



REP Certificate No. 10060

February 15, 2011

Re: Flaws in ERCOT Protocols/Market Abuse and Collusion by Generators in ERCOT

Written testimony

Honorable Senators:

You are aware of the events which transpired Feb. 3 and 4th. While we all believe in Free Market Capitalism, and limited Government Regulation, I am compelled to bring to your attention, a fatal flaw in the ERCOT protocols regarding credit exposure in the ERCOT market and which intentionally and unfairly forces some Market Participants to bear virtually all of this risk/exposure on behalf of other market participants. The egregious cost of this exposure, intentionally created by ERCOT Power Generator's, must be borne by Independently-Owned R.E.P.s and/or be passed on to electric consumers in Texas, a disastrous scenario under our current economic condition in our great State.

In the "old days" under a regulated paradigm, Utilities were not incentivized to be competitive or efficient and when a natural disaster occurred and great expense was incurred by the utilities to bring their infrastructure to operating order, the utility would go the PUCT for a rate increase and it would be granted. In the end, the consumer would pay for the utilities' inadequacy or for any unforeseen acts of nature.

Today, under the current ERCOT Protocol Structure, the Independently-Owned Retail Electric Providers (Non-Utility or Generator-affiliated R.E.P.s) bear virtually all of this risk. To date, Generators, remnants of the old utility paradigm have influenced the ERCOT protocol process greatly to the effect that they carry minimum risk and put the burden of their credit exposure on R.E.P.s. If the generators have Retail subsidiaries (NRG, Luminant, Direct Energy, Constellation, for example), their credit exposure on the retail side is basically "a wash" since their generation side/affiliate receives the benefit of the collateral posted by R.E.P.s and other Market Participants. Independent R.E.P.s such as ourselves are in the end, left "holding the bag." Some estimates are that ERCOT is two to three times over-collateralized by market Participants.

If the generators and the TDSPs are the "backbone" and "arms and legs" respectively of the electric market in Texas, then R.E.P.s are the "hands and feet" of the market. Without R.E.P.s, there is no way to get the commodity, the kwh to the consumer, Mrs. Jones or Mrs. Rodriguez or any type of small commercial or large

industrial end user. We take great financial risk by forecasting what our customers will use in the future, purchasing that volume of kwhs for a term, taking ownership of that electricity from a power producer or supplier, then having those kwhs delivered. In turn, we are responsible for paying, without fail, whether we collect from the end user or not, our suppliers (generators) , TDSPs, ERCOT, (who in turn also pay generators for imbalances) and the State comptroller's office.

Hino Electric Power Company has transacted in ERCOT since May, 2003, paying its counter parties; Power Suppliers, ERCOT and TDSPs, over \$150,000,000.00. Never once has Hino Electric been late on any payment to any counter party and Hino Electric has met and is current regarding the PUCT's and ERCOT's financial and technical requirements. As The first Hispanic owned R.E.P. in Texas, and the Only R.E.P. based in the Rio Grande Valley, we know that the Legislature and the PUCT embrace market diversity and Hino Electric certainly fits the bill, serving more than 95% of its load in the Rio Grande Valley, bringing lowest cost electric power and face to face service to Rio Grande Valley Businesses and Residential customers.

On Feb 4th, over 300 MW of load was curtailed in the Rio Grande Valley. AEP TCC and ERCOT have all of the data regarding these outages and curtailments to verify this. We received calls all day long regarding outages as many of our customers were without power on both Feb. 3 and Feb. 4. While the meters did not turn for our customers during this time, ERCOT, using its skewed and generator-biased protocols, estimated that our customers used more kwhs than normal during this same period and charged us egregious and outrageous rates per unit, to the tune of \$7.00 per kwh when going retail, not wholesale market prices are \$0.065/kwh, a difference of over 100 times the current retail market rates.

In turn, the Commission wishes that we not pass these charges on to our customers. Additionally and ironically, we are not able to charge our customers during this period since many of our customer's meters did not "turn" during the outages, yet ERCOT charges us as if they did turn and asks us for additional collateral due to their "estimate" of our TPE ("Total Potential Exposure") going forward.

Thanks to Market Participant's (Generators) incompetence and egregious failures, the independently owned R.E.P.s must bear all risk by paying for the Generator's mistakes and posting additional collateral due to their incompetence and ill-preparedness. Ultimately this is not good news for Mrs. Jones or Mrs. Rodriguez and Businesses in the Rio Grande Valley as egregious ERCOT "market charges" of \$7.00 per kwh and egregious margin calls must ultimately be passed on to these consumers. (ERCOT has made adjustments to credit calculations, market notice W-A020311 attached ). This situation will occur again if reasonable price caps are not put into place as is explained forthcoming.

Can it be that Generators are justified in charging Market Participants 100 times current retail market rates in times of natural disasters? The Texas Attorney General's office has implemented and enforced rules and laws which prohibit Gasoline marketers/retailers from "price-gouging" consumers during Hurricanes for example. During and after the approach of Hurricanes in our State, retailers are not allowed to take advantage of consumers in times of dire need. Lumber and hardware companies, gasoline retailers, ice companies and so on are to be investigated and even prosecuted if they are found to be "price gouging."

In a free market, if a business sells its product or service for too high of a price, it usually does not make the sale, a competitor makes the sale. If the business continues this trend of "pricing itself out of the market," it goes out of business. Such is not the case with generators in ERCOT. Whatever generators charge the market, R.E.P.s must pay "imbalance charges" for their load at whatever bid is settled in the SPP market. In times such as this past weather calamity, generators are able to charge the highest price possible. In times of severe need, this can be considered "price gouging."

Why then are generators in ERCOT not prohibited from price gouging during this past natural disaster or any natural disaster?

In times of severe cold snaps and severe heat waves, price caps or moratoriums on wholesale spot market power prices should be implemented in ERCOT. Hino Electric in no way is advocating that any business or enterprise should not be free to make a profit. What we are advocating is "anti-price gouging" and egregious wholesale charges.

Hino Electric and all other independent R.E.P.s should not have to collateralize billion-dollar-generators and their shareholders because of their incompetence. How coincidental it is that 50 power plants representing 7,000 MW of supply went off-line at the same time during this period? Yet Market Clearing Prices (SPP) of \$7,000.00 per MWH (\$7.00 per kwh, 100 times current retail market prices) will be charged by generators and ERCOT to R.E.P.s by ERCOT's "Estimates" of R.E.P.'s customer's loads during the exact same time periods that these same end users were without power. ERCOT engineers will come up with equations and reasons why their calculations are justified. Math is an infallible science. No one needs a PHD in math to realize how many tens of millions of dollars the generators will collect if these charges are implemented and how much Texas Consumers and R.E.P.s in Texas will lose due to the Generators' "coincidental" timely malfunction and intentional incompetence. Lastly, how coincidental is it also that these Coal and Gas power plants in many instances, owned by the same power generators in ERCOT which have plants in other states do not have these failures under blizzard conditions?

I respectfully and humbly ask that an investigation be implemented into possible market abuse and collusion among generators. I ask that price caps be implemented in the ERCOT SPP wholesale spot market during times of extreme weather events and I ask that all efforts be made to bring equity in ERCOT protocols, regarding Retail Electric Provider's credit requirements in order to bring justice and equality to our great Electric market in our Great State.

Respectfully Submitted,

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President/CEO  
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<http://online.wsj.com/article/SB121625744742160575.html>

Wall Street Journal

JULY 17, 2008

## Deregulation Jolts Texas Electric Bills

Feast or Famine

**John Henderson, senior vice president of generation for Suez, says the plant can make a decent return if it garners that \$2,250 price at least 15 hours a year. "In this business," explains Mr. Henderson, "you have feast years and you have famine years." He acknowledges that 2008 is shaping up to be a feast year.**

The practice is reminiscent of one that played a role in the meltdown of California's electricity market earlier this decade. Afterwards, the Federal Energy Regulatory Commission prohibited "hockey-stick bidding," named because a graph of the bid structure makes it look like a hockey stick standing on its blade. The deregulated Texas market, because it has no major connection to other states' grids, is not subject to FERC rules.

Suez spokesman Rob Minter says his firm doesn't practice hockey-stick bidding but uses a rational strategy to operate the plant profitably under the law.

Texas plans to make improvements to its electricity market which officials say will help ease the recent transmission congestion and, hopefully, bring prices down. Early next year, ERCOT plans to roll out a new \$325 million computer system that will change the way it handles congestion. California has been working on a similar system for seven years and is still not done.

The grid operator also will add a new energy auction for power intended to be delivered the next day instead of on the current day like the spot market, something it hopes will bring more orderliness to the market.

State officials say Texas has gone too far to turn back now. "I don't think we can put the toothpaste back in the tube," says Mr. King, the state representative. "All we can do is go forward."

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Credit calculations were adjusted, but the protocols should still be changed.

**NOTICE DATE:** February 10, 2011

**NOTICE TYPE:** W-A020311-02 Financial/Credit

**SHORT DESCRIPTION:** Clarification on credit updates

**INTENDED AUDIENCE:** Counter-Parties and QSEs

**DAY AFFECTED:** February 10, 2011

**LONG DESCRIPTION:** The following are clarifications on the approach outlined in Market Notice W-A020311-01 to exclude the impact of last week's weather event from forward components of credit calculations.

- 1) DALE – Per Market Notice W-A020311-01, the Daily Average Liability Extrapolated (DALE) calculation was held constant from Friday, February 4, 2011, through Wednesday, February 9, 2011. After February 9, ERCOT indicated that it would calculate the DALE excluding the Day-Ahead Market (DAM) runs for Operating Days February 3 and 4 from the DALE.

To exclude the DAM runs for Operating Days February 3 and 4 from the DALE, ERCOT will use Invoices generated for Operating Days subsequent to February 4 to calculate DALE. ERCOT will use the number of Invoices available (e.g. on February 10, the Invoices for Operating Days February 5 – 7 will be used; on February 11, the Invoices for Operating Days February 5 – 8 will be used, etc).

- 2) ADTE – ERCOT will exclude Operating Days February 2 **and** 3, 2011, from the Average Daily Transaction Extrapolated (ADTE) calculated beginning February 18, 2011, before determining the Highest ADTE.

**CONTACT:** If you have any questions, please contact Vanessa Spells at [vspells@ercot.com](mailto:vspells@ercot.com), (512) 225 7014, or Rizaldy Zapanta at [rzapanta@ercot.com](mailto:rzapanta@ercot.com), (512) 225-7015. You may also send credit inquiries to [ercotcredit@ercot.com](mailto:ercotcredit@ercot.com).

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