

Texas needs new laws that are stronger than TXU and other powerful utility companies

We don't need a band-aid—we need major surgery to save deregulation

Toughen CSSB 482 and CCSB 483

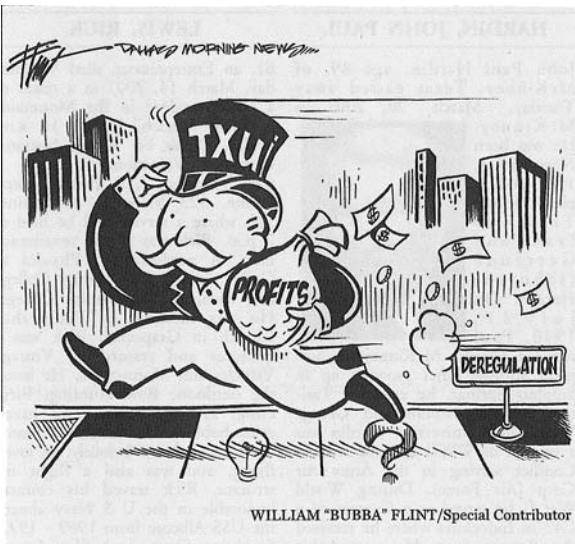
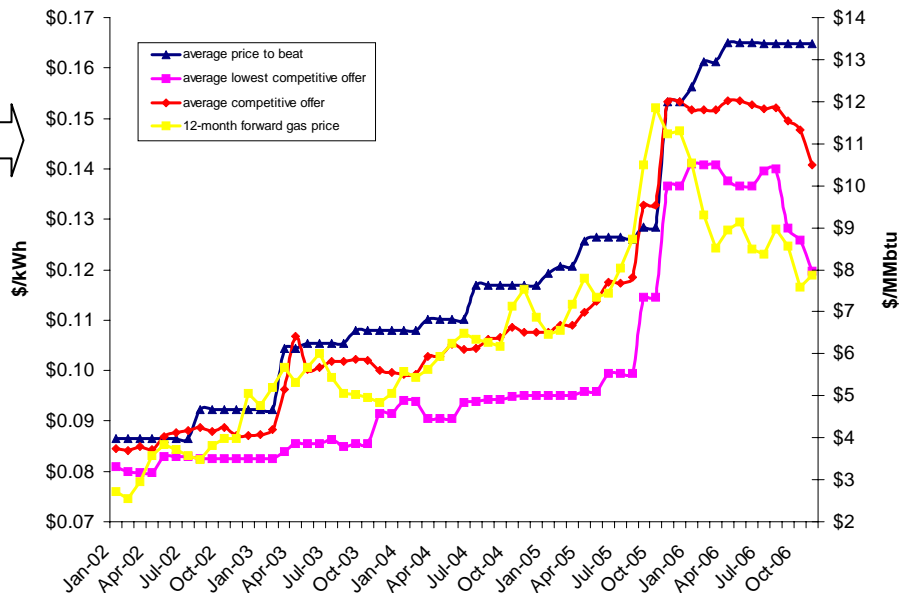


Prices have gone up 88% since deregulation – and haven't come down even though generation costs have returned to normal.

from a presentation by The Public Utility Commission of Texas Commissioner Barry T. Smitherman to KEMA's Executive Forum on March 8, 2007

SOURCE: Electric Scope Report (Dec. 2006)

Average Residential Price to Beat vs. Competitive Offers



TXU has been accused of purposefully withholding energy in zones to increase prices - and they aren't the only ones

Prices increased for all Texas electricity consumers by 15 % when TXU abused their market power. The PUC has fined TXU \$210 million—the largest fine in PUC history for misbehaving

Ultimately—what happens to prices when the new TXU flips this company and walks away with billions in profits, saddling consumers with billions in debt?

The “new TXU” is making a lot of promises- but how can we keep them to their word? (see back cover)

The following suggested amendments to CSSB 482 and CCSB 483 will protect consumers

Key consumer protections in Senate Version that need to be restored to CSSB 482

- Allow businesses to have their complaints heard by the PUC
(delete the word residential on page 1 line 8 of CCSB 482)
- No Deposits if you have good credit with utility companies
(insert section 1 of Senate's version of 482)
- No summer and winter cut-offs
(insert paragraph h 1-3, pg 6 l-5---pg 7 l-5 of Senate version)
- Protections for critical care patients
(insert section 4 pg 7 from Senate version)
- No cancellation cost for month to month plans
(insert section 5- pg 11-12 of Senate version)

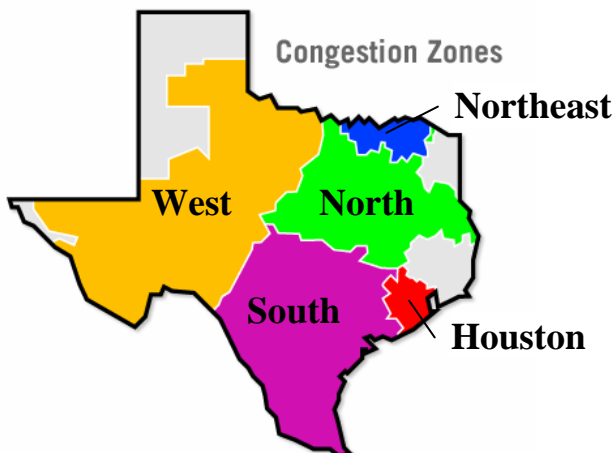
Key Market power protections:

- Senate requires full separation of companies into three parts- generation, transmission and distribution, and retailers
(insert section 2 pg 4 of Senate version of 482)
- No reduction of number of customers required for TXU in House bill
(insert section 6 of the Senate version pg 12-14 and strike section 4 l pg 4 lines)
- If consumers don't make a choice, the House version says companies can slam them and put them in whichever rate plan the energy company chooses
(See page 7 lines 12-page 8 l-15 of Senate version)
- Senate version allows the PUC to set prices at 1 cent above the average cost if a number of customers still don't make a choice
(insert section 8 of the Senate version-pg 15-16)

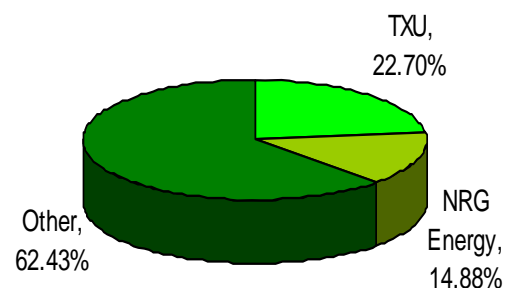
Key market power protections that need to be added to CSSB 483 to prevent abuse.

- Restore 25% cap on market power in zones or regions
(insert pg 4 line 10-12 and page 6 line 21 of Senate version)

ERCOT Congestion Management Zones



Total ERCOT Power in 2005



TXU's Size:

TXU Power has over 18,300 megawatts (MW) of generation capacity in Texas, making it the largest generator in Texas.¹ NRG Energy is second in generation capacity offering about 10,658 MW to Texans.² TXU is even more influential in ERCOT's north and west zones as a result of transmission line (power line) issues.³ In the **North Zone, TXU was in a crucial position 72%** of the time in the presence of congestion in 2003, meaning that the market depended on at least some of TXU's power to meet energy demand as there was not enough power from a mix of other generators to satisfy the market. In the **West Zone, TXU was in a crucial position 52% of the time** when congestion was present in 2003.⁴ Congestion occurs when there is "excessively high demand for power transfers across the grid".⁵

- Restore PUC authority over merger and acquisition of generating plants
(insert section 7 from senate version-pg 14)
- Allow the Office of the Attorney General the authority to pursue civil and criminal actions for market power
(insert pg 7 lines 25-pg 8 line 8 from Senate version)
- Give the PUC additional powers to protect Texas from market abuse
(see recommendations in PUC's scope of competition report-pgs 91-116)

The buyers of TXU and their bankers have been in trouble with regulators and the courts in many states:

- **OTHER STATES REJECTED SIMILAR DEALS BECAUSE OF TOO MUCH DEBT.** More than 80 percent of the \$45 billion purchase price is leveraged debt, meaning that KKR and TPG are borrowing \$37 billion from the four investment banks to buy TXU. Borrowing that much money is inherently risky and places enormous financial pressure on the borrowers (KKR and TPG) to pay back that money—and fast. The high level of debt will ruin TXU's credit ratings, making it more expensive for the company to borrow money, meaning ratepayer's bills will rise. Indeed, KKR and TPG each were rejected in recent attempts to acquire other utilities, with state officials nixing the deals citing the highly leveraged debt as posing inherent risks to ratepayers. In March 2005, the Oregon Public Utility Commission unanimously rejected the proposed buyout of Portland General Electric by TPG, citing the "large debt burden and short-term ownership as the major sources of risk."⁶ In December 2004, the Arizona Corporation Commission rejected an attempt by KKR, JP Morgan Chase and Wachovia to acquire Tucson Electric. Arizona regulators found the financial firms' offer was not in the public interest because the new company's debt load imposed too many risks for consumers.⁷
- **KKR WAS THE SUBJECT OF THE BOOK --BARBARIANS AT THE GATE --** by Wall Street Journal reporters Bryan Burrough and John Helyar, about the leveraged buyout (LBO) of RJR Nabisco. The book was later made into a made-for-TV film by HBO, also called Barbarians at the Gate. Barbarians at the Gate expounds on the evils of LBOs and the unfortunate side effect of a concerning level of debt to shareholders created through augmented buyout prices.
- **THE BANKS BEHIND THE EQUITY PARTNERS HAVE A QUESTIONABLE TRACK RECORD.** The four investment banks behind the TXU buyout have paid a combined \$6.3 billion to settle various allegations of fraud, abuse and energy market manipulation. This troubled history gives pause to them owning the largest utility in the Texas deregulated market. (see *Appendix A* for more info)

¹ TXU Corp. Announces Plan for Additional Nuclear Power, News Release 8-31-06. <http://www.txucorp.com/media/newsrel/detail.aspx?prid=980>

² NRG Energy Full Description- <http://stocks.us.reuters.com/stocks/fullDescription.asp?symbol=NRG&WTmodLOC=L2-LeftNav-8.5-FullDescription>

³ Staff Inquiry into Allegations Made by Texas Commercial Energy Regarding ERCOT Market Manipulation, Market Oversight Division-Public Utilities Commission 2003.

⁴ Staff Inquiry into Allegations Made by Texas Commercial Energy Regarding ERCOT Market Manipulation, Market Oversight Division-Public Utilities Commission 2003.

⁵ Electric Reliability Council of Texas, Inc - "Congestion" - <http://www.ercot.com/gridinfo/congestion/index.html>
www.puc.state.or.us/PUC/news/2005/2005_007.shtml

⁷ www.cc.state.az.us/news/pr12-23-04.htm

Give the PUC the tools to make TXU keep its promises:

Take the 8 key protections from SB 896 and amend them into SB 483. These provisions require the PUC to:

- (1) identify all costs, both short-term and long-term, of the transaction;
- (2) specify each promise, pledge, concession, or agreement made by the public utility or other entity;
- (3) identify any potential rate and service impacts that may occur as a result of the transaction; and
- (4) identify any and all benefits of the transaction.
- (5) the commission may conduct a public hearing on the transaction;
- (6) impose conditions that it deems necessary before granting approval of any transaction under this section;
- (7) promulgate rules to enforce deal—such rules shall include periodic reports by the public utility, holding company, or affiliate as necessary to determine whether the public utility, holding company, or affiliate has satisfied the requirements of this section and any requirements established by the commission in any order issued under this section.
- (8) Find that it is “in the public interest”

Three amendments we’d suggest adding:

- More approval options for the PUC besides changing the rate of return for the transmission company (which is only about 10% of the electric bill). Options might include: an up or down vote, modifying terms of the deal, setting conditions, performance targets or investment requirements, or other conditions that the commission may deem appropriate .
- a tougher standard for approval- such as a showing of “positive benefit” , which is the standard adopted in New Jersey
- a requirement to keep environmental promises- eg: 20% reductions, not building conventional coal plants, working for global warming emissions reductions

TXU claims we shouldn’t be able to change the rules mid-deal

- PURA is modified many times each session
- 46 states require pre-approval of mergers and acquisitions.
- The deal isn’t final until September – it’s hardly changing the rules before the deal is done.



Appendix A.

1. In April 2003, Goldman Sachs paid \$110 million to settle allegations the company engaged in conflicts of interest in the research it was providing to investors.ⁱ In January 2005, Goldman Sachs agreed to pay \$40 million for illegal practices surrounding IPOs.ⁱⁱ In September 2003, Goldman Sachs paid over \$9.3 million for trading in insider information on Treasury 30-year bonds.ⁱⁱⁱ In July 2004, Goldman Sachs was ordered to pay \$5 million as a penalty for corporate high yield bonds trading violations.^{iv} In May 2006, Goldman Sachs paid \$1.5 million to the SEC for manipulating municipal bond auctions^v and an additional \$140,000 to NASD.^{vi} In December 2002 Goldman paid \$1.65 million for failing to retain email communications as required by law.^{vii} Japan's Financial Services Agency issued a "business-improvement order" against Goldman Sachs Asset Management and barred it from managing investment-trust funds for improper stock-trading activities in December 2005.^{viii}
2. In June 2005, Citigroup agreed to pay \$2 billion to Enron shareholders over the sale of stock and bonds before Enron's bankruptcy.^{ix} In November 2004, Citigroup paid \$2.58 billion to settle a lawsuit brought by WorldCom shareholders over Citigroup's role in the collapse of that company.^x In April 2003, Citigroup agreed to pay \$400 million to settle federal and state charges that it lured investors into buying shares in companies known to be troubled.^{xi} In September 2002, Citigroup paid \$215 million to the Federal Trade Commission to settle charges that it manipulated consumers into buying overpriced mortgages and credit insurance.^{xii} In May 2005, Citigroup paid \$208 million to the SEC to settle charges that it denied investors mutual fund discounts and instead collected them as profit.^{xiii} In July 2003, Citigroup agreed to pay \$120 million to settle SEC allegations that it helped Enron and Dynegy commit fraud.^{xiv} A British regulator, the Financial Services Authority, forced Citigroup to pay \$25.4 million for illegal trades of Eurobonds.^{xv} In March 2005, Citigroup paid \$26.25 million to the SEC to settle charges that it failed to disclose conflicts of interest at the company.^{xvi} In May 2006, Citigroup paid \$1.5 million to the SEC for manipulating municipal bond auctions^{xvii} and an additional \$60,000 to NASD.^{xviii} In November 2001, the SEC cited Citigroup for violating federal securities laws by selling bonds illegally in the U.S.^{xix} In September 2004, Japan's Financial Services Agency ordered Citigroup to close its entire private banking operation because it had violated the country's financial rules after finding lax money-laundering controls and improper trading practices.^{xx} In June 2006, Korea fined Citigroup \$582,000 for irregularities in lending.^{xxi}
3. In November 2004 Lehman Bros paid \$222.5 million to investors over the company's participation in the sale of Enron notes shortly before the company went bankrupt.^{xxii} In April 2003, Lehman agreed to pay \$80 million to settle allegations of conflicts of interests in the research it provided to investors.^{xxiii} In August 2003, Lehman paid a \$2.5 million penalty for failing to adequately supervise a broker who stole millions from investors.^{xxiv} In May 2006, Lehman paid \$1.5 million to the SEC for manipulating municipal bond auctions.^{xxv} In May 2006, Lehman paid the New York Stock Exchange \$400,000 for submitting false information.^{xxvi} In February 2004, Lehman paid \$124,000 to settle charges that it defrauded mutual fund investors.^{xxvii}
4. In March 2004, Morgan Stanley paid \$857,000 to settle allegations the company manipulated energy markets.^{xxviii} In April 2003, Morgan Stanley paid \$125 million to settle allegations the company had conflicts of interest in providing research to investors.^{xxix} In January 2005, Morgan Stanley agreed to pay \$40 million to settle allegations of illegal practices surrounding IPOs.^{xxx} In November 2003, Morgan Stanley agreed to pay \$50 million to settle charges the company failed to provide customers important information relating to their purchases of mutual fund.^{xxxi} In December 2002 Morgan Stanley paid \$1.65 million for failing to retain email communications as required by law.^{xxxii} In August 2005, NASD fined Morgan Stanley \$6.1 million for violations of securities rules.^{xxxiii} In February 2006, Morgan Stanley agreed to pay \$15 million for failing to retain emails as part of an investigation by the SEC.^{xxxiv} In May 2006, Morgan Stanley paid \$1.5 million to the SEC for manipulating municipal bond auctions.^{xxxv} In May 2006, Morgan Stanley paid \$1.5 million to the SEC for manipulating municipal bond auctions.^{xxxvi}

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- ⁱ www.sec.gov/news/press/2003-54.htm
ⁱⁱ www.sec.gov/news/press/2005-10.htm
ⁱⁱⁱ www.sec.gov/news/press/2003-107.htm
^{iv} www.nasdaq.com/PressRoom/NewsReleases/2004NewsReleases/NASDW_010892
^v www.sec.gov/news/press/2006/2006-83.htm
^{vi} www.nasdaq.com/PressRoom/NewsReleases/2005NewsReleases/NASDW_014639
^{vii} www.sec.gov/news/press/2002-173.htm
^{viii} "Japan Post Bars Goldman Work on Future Funds," December 29, 2005, *The Wall Street Journal*.
^{ix} John Roper, "Citigroup agrees to \$2 billion Enron Settlement," *The Houston Chronicle*, June 10, 2005.
^x www.worldcomlitigation.com/courtbox/2004-11-10OrderApprovingCGSett&Fees.pdf
^{xi} www.sec.gov/news/press/2003-54.htm
^{xii} www.ftc.gov/opa/2002/09/associates.htm
^{xiii} www.sec.gov/news/press/2005-80.htm
^{xiv} www.sec.gov/news/press/2003-87.htm
^{xv} Heather Timmons, "Bond Trades Far Too Agile Cost Citigroup \$25 million," June 29, 2005, *The New York Times*.
^{xvi} www.sec.gov/news/press/2005-39.htm
^{xvii} www.sec.gov/news/press/2006/2006-83.htm
^{xviii} www.nasdaq.com/PressRoom/NewsReleases/2005NewsReleases/NASDW_014639
^{xix} www.sec.gov/news/press/2001-139.txt
^{xx} www.citigroup.com/citigroup/press/2004/040917a.htm
^{xxi} "Korea's FTC Fines Kookmin, Citibank Korea," *The Wall Street Journal*, June 7, 2006.
^{xxii} Mary Flood, "Lehman Bros. settles lawsuit," *The Houston Chronicle*, October 29, 2004.
^{xxiii} www.sec.gov/news/press/2003-54.htm
^{xxiv} www.sec.gov/news/press/2003-96.htm
^{xxv} www.sec.gov/news/press/2006/2006-83.htm
^{xxvi} www.nyse.com/press/1148314125304.html
^{xxvii} www.sec.gov/news/press/2004-17.htm
^{xxviii} www.ferc.gov/whats-new/comm-meet/030304/E-40.pdf
^{xxix} www.sec.gov/news/press/2003-54.htm
^{xxx} www.sec.gov/news/press/2005-10.htm
^{xxxi} www.sec.gov/news/press/2003-159.htm
^{xxxii} www.sec.gov/news/press/2002-173.htm
^{xxxiii} www.nasdaq.com/web/idcplg?IdcService=SS_GET_PAGE&ssDocName=NASDW_014804&ssSourceNodeId=5
^{xxxiv} www.sec.gov/news/press/2006/2006-69.htm
^{xxxv} www.sec.gov/news/press/2006/2006-83.htm
^{xxxvi} www.sec.gov/news/press/2006/2006-83.htm