

NO. CV-16-0401

PANDA POWER GENERATION	§	IN THE DISTRICT COURT
INFRASTRUCTURE FUND, LLC	§	
D/B/A PANDA POWER FUNDS;	§	
PANDA SHERMAN POWER HOLDINGS,	§	
LLC; PANDA SHERMAN POWER	§	
INTERMEDIATE HOLDINGS I, LLC;	§	
PANDA SHERMAN POWER	§	
INTERMEDIATE HOLDINGS II, LLC;	§	
PANDA SHERMAN POWER, LLC;	§	
PANDA TEMPLE POWER HOLDINGS,	§	
LLC; PANDA TEMPLE POWER	§	
INTERMEDIATE HOLDINGS I, LLC;	§	
PANDA TEMPLE POWER	§	
INTERMEDIATE HOLDINGS II, LLC;	§	
PANDA TEMPLE POWER, LLC;	§	
PANDA TEMPLE POWER II HOLDINGS,	§	GRAYSON COUNTY, TEXAS
LLC; PANDA TEMPLE POWER II	§	
INTERMEDIATE HOLDINGS I, LLC;	§	
PANDA TEMPLE POWER II	§	
INTERMEDIATE HOLDINGS II, LLC;	§	
and PANDA TEMPLE POWER II, LLC,	§	
	§	
	§	
Plaintiffs,	§	
	§	
V.	§	
	§	
ELECTRIC RELIABILITY COUNCIL	§	
OF TEXAS, INC.,	§	
	§	
Defendant.	§	15 <sup>th</sup> JUDICIAL DISTRICT

**PLAINTIFFS' FIRST AMENDED ORIGINAL PETITION AND JURY DEMAND**

Plaintiffs Panda Power Generation Infrastructure Fund, LLC d/b/a Panda Power Funds, Panda Sherman Power Holdings, LLC, Panda Sherman Power Intermediate Holdings I, LLC, Panda Sherman Power Intermediate Holdings II, LLC, Panda Sherman Power, LLC, Panda Temple Power Holdings, LLC, Panda Temple Power Intermediate Holdings I, LLC, Panda Temple Power Intermediate Holdings II, LLC, Panda Temple Power, LLC, Panda Temple Power

II Holdings, LLC, Panda Temple Power II Intermediate Holdings I, LLC, Panda Temple Power II Intermediate Holdings II, LLC, and Panda Temple Power II, LLC (collectively, “Plaintiffs”), demanding a jury, file this First Amended Original Petition against Defendant Electric Reliability Council of Texas, Inc. (“ERCOT”), Defendant.

**I.  
DISCOVERY LEVEL**

1. Plaintiffs plead that discovery should be conducted under Level Three in accordance with Rule 190.4 of the Texas Rules of Civil Procedure, considering the complexity of the issues presented.

**II.  
NATURE OF THE CASE**

2. This is a fraud, breach of duty, and negligent misrepresentation case. Defendant, either alone or in complicity with others, sponsored false and misleading market reports depicting capacity, demand, and reserves in the ERCOT region (these reports are also known as “CDRs”). Defendant intended the CDRs and similar misrepresentations concerning the ERCOT market to induce Plaintiffs to invest staggering sums of money toward electric power generation. Plaintiffs are investors and project companies who relied on Defendant’s representations to invest nearly \$2.2 billion to build three power plants. After the investments were irrevocably committed and after the power plants were under construction, Defendant admitted that its earlier representations were false, with devastating consequences to Plaintiffs. The earlier statements were made negligently or fraudulently and possibly to further expectations of special or personal interests. If not negligently or fraudulently made, Defendant negligently or fraudulently failed to disclose the falsity sooner than it did.

3. Defendant ERCOT is certified as an independent system operator (“ISO”) whose mandate includes ensuring the reliability and adequacy of the regional electric network. As an

ISO, ERCOT must function independently of political influence, or the influence of any particular producer or seller of electricity. To ensure this independence, ERCOT's Articles of Incorporation bind each of its directors to act as fiduciaries for ERCOT and its Members, producers and suppliers alike. Plaintiff Panda Power Funds ("Panda Power") is one such Member, and it manages the affairs of the other Plaintiffs in this case.

### **III. PARTIES**

4. Panda Power is a limited liability company. Panda Power acts as investment manager and ultimately oversees the construction of the power plants at issue in this lawsuit.

5. Panda Sherman Power Holdings, LLC ("Sherman Holdings") is a limited liability company that collected the equity investments used to help construct the power plant in Sherman, Texas at issue herein. Sherman Holdings is the sole parent of a series of holding companies that own the project company (the "Sherman Power Plant"). The assets of the Sherman Power Plant are pledged to secure millions of dollars of debt rated in reliance on the CDRs at issue in this case.

6. Panda Sherman Power Intermediate Holdings I, LLC is a limited liability company organized to act as an intermediated financing entity.

7. Panda Sherman Power Intermediate Holdings II, LLC is a limited liability company organized to act as an intermediate financing entity.

8. Panda Sherman Power, LLC, is the project company previously identified as the Sherman Power Plant. It is a limited liability company located in Sherman, Texas at 510 Progress Drive, Sherman, Texas 75092.

9. Panda Temple Power Holdings, LLC ("Temple Holdings I") is a limited liability company which collected the equity investments made to help construct one of two power plants

in Temple, Texas. Temple Holdings I is the sole parent of a series of holding companies that own the project company, (the “Temple I Power Plant”). The assets of the Temple I Power Plant are pledged to secure millions of dollars of debt rated in reliance on the CDRs at issue in this case.

10. Panda Temple Power Intermediate Holdings I, LLC is a limited liability company organized to act as an intermediate financing entity.

11. Panda Temple Power Intermediate Holdings II, LLC is a limited liability company organized to act as an intermediate financing entity.

12. Panda Temple Power, LLC is the project company previously identified as the Temple I Power Plant. It is a limited liability company located in Temple, Texas at 2892 Panda Drive, Temple, Texas 76501.

13. Panda Temple Power II Holdings, LLC (“Temple II Holdings”) is a limited liability company that collected the equity investments made to help construct a second power plant in Temple, Texas. Temple II Holdings is the sole parent of a series of holding companies that own the project company (the “Temple II Power Plant”). The assets of the Temple II Power Plant are pledged to secure millions of dollars of debt rated in reliance on the CDRs at issue in this case.

14. Panda Temple Power II Intermediate Holdings I, LLC is a limited liability company organized to act as an intermediate financing entity.

15. Panda Temple Power II Intermediate Holdings II, LLC is a limited liability company organized to act as an intermediate financing entity.

16. Panda Temple Power II, LLC is the project company earlier identified as Temple II Power Plant. It is a limited liability company located in Temple, Texas at 2892 Panda Drive, Temple, Texas 76501.

17. ERCOT is a non-profit corporation organized under the laws of the state of Texas. ERCOT may be served with citation by serving its registered agent H. B. Doggett at 7620 Metro Center Drive, Austin, Travis County, Texas 78744.

#### **IV. JURISDICTION AND VENUE**

18. The matter in controversy is within the subject matter jurisdiction of this Court. Plaintiffs seek damages in excess of \$1 million and such other relief as alleged in the Prayer herein.

19. A substantial part of the events or omissions giving rise to the claims herein arose in Grayson County, where one of the power plants at issue was financed and constructed in reliance on the misrepresentations at issue. Venue is proper in Grayson County as to those claims pursuant to TEXAS CIVIL PRACTICE AND REMEDIES CODE § 15.002(a)(1). The other plants were constructed in Bell County, but they were constructed in reliance on the same or similarly flawed CDRs. The decisions to invest by the holding companies were made by the same group of people for all plants. The rating agencies and consultants who relied on the misrepresentations are the same for all plants. There are questions of law and fact common to all Plaintiffs, including but not limited to the degree of care exercised by the Defendant in publishing the CDRs, the scienter of the Defendant, actual reliance by those investing in the projects, and whether the reliance was justified. Therefore all claims as to all Plaintiffs are properly joined under Rule 40, TEX. R. CIV. P.

## V. BACKGROUND

### A. The Transformation of the Electric Power Transmission Industry

20. In 1992 the Federal Energy Policy Act (the “Act”) was passed and this Act fundamentally changed how the electric transmission system was owned and operated. Before then, electric utilities were mostly vertically integrated. This meant that one company or family of companies bundled power generation, transmission, and distribution. Regional monopolies dominated the energy market.

21. The Federal Energy Regulatory Commission (“FERC”) wanted vertically integrated electric utilities to unbundle to promote competition in the industry. In FERC Order No. 888, FERC required all jurisdictional public utilities to unbundle.

22. While unbundling promoted competition, it also posed practical challenges. For example, the public utility monopolist was better able to keep supply and demand in balance because it was both the power generator and the power seller. Thus, the monopolist had access to vitally important market data concerning supply and demand that enabled the monopolist to gauge when to add power generation capacity. Under the new regime, there was still a need to share vital, confidential market information and projections, but this had to be accomplished without collusion between competitors.

23. To address these inefficiencies or challenges a new market entity emerged: the independent system operator or ISO.

24. While FERC Order No. 888 did not require utilities to participate in ISOs, it encouraged ISO formation as a means to effectively unbundle power generation and distribution.

25. An ISO is an organization that coordinates, controls, and monitors operation of an electric power system. ISOs are not governmental entities. ISOs perform a number of functions,

some of which require them to collect confidential data from market participants. Generally speaking, ISOs then assimilate, model, and compile market data and projections into aggregated summaries that can be shared with market participant for their use. Those market participants who are power generators or who wish to become power generators rely on the reports, projections, and assessments of market capacity in deciding whether to enter a market or enlarge their presence in a market—or to perhaps exit the market or mothball a plant. When preparing these reports, ISOs must act independently from special interests. Nor can ISOs produce reports that favor one market participant or lobby group over another.

26. Since these reports dramatically influence supply, an ISO that negligently or purposely supplies false data for market participant purposes can defeat the purpose of the free market and in the process artificially affect price, injure market participants, and ultimately destroy the competitive market. An ISO has a fiduciary duty to the market participants who supply it with confidential information to act competently and independently when using and publishing aggregated market information. To act otherwise would have the same effect on the power market as the monopolist who uses its power to manipulate the market by decreasing supply to artificially increase price or increasing supply to artificially deter entrants from the market so that it may raise prices later.

#### **B. The Market Entry Of ERCOT As An ISO**

27. In 1999, the Texas legislature enacted PURA Chapter 39 to restructure the electric utility industry in Texas and unbundle power generation and power transmission.

28. The legislature declared that each power region in Texas form an “independent organization,” or ISO, to perform the following functions:

- a) ensure access to the transmission and distribution systems for all buyers and sellers of electricity on nondiscriminatory terms;

- b) ensure the reliability and adequacy of the regional electrical network;
- c) ensure that information relating to a customer's choice of retail electric provider is conveyed in a timely manner to the persons who need that information; and
- d) ensure that electricity production and delivery are accurately accounted for among the generators and wholesale buyers and sellers in the region.

29. The Texas legislature required that the ISO had to be independent of any undue influence by power suppliers or buyers.

30. ERCOT, sometimes called the ERCOT ISO, is very unique because it is not subject to FERC oversight. FERC's current position not to assert jurisdiction over ERCOT is somewhat controversial and is justified on the basis that ERCOT is engaged solely in the intrastate transmission of energy. Instead of FERC, ERCOT is subject to the supervision by the PUCT. The chairman of the PUCT is *ex officio* a member of the ERCOT board of directors. Commissioners of the PUCT are political appointees. No representative of FERC sits on the board of any ISOs under its jurisdiction. The remaining board members of ERCOT are culled from segments of the industry and those the industry serves in an effort to achieve balance and avoid undue influence by any one group.

31. Though subject to PUCT supervision, ERCOT is not a governmental entity, and the directors of ERCOT acting in their capacity as directors expressly owe fiduciary duties to the Members of ERCOT.

### **C. The False and Misleading CDRs**

32. ERCOT's report on the Capacity, Demand and Reserves (the "CDR") is the cornerstone of investment decisions made by those wishing to invest or construct power plants in the ERCOT region. The CDR represents the expert assessment by ERCOT of power capacity



and the demands for power in the region. It also identifies the reserve margin that the PUCT says is essential to guarantee the reliability of power delivery to consumers in times of extreme demand. The reserve margin is not mandatory. It is a target reserve margin that signals when investors should build generation. If ERCOT were to artificially set the reserve margin too high or to artificially manipulate projected capacity and demand to levels below the target reserve margin, ERCOT could stimulate investment even though not actually supported by the market. The CDR is expressly provided for market participant purposes. It is reviewed, compiled, and analyzed by ERCOT, and it is compiled from confidential data separately supplied by market participants that only ERCOT possesses in full.

33. In 2006 and 2008, ERCOT experienced extraordinary demands for power. Beginning in 2010, ERCOT wanted to encourage private enterprise to invest and build more power plants to protect against power shortages in the future. Then, in the summer of 2011, the demands for power became so great that the region experienced power shortages and came dangerously close to rolling blackouts. Something had to be done to remedy the situation.

34. The problem confronting ERCOT was how to encourage investment without capacity pricing.

35. Capacity pricing is one method to assure resource adequacy. Many of the ISOs subject to FERC regulation allow for what is known as capacity pricing—a sum charged for power on top of the energy market price to ensure that power generators have sufficient incentive to construct plants that may only be used or mostly used during periods of extreme or peak demand. In a capacity market, investors analyze the capacity payments to determine whether an investment is a sound decision.

36. ERCOT does not administer a capacity market and instead relies solely on the energy market price for energy set by the market to furnish sufficient incentives to construct new power plants. Thus in an energy-only market like ERCOT, the CDRs or similar reports form the basis of investment analysis and drive the investment.

37. Depicting capacity in the CDR in excess of the target reserve margin obviously discourages investment. Conversely, depicting capacity less than the target reserve margin encourages investment. This is because investors can expect higher prices for power when there is scarcity of supply, and the higher price will cover the enormous cost of plant construction and development.

38. In November 2010, ERCOT took its first step to condition the market by increasing its target reserve margin from 12.5% to was 13.75%.

39. In late 2011, ERCOT took its next major step to spur investment. In its 2011 CDR, ERCOT for the first time projected serious and long-term scarcity of power supply. This description of the market continued in the 2012 CDR.

40. These CDRs depicted extreme capacity shortfalls in power capacity well below the target of 13.75%. The CDRs created the picture of an energy market that ERCOT knew would lure investors to construct plants because investors would believe that the price for power in such short supply would be high enough to cover the cost of construction without any need for a capacity payment.

41. In furtherance of ERCOT's plan to spur investment, ERCOT's Warren Lasher (Director of System Planning) addressed the Gulf Coast Power Association on or about May 4, 2012. At the presentation, Mr. Lasher confirmed the December 2011 CDR results. Mr. Lasher and ERCOT emphasized without qualification that "Current information indicates long-term

reserves are expected to fall well below the target reserve margin.” The purpose of this statement was to signal to the market that now was the time to invest.

42. All these representations had the intended effect. Rating agencies such as S&P relied on the representations to give favorable ratings on debt supporting construction of new power plants. Plaintiffs, their investors, and their experts looked to the CDRs as the benchmark for investment and planning decisions—and committed to building the new plants.

43. Based on the representations, Plaintiffs made investments they believed were critical for reliable power generation for Texas. But for Defendant’s representations, Plaintiffs would not have invested in or built the power plants.

44. ERCOT specifically intended to induce investments, and ERCOT assured Plaintiffs their investment was safe.

a) On or about November 8, 2012, at the Groundbreaking Ceremony for the Sherman Power Plant in Sherman, Texas, then PUCT Commissioner Rolando Pablos expressed to all present the following sentiments: “This is a very important day for Texas, for North Texas, for ERCOT. This project is very important. The plant is going to help our grid. We have strains on our infrastructure. The challenge right now is our tremendous growth is outpacing our ability to generate and deliver electricity. Thank Panda Power for stepping up. Your investment is safe in Texas.”

b) On or about January 30, 2013, a few months before the financial closing on the second Temple power plant, executives of Panda Power and certain investors in the power plants at issue met with John Dumas (ERCOT director of wholesale market operations) and Mr. Lasher to hear first-hand confirmation of under-capacity in the

region. After being reassured concerning the need for power generation, Panda Power closed on the second Temple power plant.

45. Then, things began to change.

46. In 2013, the target reserve margin and formula for the CDR was elevated to “protocol” status subject to PUCT review.

47. Then, and only after the investments closed and the plants were substantially under construction, ERCOT published new CDRs using different data and a different methodology, one depicting a far different energy market. The ERCOT market changed overnight. What was once a market showing extreme scarcity of supply became a different market of extreme over capacity.

48. Information slowly surfaced showing that ERCOT’s methodology and data points used in the 2011 and 2012 CDRs were either seriously flawed or rigged. Questions began to surface as to whether ERCOT knew about the defective forecasting but suppressed this fact to induce construction of plants without capacity payments. Questions arose concerning ERCOT’s competency and independence, and whether the science underlying the CDRs was so unsound as to be wholly unreliable.

49. In the 2011 and 2012 CDRs, ERCOT took great care on its website to disclaim any responsibility for the accuracy of the data supplied by market participants upon which the CDRs were based. But nowhere did ERCOT disclose doubts about its own methodology. Nowhere did ERCOT warn market participants that its science was unsound, or that it lacked the competence or independence to produce reliable assessments of capacity, demand, or reserves.

50. The new market reflected by the new CDRs created the perfect storm. The predictions of over capacity depressed the market price for power both in the short and long

term, making it more difficult to hedge against temporary market distortions through selling power in the forward markets.

## **VI. CAUSES OF ACTION**

### **A. Negligent Misrepresentation**

51. The foregoing allegations are incorporated by reference.

52. Defendant made or caused to be made representations in the course of their business or profession that supplied false information for the guidance of Plaintiffs in their business

53. Defendant did not exercise reasonable care or competence in obtaining or communicating the information

54. Plaintiffs justifiably relied on the information and suffered substantial damages.

### **B. Fraud**

55. The foregoing allegations are incorporated by reference.

56. Defendant knowingly or recklessly made or caused to be made false representations to induce Plaintiffs to invest and construct power plants in Sherman and Temple, Texas.

57. Plaintiffs have suffered substantial damages in reliance on the false representations.

### **C. Breach Of Duty**

58. ERCOT owed a fiduciary duty to Plaintiffs to act independently and competently in the performance of its responsibilities as an ISO.

59. A formal fiduciary relationship arose by virtue of the statutory and common law duties owed by ERCOT to members and market participants.

60. Moreover, an informal fiduciary duty arose under the facts of this investment.

61. Defendant possessed confidential market information that only it had. While other market participants might have access to bits and pieces of the market data, ERCOT, by virtue of its position as an ISO, was the only market entity with a complete, unobstructed view into the ERCOT market.

62. ERCOT knew that Plaintiffs were relying on ERCOT's superior knowledge in making their investment.

63. Defendant breached its fiduciary duty, causing Plaintiffs substantial damages.

**VII.  
JURY DEMAND**

64. Plaintiffs hereby request a trial by jury pursuant to Tex. R. Civ. P. 216(a).

**VIII.  
REQUEST OF DISCLOSURE**

65. Under Texas Rule of Civil Procedure 194, Plaintiffs request that Defendant disclose, within 50 days of service of this request, the information or material described in Rule 194.2.

**IX.  
PRAYER**

WHEREFORE, Plaintiffs request that, upon final hearing of this case, that they have and recover, from Defendant, the relief requested herein as well as pre-judgment interest, post-judgment interest, actual damages, consequential and incidental damages, costs of court, attorneys' fees and such other and further relief to which Plaintiffs may show themselves entitled, both at law and in equity.

Respectfully submitted,

/s/ Werner A. Powers

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