Steering Committee of Cities Served by Oncor

2018 Year in Review

OCSC Has Another Productive Year in 2018

This past year was another active year for the Steering Committee of Cities Served by Oncor (OCSC). On behalf of its member cities and their residents, OCSC participated in numerous proceedings before the Public Utility Commission (PUC). This Year in Review highlights the significant events of 2018 that impacted OCSC and what is on the horizon for this year. Looking ahead, 2019 will likely be another busy year for OCSC at the PUC, the Electric Reliability Council of Texas (ERCOT), the Legislature, and the courts.

Oncor to Acquire InfraREIT and Sharyland Utilities

On November 30, 2018, Oncor Electric Energy Delivery Company LLC (Oncor), Sharyland Distribution & Transmission Services, L.L.C. (SDTS), Sharyland Utilities, L.P. (Sharyland) and Sempra Energy (Sempra) filed a Joint Report and Application for Regulatory Approvals at the Public Utility Commission (Commission).

The application seeks approval for several transactions: (1) the exchange of transmission assets between SDTS and Sharyland and the respective CCN amendments required; (2) the acquisition of InfraREIT, Inc. (InfraREIT) by Oncor; and (3) the acquisition of a 50% indirect interest in Sharyland by Oncor and Sempra.

On October 18, Sempra announced this deal will result in Oncor acquiring, and co-investing by the parties in, Sharyland. InfraREIT owns and leases rate-regulated electric transmission assets in Texas. Sharyland is an electric transmission utility. Sempra Energy owns an approximate 80-percent ownership stake in Oncor.

As you may recall, last July Oncor and Sharyland agreed to swap assets in a transaction valued at approximately $400 million. Sharyland received approximately 258 miles of 345 kV transmission lines from Oncor, and Oncor received all of Sharyland's distribution network and its approximately 54,000 retail delivery customers.

Under the agreement, Oncor will acquire 100% of the equity interests of InfraREIT, including all the limited-partnership units in its subsidiary InfraREIT Partners, LP, for approximately $1.275 billion.

Concurrently, Sempra Energy will acquire a 50-percent limited-partnership interest in a holding company that will own Sharyland for approximately $98 million. The other 50% of the holding company will be owned by entities controlled by Hunter L. Hunt (founder and Chairman of Sharyland) and other members of the family of Ray L. Hunt.

Upon closing, Oncor will own and operate all of Sharyland's existing electric transmission assets located in Central Texas, West Texas, and the Texas Panhandle and South Plains. Sharyland will continue as an independent privately-held transmission utility, owned by the new holding company, and will own the transmission assets that it developed in South Texas.

The application enumerates the benefits of the proposed transaction, including elimination of the Sharyland/SDTS REIT structure, consolidation of geographically compatible transmission systems, and Sempra's financial investment in the South Texas region.

The transactions will ultimately require the approval of the Public Utility Commission of Texas, as well as a vote of approval from the majority of InfraREIT shareholders, among other approvals. Currently, the hearing on the merits is scheduled for April 10-12, 2019.

The PUC Still Contemplating Decision on Market Changes after Summer 2018 ERCOT Review Project

As the summer peak season ended, the PUC opened Project No. 48551, seeking comments from interested parties on a number of questions related to the performance of the ERCOT wholesale market and whether any changes need to be made to account for the current state of the market.

Leading up to summer, observers expressed concern that ERCOT could experience rolling blackouts due to high temperatures and plant retirements. Thankfully, no such grid emergency developed, and the system appeared to have handled record electricity usage and persistent high temperatures. However, because summer 2018 experienced so few days of constraint, generators did not benefit from as many instances of peak pricing as expected.

In their comments and at the PUC workshop, power generators such as Calpine Corp., NRG Energy, and Exelon Corp. asked the PUC to change the way ERCOT determines wholesale prices by shifting the Loss of Load Probability (LOLP) factor in the Operating Demand Reserve Curve (ORDC). Exelon estimates that this shift in the ORDC would raise electricity prices $4 billion for Texas consumers. Generators insist that this change is needed to guarantee higher revenues, which would provide the much needed incentive necessary to invest in new power plants, and accordingly, provide more reliability to consumers. Others, including Texas Industrial Energy Consumers (TIEC) and the independent market monitor, Potomac Economics, believe that the ORDC is working within the intended parameters and that an LOLP shift may not be absolutely necessary.

Ultimately, it is a policy decision for the PUC to determine whether changing the wholesale price structure is necessary to incentivize future generation growth and ensure grid reliability. ERCOT's recent forecast of tightening reserve margins over the next five years will certainly be a factor in the PUC's decision.

While the Project was listed on the December 7 and 20 open meeting agendas, and stakeholders were prepared for a contentious discussion, the PUC opted not to discuss the matter. There is no current estimate for when the Project will come up again for consideration, but we can likely expect a decision early in the new year.

Commission Holds Workshop in Substation Rulemaking

On April 10, the Public Utility Commission (PUC) opened Project No. 48251, Rulemaking Regarding the Review and Approval of Substations. The Commission issued a request for comments from parties regarding whether high-voltage switching substations should remain exempt from the requirement to obtain a certificate of convenience and necessity (CCN). Comments were filed on October 30, and on November 7, the PUC held a workshop for stakeholders to discuss their views and comments.

A number of utilities opposed the removal of the existing exemption for substations for the need to obtain a CCN. The Oncor Cities Steering Committee filed comments and advocated for the creation of some process by which cities can express their concerns over the effects of a proposed substation, preferably through the Commission's existing CCN process. The utilities and other industrial level consumers raised concerns over slowing down the process by which substation infrastructure could be completed, and thus affecting economic growth.

The Commissioners expressed a desire to have some sort of review over these types of projects, so we anticipate some form of change will occur, but it remains to be seen as to whether it will be the creation of an Electric Reliability Council of Texas (ERCOT) review process, PUC review process, or a combination of the two. PUC Staff has been directed to summarize the comments received and file those with the Commission. We anticipate seeing the summary within the first few months of 2019, after which the Commission will provide Staff with further direction on whether to draft proposed rule changes.

PUC Project No. 48540 - Review of Real-Time Co-optimization in the ERCOT Market

The Public Utility Commission (PUC) opened up several projects this summer. At the August 9 open meeting, the PUC issued questions for stakeholders to address issues related to the June 29 Electric Reliability Council of Texas (ERCOT) report of its studies of the benefits of real time co-optimization of energy and ancillary services and the benefits of including marginal losses in security-constrained economic dispatch.

Parties filed comments in Project 48540 - Review of Real-Time Co-optimization in the ERCOT Market. According to Potomac Economics (the firm that provides Independent Market Monitoring services for the ERCOT system), real-time co-optimization would result in significant savings to customers for costs associated with congestion on the transmission system, ancillary services, and the cost of energy itself. Potomac's results indicated that the market would see a $257 million reduction in system congestion costs, a $155 million reduction in the cost of ancillary services, and a $1.6 billion savings in energy costs, equating to approximately $4/Mwh. ERCOT also issued a review of the benefits of real-time co-optimization in June.

Several parties supported the transition to real-time co-optimization, citing benefits such as lower production costs and other market improvements. Other parties expressed support but raised some concerns with the transition itself on the market. Very few parties opposed the transition.

This project was not discussed at the December 7 or 20 open meetings, but will likely be discussed on the January 17 open meeting along with other, related projects.

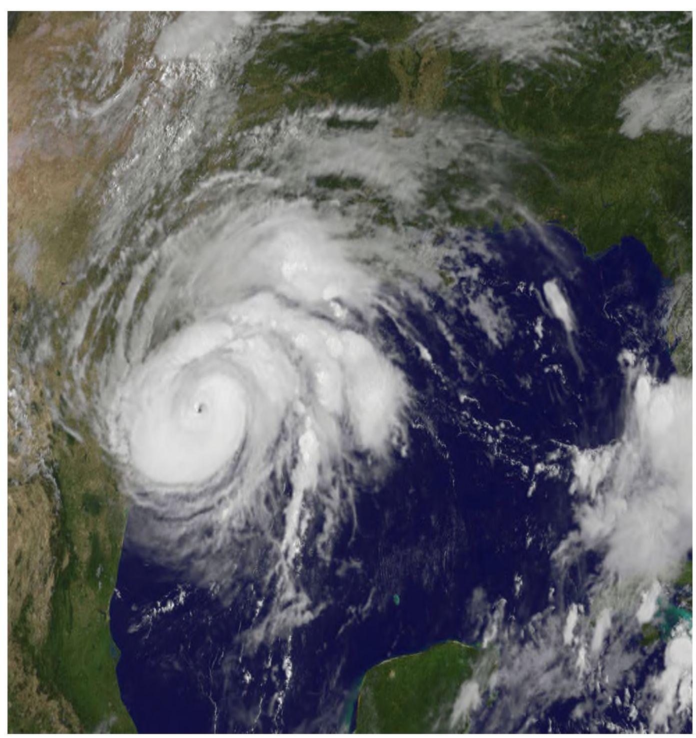
AEP Texas Hurricane Harvey Proceeding Settles

On August 7, 2018, AEP Texas filed an Application at the Commission seeking approval of approximately $415 million in costs associated with Hurricane Harvey. These costs are spread out by distribution and transmission functions. The cities of Corpus Christi, Penitas and Sullivan City, the Gulf Coast Coalition of Cities (GCCC), the Lower Rio Grande Valley Development Council (LRGVDC), and Oncor Cities Steering Committee (collectively Cities) intervened in the proceeding. Cities retained a consultant and examined the application to ensure that AEP Texas' expenditures are reasonable and prudent, and comport with PURA.

Cities filed testimony recommending an adjustment of $24.2 million to reflect double counting of distribution operations and maintenance costs, and $3.7 million for incorrectly included transmission-related costs. Commission Staff filed testimony recommending an additional disallowance of AEP Texas' litigation costs of $571,200. Parties reached a settlement that resolved all issues in the case.

As a result of the settlement, AEP Texas will reduce its requested distribution-related costs by $5 million, remove $3.7 million of transmission-related costs, and reduce the transmission cost recovery by $5 million to account for insurance proceeds, subject to a true-up once the final insurance proceeds are received. Additionally, AEP Texas has agreed to pay Cities' litigation costs. These will be paid directly to the city groups involved in the case.

AEP Texas filed settlement documents in Docket No. 48577 on November 30, 2018. A final decision is expected in January.



PUC Project No. 48023 - Rulemaking to Address the Use of Non-Traditional Technologies in Electric Delivery Service

Last fall, the PUC received initial and reply comments in Project No. 48023 – Rulemaking to Address the Use of Non-Traditional Technologies in Electric Delivery Service. Many parties filed comments addressing the uncertainty of the law surrounding a transmission and distribution utility (TDU) owning and implementing an energy-storage device; yet, others argued that the law clearly prohibits a TDU from owning such a device. The Oncor Cities Steering Committee (Cities) filed comments in the Project, arguing that the statute and Commission rules are unclear as to whether TDUs can legally own an energy-storage device.

The PUC has not yet determined whether a TDU-owned energy-storage device falls within the Public Utility Regulatory Act's (PURA) definition of "generation asset," or whether TDU ownership and use violates the prohibition against a TDU providing competitive services. However, the PUC Chairman did informally mention at the December 20 open meeting that she believes the statute is unclear.

Utility-owned energy-storage devices have the potential to provide reliability and cost-saving benefits over traditional transmission and distribution approaches, but stakeholders must first be given clarity on the PUC's application of the relevant PURA provisions. On the basis that the PUC determines PURA and PUC rules currently provide for a legal basis for utilities to own and operate energy-storage devices, many parties, including Cities in its comments and reply comments, argue that a CCN or similar pre-approval process should be required, providing further oversight of such projects.

The Commissioners also discussed whether the PURA definition of "generation asset" regarding batteries requires municipalities or co-ops (either is considered a "Non-Opt-In Entity" or "NOIE") to register as a power generator. While the Scope of Competition Report explains how the PURA definition of "generation asset" may require NOIEs to register as a power generator, Commissioner D'Andrea, at the December 20 open meeting, made a lengthy, convincing argument for why Chapters 40 and 41 of the Texas Utilities Code make clear that NOIEs can own batteries without having to register. While this discussion does not have any binding effect, the unanimous agreement amongst the Commissioners regarding Commissioner D'Andrea's argument is a strong indication of how the Commission will view any potential conflicts or issues regarding NOIE ownership of batteries.

At the December 20 open meeting, the Chairman indicated that the Commission would make a decision regarding Project No. 48023 at the January 17, 2019 open meeting.

2019 OCSC Meetings

March 7

May 9

August 15

December 12

2019 Officers

Paige Mims—Chair

Don Knight—Vice Chair

Adrienne Lothery—Secretary

Questions?

For questions about any OCSC matter or communication, please feel free to contact:

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