provided, and related expenses are incurred.

*Reliability organization pass-through* – The North American Electric Reliability Corporation (NERC) invoices ERCOT for reliability functions performed by NERC and its delegated Texas Reliability Entity, Inc. In turn, ERCOT collects payment from market participants for this Electric Reliability Organization (ERO) billing. The ERO billing is based on actual NERC funding, and ERCOT collects this payment and remits it to NERC on a quarterly basis. ERO billing amount was \$19,541 and \$19,400 in 2021 and 2020, respectively. No revenue is recognized as there is no consideration to earn during this ERO billing pass-through.

Electric Reliability Council of Texas, Inc.

Notes to Consolidated Financial Statements (continued)  
(Dollars in Thousands)

As of and for the Years Ended  
December 31, 2021 and 2020

2. Summary of Significant Accounting Policies (continued)

Accounts Receivable and Revenue Recognition (continued)

B. Disaggregation of Revenue

The following table illustrates the disaggregation disclosure by service types and timing of revenue recognition.

<u>Service Types</u>	<u>Services</u> <u>transferred</u> <u>over time</u>	<u>Services</u> <u>transferred</u> <u>at a point in time</u>	<u>2021 Total</u>
System administration	\$ 218,339	\$ -	\$ 218,339
Default Charges fees	3,273	-	3,273
WAN	4,667	-	4,667
Connectivity to ERCOT's grid	-	3,246	3,246
Weatherization inspection	-	2,668	2,668
Training for market participants	-	286	286
Membership	297	-	297
Other miscellaneous services	119	-	119
Total	<u>\$ 226,695</u>	<u>\$ 6,200</u>	<u>\$ 232,895</u>



# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

As of and for the Years Ended  
December 31, 2021 and 2020

### 2. Summary of Significant Accounting Policies (continued)

#### Accounts Receivable and Revenue Recognition (continued)

<u>Service Types</u>	<u>Services transferred over time</u>	<u>Services transferred at a point in time</u>	<u>2020 Total</u>
System administration	\$ 212,185	\$ -	\$ 212,185
WAN	3,624	-	3,624
Connectivity to ERCOT's grid	-	2,770	2,770
Training for market participants	-	113	113
Membership	283	-	283
Other miscellaneous services	76	-	76
Total	<u>\$ 216,168</u>	<u>\$ 2,883</u>	<u>\$ 219,051</u>

### C. Contract Balances

The following table provides information about receivables, contracts assets, and contract liabilities from contracts with customers at December 31.

	<u>2021</u>	<u>2020</u>
Receivables-current	\$ 18,252	\$ 3,164
Receivables-non-current	\$ 784,181	\$ -
Contract assets	\$ 9,132	\$ 2,607
Contract liabilities	<u>\$ 1,072</u>	<u>\$ 960</u>

Balances of accounts receivable at December 31, 2021 and 2020 on the consolidated statements of financial position also include \$7 and \$78 interest receivable, respectively and, \$715 and \$1,781 pass-through receivable, respectively, in addition to receivables-current from contracts with customers.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Accounts Receivable and Revenue Recognition (continued)

Receivables-non-current are comprised solely of default charges receivable, non-current, and are represented that way on the consolidated statements of financial position. Contract assets relate to the Company's rights to consideration for services provided but not billed at the reporting date for system administration and Texas Market Stabilization M Bonds, Series 2021 interest expenses. The contract assets are transferred to the receivables when invoices are billed. Contract liabilities relate to advance consideration received from customers for connectivity to ERCOT's grid and membership. Revenues are recognized when performance obligations are satisfied.

##### D. Significant Judgements

The Company recognizes revenues from system administration, default charges fees, WAN, membership, and other miscellaneous services over time, as the Company determines that customers simultaneously receive and consume the benefits provided by the Company's performances. Revenue from system administration is recognized over time using output method which is based on actual load volume consumption. Revenues from default charges fees, WAN, and other miscellaneous services are recognized over time using cost based input method, which is based on actual incurred costs of the services provided by the Company. Revenue from membership is recognized over time on a straight-line basis, as the Company determines that customers benefit from membership services throughout the year, and the best measure of progress toward complete satisfaction of the performance obligation over time is a time-based straight-line measure.

The Company recognizes revenues from connectivity to ERCOT's grid studies, weatherization inspection, and training from market participants at a point of time. The Company determines that customers receive the benefits from the services when the Company's performance obligations are satisfied, which are when the connectivity to ERCOT's grid study is completed, weatherization inspection is completed, and training to market participants is provided.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Accounts Receivable and Revenue Recognition (continued)

The Company has no significant continuing obligation and collection is reasonably assured. The Company does not maintain an allowance for doubtful accounts as it does not believe it has a material risk of loss associated with lack of collection.

##### Investments

Investments consist of US Treasury bonds and bills, and are recorded at fair value in the consolidated statements of financial position. Net investment return is reported in the statements of activities and net assets, and consists of interest and unrealized capital gains and losses, less external investment expenses.

Investments are made by investment advisors whose performance is monitored by ERCOT's Investment Officers. Although the fair values of investments are subject to fluctuation on a year-to-year basis, we believe that the investment policies and guidelines are prudent for the long-term welfare of ERCOT.

Investments were sold in year 2021. There was no investment as of December 31, 2021.

##### Prepaid Expenses and Other Current Assets

Prepaid expenses consist of amounts paid in advance for items that had not yet occurred as of the end of fiscal year. Prepaid expenses are amortized in the periods when items occur. Other current assets primarily include the non-vested portion of former employees' 401K accounts. The balances at December 31 are as following:

	2021	2020
Prepaid expenses	\$ 25,045	\$ 26,591
Other current assets	337	197
Total prepaid expenses and other current assets	<u>\$ 25,382</u>	<u>\$ 26,788</u>

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Property and Equipment

Property and equipment consist primarily of computer equipment, software, and buildings for operations, and finance lease right-of-use assets, and are recorded at cost. Depreciation is computed on the straight-line method over the estimated life of the asset. The cost of betterments to, or replacement of, property and equipment is capitalized. When assets are retired or otherwise disposed of, the cost and related depreciation are removed from the accounts and any resulting gain or loss is reflected in non-operating income (expense) in the consolidated statements of activities and net assets for the period. ERCOT recognized a gain of \$1 and \$0 in 2021 and 2020, respectively, related to property and equipment. Repairs and maintenance costs are expensed when incurred.

ERCOT's depreciable lives (in years) for property and equipment are as follows:

<u>Asset Category</u>	<u>Depreciable Life</u>
Computer hardware	3
Software	5
Vehicles	5
Furniture and equipment	7
Mechanical building components	10
Buildings and improvements	Up to 30
Finance lease right-of-use assets	30
Leasehold improvements	Lesser of useful life or respective lease term

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Systems Under Development

ERCOT continues to develop the information systems and grid operating systems that are being used in its operations. Direct costs and related indirect and interest costs incurred to develop or obtain these systems during the application development stage are capitalized. Such costs are expensed when incurred during the preliminary project stage. Internal costs and contract expenditures not related directly to the development of systems, and related testing activities, are expensed as incurred. Costs from completed projects are transferred to property and equipment when the systems are placed in service.

##### Impairment

The Company evaluates long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If impairment exists, it is measured as the difference between the net book value of the asset and its estimated fair value. Impairment is computed by comparing the expected future cash flows, undiscounted and before interest, to the carrying value of the asset.

There is no impairment loss in 2021 and 2020, respectively.

##### Interest Capitalization

Interest is capitalized in connection with the construction of major software systems, buildings, and improvements. The capitalized interest is recorded as part of the asset to which it relates and is amortized or depreciated over the asset's estimated useful life. During 2021 and 2020, capitalized interest costs were \$766 and \$503, respectively.

# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

### 2. Summary of Significant Accounting Policies (continued)

#### Market Settlement Liabilities

Market settlement liabilities primarily represent two types of funds held on behalf of the ERCOT market: congestion management funds and payments of settlement obligations. Market participant settlement obligations amounts are collected and redistributed by ERCOT in the normal course of managing the settlement of ERCOT's markets. Such settlement obligations are generally held before distribution to the market in accordance with timetables set forth in ERCOT's Protocols.

ERCOT manages a congestion revenue rights (CRR) program that includes monthly auctions and auctions for longer than one month. ERCOT collects and holds the proceeds from the auctions until the proceeds are distributed according to provisions of the ERCOT Protocols. ERCOT's Financial Corporate Standard, adopted by the Board of Directors, includes a provision that a certain portion of the funds held as a result of CRR auctions may be used to fund ERCOT working capital and capital expenditure needs within certain guidelines.

ERCOT acts as the central counter-party for transactions in the ERCOT wholesale market between buyers and sellers, and ERCOT must maintain revenue neutrality in serving this market function. Because ERCOT acts only as the clearinghouse through which funds are exchanged between buyers and sellers in the ERCOT wholesale market, when an ERCOT market participant with a payment obligation "short pays" an invoice, the result is that ERCOT market participants that are due payments from those "short paid" invoices cannot be paid in full. ERCOT is a non-recourse entity for settlement of market participant "short payments" – meaning ERCOT does not take on the financial obligation. Per ERCOT Protocol Section 9.19.1(1), the "Default Uplift Invoice" process must be used by ERCOT to collect outstanding "short pay amounts for all Settlement Invoices in a month," in order to fully pay the ERCOT market participants that are due payments but have been "short paid." By Protocol, ERCOT's fees are paid from market receipts as a first priority before any market obligations are paid, and ERCOT bears no liability from market participant "short payments."



## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Market Settlement Liabilities (continued)

As a result of the February 2021 extreme winter weather event, extraordinary prices in the wholesale electricity market caused some wholesale market participants to default on their payment obligations to ERCOT for power under the ERCOT Nodal Protocols. As a result of these payment defaults, ERCOT was unable to fully pay certain wholesale market participants who were due payments from ERCOT for the power they produced during the storm. Under the order of the PUCT, ERCOT utilized approximately \$800,000 from the CRR auction funds to cover part of the “short payment” invoices that were due to ERCOT market participants on February 26, 2021, to address the liquidity problems in the wholesale market. Part of the CRR auction funds used for short payments were paid back to ERCOT from the market participants. A small portion of the “short payment” amount was collected directly from the owing ERCOT market participants through payment plans. In November 2021, TEMSFM issued \$800,000 Texas Market Stabilization M Bonds, Series 2021 to finance upfront costs of bonds issuance, a portion of the unpaid defaulted amounts, and replenish a portion of the CRR auction funds used for short payment. As stated above, ERCOT does not take on the financial obligation of wholesale market participant transactions, and as such, bears no liability for short payments.

Market settlement liabilities consist of the following at December 31:

	2021	2020
Short-term CRR auction funds	\$ 756,009	\$ 640,338
Settlement obligations	105,836	49,045
Use of CRR for market short payments	(274,961)	-
Total current market settlement liabilities	586,884	689,383
Long-term CRR auction funds	488,594	377,047
Total market settlement liabilities	<u>\$1,075,478</u>	<u>\$1,066,430</u>

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Security Deposits and Reserves

Market participants not meeting certain creditworthiness standards referenced in ERCOT Protocols must maintain a means of security with the Company in order to mitigate market credit risk. Market participants have discretion in the means of security, such as corporate guaranties, letters of credit, surety bonds, or cash security deposits provided the market participants remain in compliance with ERCOT Protocols. The Company is required to remit interest earned on security deposits to market participants.

In addition, a portion of the proceeds from \$800,000 Texas Stabilization M Bonds, Series 2021 issuance are reserved for retiring or refunding ERCOT existing debt, and debt service.

Cash security deposits and debt reserves are classified as restricted cash and cash equivalents on the consolidated statements of financial position. See Note 2 Restricted Cash and Cash Equivalent. The balance of cash security deposits and reserves is \$1,135,962 and \$658,559 at December 31, 2021 and 2020, respectively.

##### Income Taxes

ERCOT is exempt from federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(4), and TEMSFM is classified as a disregarded entity for tax purposes. ERCOT is also exempt from state income taxes. Accordingly, no provision for income taxes or uncertain tax positions has been reflected in the consolidated financial statements.

##### Debt Issuance Costs

The Company capitalizes issuance costs related to debt. The amounts are presented as a direct deduction from the debt liability, and amortized over the life of the debt.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Adoption of Accounting Standards Update (ASU)

The Financial Accounting Standards Board (FASB) issued ASU No. 2018-15 “Intangibles - Goodwill and Other - Internal-Use Software”, with an effective date January 1, 2021. The update aligns the requirement for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. Capitalized implementation costs shall be amortized over the term of the associated hosting arrangement, on a straight-line basis unless another systematic and rational basis is more representative of the pattern in which the entity expects to benefit from access to the hosted software. ERCOT adopted the amendments on January 1, 2021. The amendments are applied prospectively to all implementation costs incurred after January 1, 2021.

In February 2016, the FASB issued ASU No. 2016-02 “Leases (Topic 842)”. The guidance requires lessees to recognize assets and liabilities for most leases in their balance sheet. ERCOT adopted the amendments for its fiscal year beginning January 1, 2020, and used the optional transition method for all existing leases. The optional transition method enabled the adoption of the new standard as of the beginning of the period of adoption and did not require restatement of prior period financial information. As a result, prior period financial information was not recast and continues to be reported under the accounting guidance effective during those periods. At adoption, ERCOT elected the following practical expedients: (1) the “package of practical expedients”, pursuant to which ERCOT did not need to reassess prior conclusions regarding lease identification, lease classification and initial direct costs and (2) the creation of an accounting policy for short-term leases resulting in lease payments being recorded as an expense on a straight-line basis over the lease term. See Note 10 Leases.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 2. Summary of Significant Accounting Policies (continued)

##### Accounting for the Effects of Regulation

The Company is subject to the provisions of the FASB in accounting for the effects of rate regulation. These provisions require regulated entities, in appropriate circumstances, to establish regulatory assets and/or liabilities, and thereby defer the statements of activities and net assets impact of certain revenues and charges because it is probable they will be recovered or repaid in future periods. The Company does not have any regulatory assets or liabilities as of December 31, 2021 and 2020.

##### 3. Reclassification of Prior Year Presentation

Certain prior year amounts have been reclassified for consistency with the current year presentation. These reclassifications had no effect on the reported results of operations. Adjustments have been made to the consolidated statements of financial position for the year ended December 31, 2020, to reclassify deferred ERO revenue from deferred revenue to accrued liabilities.

##### 4. Liquidity and Availability

Financial assets available for general expenditures, that is, without donor or other restrictions limiting their use, within one year of the consolidated statements of financial position date, comprise the following:

	2021	2020
Cash and cash equivalents	\$ 1,099,267	\$ 996,337
Accounts receivable	18,975	5,023
Unbilled revenue	9,132	2,607
Short-term investments	-	102,965
Total	<u>\$ 1,127,374</u>	<u>\$1,106,932</u>

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 4. Liquidity and Availability (continued)

As part of the Company's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, ERCOT invests cash in excess of daily requirements in short-term investments and money market funds. To help manage unanticipated liquidity needs, ERCOT has committed a line of credit in the amount of \$100,000 (see Note 7), which it could draw upon.

#### 5. Fair Value Measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are based on inputs of observable and unobservable market data that a market participant would use in pricing the asset or liability. The use of observable inputs is maximized where available and the use of unobservable inputs is minimized for fair value measurement. In a three-tier fair value hierarchy, which prioritizes inputs to valuation techniques used for fair value measurement, the following levels were established for each input:

- Level 1 valuations use quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date. An active market is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 valuations use inputs, other than those included in Level 1, that are observable for the asset or liability, either directly or indirectly.
- Level 3 valuations use unobservable inputs for the asset or liability. Unobservable inputs are used to the extent observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. The input may reflect the assumptions of the reporting entity of what a market participant would use in pricing an asset or liability.

# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

As of and for the Years Ended  
December 31, 2021 and 2020

### 5. Fair Value Measurement (continued)

In the case of multiple inputs being used in a fair value measurement, the lowest level input that is significant to the fair value measurement represents the level in the fair value hierarchy in which the fair value measurement is reported.

The following tables set forth by level within the fair value hierarchy the Company's financial assets. The fair value on a recurring basis as of December 31 is as follows:

	2021			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Cash equivalents	\$ 1,062,611	\$ 1,062,611	\$ -	\$ -
Restricted cash equivalents	1,075,454	1,075,454	-	-
Total assets at fair value	<u>\$2,138,065</u>	<u>\$2,138,065</u>	<u>\$ -</u>	<u>\$ -</u>

	2020			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Cash equivalents	\$ 990,811	\$ 990,811	\$ -	\$ -
Restricted cash equivalents	658,406	658,406	-	-
Investment				
US Treasury bonds	102,965	102,965		
Total assets at fair value	<u>\$1,752,182</u>	<u>\$1,752,182</u>	<u>\$ -</u>	<u>\$ -</u>

# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

### 6. Property and Equipment

Property and equipment consist of the following at December 31:

	2021	2020
<b>Depreciable:</b>		
Software	\$ 732,450	\$ 718,900
Building and leasehold improvements	102,201	101,573
Computer hardware and equipment	84,628	83,937
Furniture and fixtures	37,985	37,986
Finance lease right-of-use assets	12,637	-
Vehicles	286	283
<b>Non-depreciable:</b>		
Land	947	947
Construction in progress	6,299	294
	<u>977,433</u>	<u>943,920</u>
Accumulated depreciation	(861,801)	(834,564)
Total property and equipment, net	<u>115,632</u>	<u>109,356</u>
Systems under development	40,209	27,522
Total	<u>\$ 155,841</u>	<u>\$ 136,878</u>

### 7. Debt Payable

The Company's consolidated debt payable consists of the following:

	2021	2020
3.00% Senior Notes	\$ 43,000	\$ 47,000
Texas Market Stabilization M Bonds, Series 2021	800,000	-
Total	<u>\$ 843,000</u>	<u>\$ 47,000</u>

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 7. Debt Payable (continued)

##### Revolving Line of Credit

ERCOT has one revolving line of credit with JPMorgan Chase Bank that was entered into in June 2012, and amended in subsequent years when it expired. This facility is primarily used for short-term working capital needs, has a maximum amount of available credit of \$100,000 and expires on December 31, 2024. As of December 31, 2021 and 2020, there was no debt outstanding under this line of credit.

The interest rate on this facility is based on the prime rate, a Eurodollar based rate, or other rate as described in the debt agreements. The contractual rate of interest on the revolving line of credit's outstanding balance was 0.86% and 0.79% at December 31, 2021 and 2020, respectively. Additionally, at December 31, 2021, ERCOT pays a commitment fee of 0.15% on the unused portion of the \$100,000 revolving credit facility. ERCOT incurred commitment fees totaling \$152 and \$153 in 2021 and 2020, respectively, in connection with its debt facilities. The revolving line of credit has several debt covenants, the most restrictive of which limits ERCOT's indebtedness. At December 31, 2021 and 2020, the revolving line of credit had unamortized debt issuance costs of \$12 and \$16, respectively. ERCOT was in compliance with its debt covenants for this facility.

##### 3.00% Senior Notes

On October 31, 2012, ERCOT issued \$80,000 in senior notes through a private placement. These notes bear interest at 3.00% and are due in equal quarterly principal payments beginning in December 2012 through September 2032. The private placement has several covenants, the most restrictive of which limits ERCOT's indebtedness. At December 31, 2021 and 2020, there were \$43,000 and \$47,000 outstanding senior notes, respectively and, \$144 and \$157 of unamortized debt issuance costs, respectively. ERCOT was in compliance with its covenants for these notes.



## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 7. Debt Payable (continued)

##### Texas Market Stabilization M Bonds, Series 2021

On November 12, 2021, TEMSFM issued \$800,000 of Texas Market Stabilization M Bonds, Series 2021, as a result of securitization of default charges, pursuant to The Order (see Note 1 Organization and Operations). The bonds were sold to the Texas Treasury Safekeeping Trust Company, which was incorporated by the Texas Comptroller of Public Accounts. The bonds proceeds were allocated to first pay upfront costs, then to pay amounts owed to ERCOT by competitive wholesale market participants, and finally to use the rest to replenish CRR auction funds temporarily used by ERCOT to reduce the short payments to wholesale market participants due to Winter Storm Uri. The bonds are payable out of default charges to all wholesale market participants except those expressly exempted by PURA. The bonds have target scheduled final maturities of approximately 28 years and legal final maturities not exceeding 30 years from the date of issuance. The interest rate is calculated by using the rate determined by the Municipal Market Data Municipal Electric Index, as published by Refinitiv TM3, based on the credit rating of ERCOT, plus 2.5%. The interest rate is fixed at 2.97% for the first 3 years, after 01/31/2025 the interest rate will be reset based on the aforementioned calculation. The following future maturities table was based on an assumed rate of 4.12%. Payments of the bonds are semi-annual, beginning August 1, 2022. At December 31, 2021, the unamortized debt issuance costs were \$1,899.

Under PURA § 39.603(i), the Texas Stabilization M Bonds, Series 2021 authorized to be issued under The Order are a nonrecourse debt secured solely by the default charges created by The Order and explicitly assessed to repay the Texas Stabilization M Bonds, Series 2021 (including the default property as well as earnings from the investment and reinvestment of default charges). The Texas Stabilization M Bonds, Series 2021 authorized to be issued under The Order and PURA § 39.603 do not create a personal liability for ERCOT.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 7. Debt Payable (continued)

##### Future Maturities

Future maturities of the debt payable are as follows:

	3.00% Senior Notes	Texas Market Stabilization M Bonds, Series 2021	Total
Year Ending December 31:			
2022	\$ 4,000	\$ 4,244	\$ 8,244
2023	4,000	19,479	23,479
2024	4,000	20,062	24,062
2025	4,000	19,166	23,166
2026	4,000	18,375	22,375
Thereafter through 2049	23,000	718,674	741,674
	<u>\$ 43,000</u>	<u>\$ 800,000</u>	<u>\$ 843,000</u>

#### 8. Expenses by Nature and Function

The consolidated financial statements report certain categories of expenses that are attributed to both program and supporting functions. Therefore, expenses require allocation on a reasonable basis that is consistently applied. Depreciation is allocated based on ratio of each function's operating expenses to the total operating expenses. Interest expense is allocated based on project efforts. Other expenses are allocated based on the functions.

The tables below present expenses by both their nature and function for years ended December 31, 2021 and 2020, respectively.

Electric Reliability Council of Texas, Inc.

Notes to Consolidated Financial Statements (continued)  
(Dollars in Thousands)

As of and for the Years Ended  
December 31, 2021 and 2020

8. Expenses by Nature and Function (continued)

	2021		
	Program Services	Management and General	Total
Salaries and related benefits	\$ 110,953	\$ 22,100	\$ 133,053
Hardware and software maintenance and licensing	32,381	427	32,808
Outside services	15,196	11,864	27,060
Facility and equipment costs	6,245	4,615	10,860
Depreciation	21,569	6,333	27,902
Other	3,144	7,876	11,020
Subtotal expenses by function	189,488	53,215	242,703
Less capitalized labor expense included on the consolidated statement of financial position	(9,161)	(257)	(9,418)
Total operating expenses included on the consolidated statement of activities	\$ 180,327	\$ 52,958	\$ 233,285
Interest expense	\$ 3,956	\$ 1,271	\$ 5,227
Less capitalized interest expense included on the consolidated statement of financial position	(766)	-	(766)
Total interest expense included on the consolidated statement of activities	\$ 3,190	\$ 1,271	\$ 4,461
Total operating and interest expenses included on the consolidated statement of activities	\$ 183,517	\$ 54,229	\$ 237,746

Electric Reliability Council of Texas, Inc.

Notes to Consolidated Financial Statements (continued)  
(Dollars in Thousands)

As of and for the Years Ended  
December 31, 2021 and 2020

8. Expenses by Nature and Function (continued)

	2020		
	Program Services	Management and General	Total
Salaries and related benefits	\$ 107,843	\$ 21,842	\$129,685
Hardware and software maintenance and licensing	28,807	905	29,712
Outside services	14,012	2,574	16,586
Facility and equipment costs	4,793	4,679	9,472
Depreciation	24,569	5,573	30,142
Other	3,019	3,682	6,701
Subtotal expenses by function	183,043	39,255	222,298
Less capitalized labor expense included on the consolidated statement of financial position	(10,495)	(91)	(10,586)
Total operating expenses included on the consolidated statement of activities	\$ 172,548	\$ 39,164	\$ 211,712
Interest expense	\$ 503	\$ 1,576	\$ 2,079
Less capitalized interest expense included on the consolidated statement of financial position	(503)	-	(503)
Total interest expense included on the consolidated statement of activities	\$ -	\$ 1,576	\$ 1,576
Total operating and interest expenses included on the consolidated statement of activities	\$ 172,548	\$ 40,740	\$ 213,288

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 9. Employee Benefit Plans

##### Defined Contribution Plan

ERCOT sponsors the ERCOT Defined Contribution 401(k) Savings Plan (the 401(k) Plan), which is subject to the provisions of the Employee Retirement Income Security Act of 1974. The 401(k) Plan utilizes a third-party administrator. Employees must be 21 years of age to be eligible to participate.

ERCOT matches 75% of the employee's contribution up to 6% of eligible compensation as defined in the 401(k) Plan document. Employees are fully vested for the ERCOT match of 75% after five years. In addition, ERCOT contributes 10% of a participant's eligible compensation as defined in the 401(k) Plan document. Employees are fully vested for the ERCOT contributions of 10% after three years. Employer contributions to the 401(k) Plan are summarized in the table below:

	2021	2020
75% of the employee's contribution up to 6%	\$ 4,150	\$ 3,960
10% of the employee's compensation	9,962	9,544
Total employer contributions	<u>\$ 14,112</u>	<u>\$ 13,504</u>

##### Health Insurance Reserve

ERCOT provides a self-insured group health plan to its employees and pays for all health claims. Incurred-but-not-reported claims liability is accrued. At December 31, 2021 and 2020, the liability is \$1,016 and \$701, respectively.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 10. Leases

ERCOT has non-cancelable operating leases for office facilities and office and telecommunication equipment. The terms of ERCOT's leases require monthly payments and expire in varying dates ranging from 2022 through 2035. All of the operating leases are fixed lease payments. ERCOT elected the practical expedient not to separate lease and non-lease components for the office facilities and office equipment leases. Most leases include options to renew, with renewal terms that can extend the lease term from 3 to 5 years. The exercise of lease renewal options is at ERCOT's sole discretion. The amounts of the right-of-use assets and lease liabilities are measured based on current expectations of not exercising the available renewal options. The existing leases are not subject to any restrictions or covenants which preclude ERCOT's ability to obtain financing or enter into additional leases.

As of December 31, 2021, ERCOT has a finance lease for a new Austin office facility. This lease commenced in year 2021 with a lease term of 123 months and two 5 year renewal options. The rent payment will start in March 2022. There was no cash paid for amounts in the measurement of finance lease liabilities in the consolidated statements of cash flows as of December 31, 2021. The lease has a purchase option that ERCOT intends to exercise in year 2022.

Because the rate implicit in the leases was not readily determinable, ERCOT used a risk-free discount rate for all operating and finance leases.

Electric Reliability Council of Texas, Inc.

Notes to Consolidated Financial Statements (continued)  
(Dollars in Thousands)

As of and for the Years Ended  
December 31, 2021 and 2020

10. Leases (continued)

Lease costs and related information as December 31 are as follows:

	2021	2020
Lease cost		
Operating lease cost	\$ 990	\$ 927
Finance lease cost	285	-
Amortization of right-of-use assets	281	-
Interest on lease liabilities	4	-
Total lease cost	\$ 1,275	\$ 927
Other information		
Cash paid for amounts included in the measurement of lease liabilities	\$ 581	\$ 540
Operating cash flows from operating leases	581	540
Right-of-use assets obtained in exchange for new operating lease liabilities	354	1,241
Right-of-use assets obtained in exchange for new finance lease liabilities	12,637	-
Weighted-average remaining lease term-operating leases	5.3 years	3.9 years
Weighted-average remaining lease term-finance leases	0.58 years	-
Weighted-average discount rate-operating leases	1.24%	1.68%
Weighted-average discount rate-finance leases	0.05%	-

# Electric Reliability Council of Texas, Inc.

## Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

### 10. Leases (continued)

Amounts recognized as right-of-use assets related to operating leases are included in other long-term assets; while related lease liabilities are included in accrued liabilities and other long-term liabilities. Amounts recognized as right-of-use assets related to finance leases are included in property and equipment, net, and related lease liabilities are recorded in finance lease liabilities current.

As of December 31, right-of-use assets and lease liabilities related to operating leases and finance leases were as follows:

	2021	2020
<b>Operating leases:</b>		
Other long-term assets	\$ 867	\$ 1,042
Total operating lease right-of-use assets	<u>\$ 867</u>	<u>\$ 1,042</u>
Accrued liabilities	\$ 213	\$ 471
Other long-term liabilities	334	246
Total operating lease liabilities	<u>\$ 547</u>	<u>\$ 717</u>
<b>Finance leases:</b>		
Property and equipment, net	\$ 12,637	-
Total finance lease right-of-use assets	<u>\$ 12,637</u>	<u>-</u>
Finance lease liabilities current	\$ 12,642	-
Total finance lease liabilities	<u>\$ 12,642</u>	<u>-</u>



## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 10. Leases (continued)

The following table presents the future undiscounted maturities of operating leases at December 31, 2021 and for each of the next five years and thereafter:

2022	\$	218
2023		101
2024		76
2025		58
2026		24
Thereafter		98
Total lease payments		575
Less imputed interest		(28)
Lease liabilities recognized	\$	<u>547</u>

The following table presents the future undiscounted maturities of finance leases at December 31, 2021:

2022	\$	12,646
Less imputed interest		(4)
Lease liabilities recognized	\$	<u>12,642</u>

#### 11. Concentrations

ERCOT provides reliability and market services to market participants. ERCOT settles the costs of these services by passing through the costs of such services from the providers to the users of such services. In the event that a market participant is unable to make payment on its market obligations, ERCOT's Protocols stipulate that the amount of the default is to be allocated to other market participants based on their market activity and define the allocation mechanism. In order to limit the risks associated with such occurrences, ERCOT requires a cash security deposit, letter of credit, corporate guaranty, or surety bond from market participants that do not meet certain credit standards. Credit

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 11. Concentrations (continued)

risk related to trade receivables associated with ERCOT's fees is substantially mitigated by the fact that, by Protocol, ERCOT's fees are paid from market receipts as a first priority before any market obligations are paid.

ERCOT's fee revenue is driven by the demand for electricity rather than the number of market participants. In the event that any market participant representing load ceased to operate, another market participant representing load would assume the role in response to the demand for electricity. As such, ERCOT believes its exposure to a material reduction in revenues associated with the loss of any market participant is limited.

TEMSFM default charges receivable and default charge fees revenue are decided by the amounts needed to cover the \$800,000 of Texas Market Stabilization M Bonds, Series 2021 principal, interest, and other debt related expenses, rather than the number of market participants that are subject to subchapter M. Wholesale market participants, except those expressly exempted by PURA, are billed and payments are collected monthly on a pro rata basis in amounts sufficient to ensure the recovery of default charges receivable and ongoing expenses. Cash security deposit or letter of credit from market participants that do not meet certain credit standards is required to mitigate the risk that a market participant is not able to make payment. TEMSFM believes that it does not have a material concentration risk.

#### 12. Contingencies

The Company is party to regulatory and legal proceedings that management considers to be normal actions to which an enterprise of its size and nature might be subject. Such proceedings are not anticipated to have a material impact on ERCOT's financial condition, results of operations, or cash flows.

## Electric Reliability Council of Texas, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

*As of and for the Years Ended  
December 31, 2021 and 2020*

#### 12. Contingencies (continued)

As a result of the February 2021 extreme winter weather event, ERCOT is also party to numerous additional legal and regulatory proceedings. Specifically, ERCOT is a defendant in more than 100 personal injury and property damage lawsuits, which have been consolidated for adjudication in a multi-district litigation pre-trial court. ERCOT is also currently party to other lawsuits and administrative proceedings at the PUCT challenging energy pricing during the February 2021 extreme winter weather event. Two of the matters to which ERCOT is currently a party are appellate matters that seek review of intermediate appellate decisions regarding the issues of whether ERCOT is entitled to sovereign immunity and whether the PUCT has exclusive jurisdiction over claims asserted against ERCOT. Although ERCOT believes that the facts support ERCOT's claims to sovereign immunity and that the PUCT has exclusive jurisdiction over claims asserted against ERCOT, these matters are now before the Texas Supreme Court and a decision is not expected until 2023. ERCOT does not anticipate that the proceedings to which it is a party will have a material impact on ERCOT's financial condition, results of operations, or cash flows.

#### 13. Subsequent Events

The Company has evaluated material subsequent events through April 29, 2022, the date the Company's consolidated financial statements were available to be issued.

Electric Reliability Council of Texas, Inc.

Supplementary Information

December 31, 2021

Electric Reliability Council of Texas, Inc.

Consolidating Statements of Financial Position Information

	December 31, 2021			
	ERCOT	TEMSFM	Eliminations	Consolidated
	(In Thousands)			
<b>Assets</b>				
Current assets:				
Cash and cash equivalents	\$ 1,095,267	\$ 4,000	\$ -	\$ 1,099,267
Accounts receivable	5,063	13,912	-	18,975
Unbilled revenue	5,951	3,264	(83)	9,132
Restricted cash and cash equivalents	1,075,543	60,419	-	1,135,962
Prepaid expenses and other current assets	25,374	8	-	25,382
Total current assets	2,207,198	81,603	(83)	2,288,718
Long-term investments	4,000	-	(4,000)	-
Property and equipment, net	115,632	-	-	115,632
Systems under development	40,209	-	-	40,209
Default charges receivable, non-current	-	784,181	-	784,181
Other long-term assets	867	-	-	867
Total assets	\$2,367,906	\$ 865,784	\$ (4,083)	\$ 3,229,607

Electric Reliability Council of Texas, Inc.

Consolidating Statements of Financial Position Information (continued)

	December 31, 2021			
	ERCOT	TEMSFM	Eliminations	Consolidated
	(In Thousands)			
<b>Liabilities and Net Assets</b>				
Current liabilities:				
Accounts payable	\$ 3,108	\$ -	\$ -	\$ 3,108
Accrued liabilities	26,085	3,264	(83)	29,266
Finance lease liabilities current	12,642	-	-	12,642
Deferred revenue	1,072	-	-	1,072
Market settlement liabilities	586,884	-	-	586,884
Security deposits and reserves	1,075,543	60,419	-	1,135,962
Debt payable, current portion	4,000	4,244	-	8,244
Total current liabilities	1,709,334	67,927	(83)	1,777,178
Debt payable, less current portion:				
Principal	39,000	795,756	-	834,756
Less unamortized debt issuance costs	156	1,899	-	2,055
Debt payable, less current portion and unamortized debt issuance costs	38,844	793,857	-	832,701
Long-term CRR liabilities	488,594	-	-	488,594
Other long-term liabilities	659	-	-	659
Total liabilities	2,237,431	861,784	(83)	3,099,132
Net assets without donor restrictions	130,475	4,000	(4,000)	130,475
Total liabilities and net assets	\$2,367,906	\$ 865,784	\$ (4,083)	\$3,229,607

Electric Reliability Council of Texas, Inc.

Consolidating Statements of Activities and Net Assets Information

	December 31, 2021			
	ERCOT	TEMSFM	Eliminations	Consolidated
	<i>(In Thousands)</i>			
<b>Operating revenues:</b>				
System administration fees	\$ 218,339	\$ -	\$ -	\$ 218,339
Default charges fees	-	3,273	-	3,273
Other services revenue	11,366	-	(83)	11,283
Total operating revenues	229,705	3,273	(83)	232,895
<b>Operating expenses:</b>				
Salaries and related benefits	123,635	-	-	123,635
Hardware and software maintenance and licensing	32,808	-	-	32,808
Outside services	27,060	83	(83)	27,060
Facility and equipment costs	10,860	-	-	10,860
Depreciation	27,902	-	-	27,902
Other	11,020	-	-	11,020
Total operating expenses	233,285	83	(83)	233,285
(Loss) income from operations	(3,580)	3,190	-	(390)
<b>Other income (expense):</b>				
Investment return, net	200	-	-	200
Interest expense	(1,271)	(3,190)	-	(4,461)
Non-operating income	2	-	-	2
Change in net assets without donor restrictions	(4,649)	-	-	(4,649)
Net assets without donor restrictions, beginning of year	135,124	-	-	135,124
Equity contribution from parent company	-	4,000	(4,000)	-
Net assets without donor restrictions, end of year	\$ 130,475	\$ 4,000	\$ (4,000)	\$ 130,475

Electric Reliability Council of Texas, Inc.

Consolidating Statements of Cash Flow Information

	December 31, 2021			
	ERCOT	TEMSFM	Eliminations	Consolidated
	(In Thousands)			
<b>Operating activities</b>				
Change in net assets without donor restrictions	\$ (4,649)	\$ -	\$ -	\$ (4,649)
Adjustments to reconcile change in net assets without donor restrictions to net cash provided by operating activities:				
Depreciation/amortization of assets	27,902	-	-	27,902
Amortization of debt issuance costs	17	9	-	26
Interest expense accrual on finance lease liabilities	5	-	-	5
Amortization of bond premium	290	-	-	290
Net gain on property, equipment and systems under development	(1)	-	-	(1)
Changes in operating assets and liabilities:				
Accounts receivable	(40)	(13,912)	-	(13,952)
Unbilled revenue	(3,344)	(3,264)	83	(6,525)
Prepaid expenses and other current assets	1,414	(8)	-	1,406
Default charges receivable, non-current	-	(784,181)	-	(784,181)
Other long-term assets	175	-	-	175
Other long-term liabilities	62	-	-	62
Accounts payable	(247)	-	-	(247)
Accrued liabilities	6,847	3,264	(83)	10,028
Deferred revenue	112	-	-	112
Security deposits and reserves	416,984	60,419	-	477,403
Market settlement liabilities	(102,499)	-	-	(102,499)
Long-term CRR liabilities	111,547	-	-	111,547
Net cash provided by (used in) operating activities	\$ 454,575	\$ (737,673)	\$ -	\$ (283,098)



Electric Reliability Council of Texas, Inc.

Consolidating Statements of Cash Flow Information (continued)

	ERCOT	December 31, 2021 TEMSFM	Eliminations	Consolidated
	(In Thousands)			
<b>Investing activities</b>				
Purchase of investments	(27,830)	-	-	(27,830)
Proceeds from investments	130,505	-	-	130,505
Investments in subsidiary	(4,000)	-	4,000	-
Capital expenditures for property and equipment and systems under development	(33,338)	-	-	(33,338)
Proceeds from sale of property and equipment	2	-	-	2
Net cash provided by investing activities	65,339	-	4,000	69,339
<b>Financing activities</b>				
Proceeds from parent company investment	-	4,000	(4,000)	-
Proceeds from debt issuance	-	800,000	-	800,000
Repayment of debt payable	(4,000)	-	-	(4,000)
Payment of debt issuance costs	-	(1,908)	-	(1,908)
Net cash (used in) provided by financing activities	(4,000)	802,092	(4,000)	794,092
Net increase in cash, cash equivalents, and restricted cash and cash equivalents	515,914	64,419	-	580,333
Cash, cash equivalents, and restricted cash and cash equivalents, beginning of year	1,654,896	-	-	1,654,896
Cash, cash equivalents, and restricted cash and cash equivalents, end of year	\$2,170,810	\$ 64,419	\$ -	\$2,235,229