

November 2, 2022

Public Utility Commission of Texas
Chairman Peter Lake
Commissioner Will McAdams
Commissioner Lori Cobos
Commissioner Jimmy Glotfelty
Commissioner Kathleen Jackson
1701 N. Congress Ave.
Austin, Texas 78711

Re: *Brazos Electric Power Cooperative, Inc. v. Electric Reliability Council of Texas, Inc.*
(Brazos Adversary Proceeding) – ERCOT Settlement Update

PUC Project No. 52933 – CY 2022 Reports of the Electric Reliability Council of Texas

PUC Project No. 52937 – CY 2022 Open Meeting Agenda Items Without an Associated Control Number

Dear Chairman and Commissioners:

Electric Reliability Council of Texas, Inc. (ERCOT) hereby provides notice that it supports a final resolution of the Brazos Adversary Proceeding and submits the attached *Brazos Adversary Proceeding Settlement – ERCOT Settlement Update*, which is anticipated to be presented at the Commission’s November 3, 2022, Open Meeting.

Background

On March 1, 2021, Brazos Electric Power Cooperative, Inc. (Brazos) filed its bankruptcy petition under Chapter 11 of the United States Bankruptcy Code (Bankruptcy Code) after failing to pay invoices due to ERCOT in the amount of approximately \$1.9 billion for electricity and Ancillary Services purchased during Winter Storm Uri. ERCOT subsequently filed a proof of claim in the amount of approximately \$1.9 billion based on Brazos’ failure to pay ERCOT as required, which became the subject of the Brazos Adversary Proceeding. Brazos sought to substantially reduce ERCOT’s approximately \$1.9 billion proof of claim and have the entire amount of the reduced claim classified as an unsecured claim. Specifically, Brazos asserted nine separate causes of actions against ERCOT, which are generally based on allegations that: (1) ERCOT failed to follow the Standard Form Market Participant Agreement (SFA) and the ERCOT Protocols by charging excessive prices during Winter Storm Uri; (2) ERCOT failed to mitigate its damages; (3) Winter Storm Uri constituted a force majeure event under the SFA; (4) ERCOT charged excessive Ancillary Services prices; (5) ERCOT failed to ensure the reliability and adequacy of the Texas power grid; (6) “exorbitant and excessive” charges were avoidable and constituted “constructively fraudulent obligations;” and (7) electricity and Ancillary Services are not goods under the

Bankruptcy Code and, accordingly, no portion of ERCOT's proof of claim is entitled to priority status. Certain of Brazos's member co-ops and certain ERCOT Market Participants were authorized by the bankruptcy court to intervene in the Brazos Adversary Proceeding.

In the Brazos Adversary Proceeding, Brazos sought to reduce ERCOT's proof of claim by more than \$1.1 billion—the amount of ERCOT's claim attributable to ERCOT's administrative adjustment to wholesale market prices based on the Commission's Emergency Orders entered February 15 and 16, 2021, directing ERCOT to set prices at their highest to reflect the scarcity in the market during Winter Storm Uri. During the trial, Brazos acknowledged that it owed ERCOT approximately \$762 million. Additionally, Brazos reserved its right to contest in a separate proceeding approximately \$350 million in pre-petition transfers over and above the \$1.9 billion proof of claim. This approximately \$350 million amount represents collateral drawn down by ERCOT before Brazos filed for bankruptcy protection on March 1, 2021. Such action is consistent with the ERCOT Protocols when there is a short-pay event by a Market Participant. Absent those collateral sweeps by ERCOT, Brazos's outstanding short-pay balance would be approximately \$2.25 billion.

Trial in the Brazos Adversary Proceeding began on February 22, 2022. It was suspended on March 3, 2022, at the urging of the Bankruptcy Court in order for the parties to engage in mediation. Following suspension of the trial, ERCOT, Brazos, and certain impacted Market Participants engaged in a lengthy mediation led by U.S. Bankruptcy Judge Marvin Isgur. Mediation culminated in Brazos filing a Chapter 11 Plan of Reorganization (Plan) on September 1, 2022, which included a proposed settlement of the Brazos Adversary Proceeding. The Plan has been subsequently modified by Brazos, and a final version of the Plan was filed on October 27, 2022, with the Bankruptcy Court. All material settlement terms are in the final version of the Plan, which is referred to herein as the "ERCOT Settlement."

The ERCOT Settlement

Under the ERCOT Bylaws, the ERCOT Board of Directors (Board) has broad authority to manage the affairs of ERCOT.¹ Such affairs include litigation against the organization. The Board has authorized ERCOT to pursue settlement and finally resolve the Brazos Adversary Proceeding. ERCOT supports the settlement of the Brazos Adversary Proceeding because it achieves key economic and noneconomic principles, while at the same time mitigating the risk of an adverse judgment. Importantly, the ERCOT Settlement includes the following critical economic terms:

- ERCOT will be promptly reimbursed (on the Effective Date of the Plan) \$599,709,609.22, which represents the amount of Congestion Revenue Rights (CRRs) temporarily used by ERCOT to reduce the amount of the market shortfall immediately following Winter Storm Uri that was attributable to Brazos's short-pay.
- Impacted Market Participants having at least two payment options to address their short-

¹ Amended and Restated Bylaws of Electric Reliability Council of Texas, Inc., Section 4.1.

pays: (1) an earlier discounted payment on the condition they release ERCOT of any obligation to pay the remaining balance or (2) full payment over 30 years.²

ERCOT issued various Market Notices alerting Market Participants to the ERCOT Settlement. In addition, on September 20 and 21, 2022, ERCOT conducted live virtual presentations to present the terms of the ERCOT Settlement and assist Market Participants in the payment election process made part of the Plan. Finally, ERCOT created the following website to provide Market Participants information concerning the ERCOT Settlement: <https://www.ercot.com/about/legal/brazos>. The attached *Brazos Adversary Proceeding Settlement – ERCOT Settlement Update* highlights the key principles and terms of the ERCOT Settlement included in the Plan.

On October 28, 2022, ERCOT voted to approve the Plan, which includes the ERCOT Settlement. No objection to the ERCOT Settlement was filed with the Bankruptcy Court prior to the objection deadline of October 28, 2022. On November 14, 2022, ERCOT will participate at the Brazos Combined Confirmation & Disclosure Statement Hearing and provide testimony on the election notice process. Assuming the Plan is confirmed by the Bankruptcy Court, ERCOT has been informed that first payments are expected by January 2023.

Sean Taylor and I will be available at the Open Meeting to discuss the ERCOT Settlement and answer any questions.

Respectfully,

/s/ Chad V. Seely

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² Impacted Market Participants received an “Eligible Market Participant Election Notice” providing four options, which generally fall into the two options described herein.



In re: Brazos Electric Power Cooperative, Inc.

**Brazos Adversary Proceeding Settlement –
ERCOT Settlement Update**

Chad V. Seely

ERCOT Vice President, General Counsel and
Corporate Secretary

Sean Taylor

ERCOT Vice President and Chief Financial Officer

PUC Open Meeting – November 3, 2022

ERCOT Settlement Principles

- **Overall Objectives:**

- Cognizant of 87th Legislative Session statutory changes regarding defaulting Market Participants (PURA § 39.160). With the ERCOT Settlement, Brazos will not be in default
- Balance current and future wholesale market integrity with litigation risk (*i.e.*, uncertainty in Bankruptcy Court and any subsequent appeals)

- **PURA § 39.160. Default of Market Participant.**

- (b) If a market participant has failed to fully repay all amounts calculated solely under the protocols in effect during the period of emergency of the independent organization certified under Section 39.151 for the ERCOT power region, **the independent organization shall report the market participant as in default to the commission. The commission may not allow the independent organization to accept the defaulting market participant's loads or generation for scheduling in the ERCOT power region,** or allow the defaulting market participant to be a market participant in the ERCOT power region for any purpose, until all amounts owed to the independent organization by the market participant as calculated under the protocols are paid in full



ERCOT Settlement Principles (Continued)

- **Economic Principles**

- **No Default Uplift** under ERCOT Protocols to the wholesale market under any scenario
- Recovery Considerations:
 - Full recovery for Eligible Market Participants in less time than Default Uplift process
 - Flexibility for Eligible Market Participants to choose among several recovery options
- **Immediate recovery** of Brazos-attributable Congestion Revenue Rights (“CRR”) funds (**\$599.7 million (“mm”)**) to fully replenish CRR funds and pay down securitization Subchapter M Bonds
- Release of reserved and unasserted claims regarding ERCOT prepetition transfers of Brazos collateral (approximately \$350.2mm)



ERCOT Settlement Principles (Continued)

- **Non-Economic Principles**

- Brazos (and any Affiliate) no longer acts as financial Counter-Party (Qualified Scheduling Entity (“QSE”) or CRR Account Holder) with ERCOT in the wholesale market
 - Upon transition, will no longer schedule load or generation
 - Upon transition, will never create new financial exposure/risk to the wholesale market
- Appropriate senior management changes for Brazos going forward

Settlement Overview

Material Economic Provisions

- Brazos filed its proposed Plan on September 1, 2022 (revised versions filed thereafter), with terms reflecting those outlined in United States Bankruptcy Judge Marvin Isgur’s final mediator’s proposal (“Mediator Proposal”)
- Entire ERCOT claim amount of \$1,886.6mm (“Brazos Short Pay Claim”) to be allowed and ERCOT will avoid further litigation
 - \$599.7mm is owed to replenish Brazos-attributable CRR funds previously advanced to Market Participants
 - \$374.8mm owed to pay down securitization Subchapter M Bonds
 - \$224.9mm owed to fully replenish CRR funds
 - **The remaining \$1,286.9mm is owed to Market Participants**



Settlement Overview

Election Options for Eligible Market Participants

- Eligible Market Participants could elect among the following four options regarding treatment of their allocable portion of the Brazos Short Pay Claim
 - **Option 1:** Market Participant Accelerated Cash Recovery (“Accelerated Recovery”)
 - Approximately 65% nominal recovery: Effective Date: ~43%; Generation Asset Sale Date: ~9%; over 12 years from operations: ~13%
 - **Option 2:** Market Participant Deferred Cash Recovery (“Deferred Recovery”)
 - 100% nominal recovery over 30 years
 - **Option 3:** Market Participant Convenience Cash Recovery
 - Approximately 63% nominal recovery on Effective Date
 - **Option 4:** Allocation of the Eligible Market Participant share between Option 1 and Option 2
- Failure to elect any of the above four options, or selecting more than one option, would result in an Eligible Market Participant automatically being deemed to have elected Option 2.

Settlement Overview

Primary Funding Sources for Brazos Short Pay Claim Recovery

- Brazos has estimated the following funding requirement for payments
 - \$1,153.5mm on Effective Date
 - \$116.6mm on Generation Asset Sale Date
 - \$166.0mm over 12 years funded from Transmission & Distribution (“T&D”) operations
- \$599.7mm paid on Effective Date replenishes CRR funds and pays down securitization Subchapter M Bonds
- Remaining allocable portion of these amounts will be:
 - Paid to ERCOT (who will subsequently pay Eligible Market Participants) on the relevant dates for Accelerated Recovery and Market Participant Convenience Cash Recovery
 - Funded into a designated escrow account⁽¹⁾ for Deferred Recovery



1) Interest-bearing escrow account with a banking institution, with a minimum rating of A- with S&P or Fitch or A3 with Moody's; selected by ERCOT and Brazos

Settlement Overview

Material Non-Economic Provisions

- The ERCOT Settlement also includes material non-economic provisions requested by ERCOT including:
 - Brazos will no longer be a financial Counter-Party (QSE and CRR Account Holder)
 - Brazos will stop scheduling load by March 1, 2023
 - Brazos will sell all owned Generation Assets
 - Brazos will stop scheduling its own generation by no later than one year from Effective Date
 - Brazos Retained Agreements must be through a third-party non-Affiliate QSE starting March 1, 2023
 - Certain post-Effective Date changes in Brazos senior management team (as listed on the following page)

Settlement Overview

Changes in Brazos Senior Management Team

- **Clifton Karnei** (Brazos Executive Vice President & General Manager) will cease his employment before the earlier of (i) March 31, 2023, or (ii) the date that is 30 days after the Generation Sale Closing Date
- **Josh Clevenger** (Brazos Vice President of Power Supply) and **Travis “Dean” Thrall** (Brazos Vice President of Generation) shall cease their employment on or before the date that is 30 days after the Generation Sale Closing Date
- **Philip Segrest** (Brazos General Counsel) shall exit his existing role as General Counsel on the date that is 30 days after the Effective Date
- Additionally, no current or former Brazos employee in its power supply or generation functions may become a Principal of Brazos in the future, as defined in ERCOT Protocols

Election Notice Process

- From September 20, 2022 – October 21, 2022, ERCOT facilitated an Election Notice process for the **\$1,286.9mm** owed to Market Participants
- 755 Election Notices were distributed to Eligible Market Participants
- The table below summarizes final⁽¹⁾ Election Notice results

	Count	Count %	Dollars	Dollars %
Total Election Notices (Notices)	755	100.00%	\$1,286.9mm	100.00%
Returned Notices	740	98.01%	\$1,286.3mm	99.95%
Selected Option 1 (Accelerated Cash Recovery)	388	51.39%	\$1,239.2mm	96.30%
Selected Option 2 (Deferred Cash Recovery)	34	4.50%	\$4.4mm	0.34%
Selected Option 3 (Convenience Cash Recovery)	316	41.85%	\$1.2mm	0.09%
Selected Option 4 (Allocation between Option 1 & 2)	2	0.27%	\$41.5mm	3.22%
Notices Not Returned (Option 2: Deferred)	15	1.99%	\$0.6mm	0.05%

- Before November 14, ERCOT will file the ERCOT Recovery Appendix which will include election and recovery information and be part of the Brazos Combined Confirmation & Final Disclosure Statement Hearing



1) Election Notice counts and related dollars are subject to final verification

Update on Brazos Plan Negotiations – Resolved

- On October 27, 2022, Brazos filed an amended Plan to, among other things, resolve ERCOT’s open issues with the Plan
- The amended Plan includes the following changes:
 - Modifications to certain defined terms in the Plan
 - Modification to the ERCOT release language in the Plan to address comments provided by certain Market Participants
 - Addition of new language capping Brazos’ power-supply resources at each single delivery point and collectively **across its wholesale transmission or distribution service area** (but subject to being increased with the consent of ERCOT, the Public Utility Commission of Texas (“PUCT”), or such other regulatory body with jurisdiction over the services provided)
 - Addition of new language stating that Brazos shall never own or operate generation assets or electric energy storage facilities for the purpose of offering power for sale into the wholesale energy market

Update on Brazos Plan Negotiations – Resolved (Continued)

- **Restrictions on Retained Agreements:** Brazos’ ability to extend the maturity dates of two Retained Agreements (Hydro Power Sales Contract for 36 MW [Whitney Dam] & Solar Power Sales Contact for 42.5 MW) is restricted
- **Distribution of T&D Asset Proceeds:** Brazos is prohibited from distributing the proceeds of any sale of T&D Assets to any entity (other than to creditors with valid liens on such assets) prior to the payment in full of the \$116.6mm funding requirement from the sale of the generation assets; thereafter, Brazos may distribute the proceeds under limited conditions including ERCOT providing approval in its sole discretion

Update on Brazos Plan Negotiations – Resolved (Continued)

- **Third-Party Bankruptcy Monitor:** In the event Brazos is required to schedule Load (even through a third-party QSE) for a Defaulting Member (if any), Brazos shall, in consultation with ERCOT, retain an independent third-party monitor appointed by the Bankruptcy Court to assess the adequacy of supply/load arrangements relative to market risks, which assessments shall be evidenced by a report to the Bankruptcy Court and ERCOT; includes corrective measure processes and monetary payments to the Ratepayer Hardship Fund for failure to satisfy conditions

Final Comments

- On October 28, 2022, ERCOT voted to approve the Brazos Plan which includes the ERCOT Settlement
- No objections to the ERCOT Settlement have been filed with the Bankruptcy Court
- ERCOT will participate at the Brazos Combined Confirmation & Disclosure Statement Hearing, and provide testimony on Election Notice process, on November 14, 2022
- Assuming the Bankruptcy Court confirms Brazos' Plan, Brazos has indicated first payments to ERCOT by end of year or January 2023

Calendar of Key Plan Dates

October 2022						
S	M	T	W	T	F	S
						1
2	3	4	5	6	7	8
9	10	11	12	13	14	15
16	17	18	19	20	21	22
23	24	25	26	27	28	29
30	31					

November 2022						
S	M	T	W	T	F	S
		1	2	3	4	5
6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30			



Plan-related Events



Market Participant Events



Past Events

Event	Date
Election Notice Submission Deadline	Oct. 21, 2022, at 5:00 p.m. (CT)
Deadline to File Plan Supplement	Oct. 24, 2022
Objection Deadline	Oct. 28, 2022
Voting Deadline	Oct. 28, 2022
Combined Confirmation & Final Disclosure Statement Hearing	Nov. 14, 2022, at 9:30 a.m. (CT)

