Carr, Riggs & Ingram, LLC
111 Veterans Boulevard
Suite 350
Metairie, LA 70005

504.837.9116
504.837.0123 (fax)
CRIcpa.com

Executive Summary

Purpose

Carr, Riggs & Ingram ("CRI") was engaged to provide forensic services to the City of Brownsville ("COB"), investigating the activities of the Brownsville Public Utilities Board ("BPUB") leading up to and occurring subsequently to the execution of an agreement with Tenaska to build and operate a gas-fired electric generating station (the "Project"), and a related gas pipeline (the "Pipeline"). We performed this engagement in accordance with the Statement on Standards for Forensic Services as promulgated by the American Institute of CPAs ("AICPA"). Our work did not constitute an audit in accordance with generally accepted auditing standards, an examination of internal controls, or any other attestation or review service in accordance with standards established by the AICPA.

Objectives

The objectives of our forensic engagement were to:

1. Ascertain whether there were any improper activities conducted in furtherance of the Project.
2. Provide an accounting of all funds set aside for and expended in connection with the Project.
3. Evaluate the propriety, nature, and timing of expenditures made in furtherance of the Project and the accumulation of costs consisting of recorded construction-in-progress asset(s).
4. Determine the amount and disposition of any funds raised or collected in furtherance of the Project.
5. Document the justification of the Project and evaluate its reasonableness.
6. Ascertain that all activities and transactions were initiated under either specific or general approval.
7. Provide Brownsville, through its City Attorney, a final report identifying whether any irregularities or illegal acts were detected in connection with all transactions identified in the scope of services. The report shall detail evidence, if any, of illegal or irregular acts.

Background

Throughout the report, CRI references either BPUB as a whole, the BPUB board of directors (the "Board"), and BPUB management ("Management"). When referring to Management, the key personnel throughout the scope of the investigation included:

1. John Bruciak("Mr. Bruciak"), CEO/GM
2. Fernando Saenz, COO/Assistant GM
3. Leandro Garcia, CFO
4. Marilyn Gilbert "Ms. Gilbert"), former Energy Risk Manager and former Director of Energy Services.[1]

The Board comprises seven members, six of whom are appointed by the City Commission for four-year terms. COB's mayor serves as the seventh ex-officio member[2].

[1] Ms. Gilbert left BPUB in 2014 and returned in 2022, serving in the capacity of Assistant GM/COO.
[2] An ex-officio member is not appointed' rather he has a seat on the board as a result of a position that he holds. In this case, the mayor has a seat based on his position as current mayor of Brownsville...

Tenaska proposed the Project to the Board in late 2011. In December 2012, the COB approved a series of electric rate[3] increases to fund both the Project and BPUB operations and maintenance ("O&M") costs. The finalized agreements (the "Definitive Agreements") were executed January 25, 2013. The Tenaska Brownsville Generation Station ("TBGS") would have generated up to 800 Megawatts ("MW") of electricity, of which BPUB would own 25 percent, or 200 MW. BPUB also planned to build a natural gas pipeline[4] to supply fuel to the TBGS. The initial commercial operation date ("COD") was expected to be June 2016.

Tenaska was responsible for subscribing[5] the remaining capacity of the TBGS. BPUB was responsible for certain development expenses, which required hiring outside engineering firms, attorneys, and consultants. Tenaska's inability to subscribe the remaining capacity was the ultimate reason for the Project's failure.

On November 1, 2021, CRI was engaged by COB to conduct a forensic analysis of the events leading up to and subsequent to the formation of the project.

Project Origins

As part of its planning cycle, BPUB engaged engineering firm R.W. Beck in 2008 to conduct a 20-year load forecast (the "Beck Forecast" or the "Forecast").[6] The Beck Forecast projected growth in system energy requirements and annual peak demand for the years 2009 through 2028; the annual peak demand would grow to 405MW by 2018. The Forecast also noted that the economic data used in the forecast after 2007 was projected, i.e. historical data used in the study was from 2007. It further noted that the most recent years of data were also subject to substantial revision. Because of this, the Beck Forecast recommended that the Forecast be updated periodically and cautioned that "plans for large capital expenditures, which are based on such forecast" be made with care and an allowance for flexibility.

In 2011, BPUB engaged professional engineering firm Black and Veatch ("B&V") to develop an Integrated Resource Plan ("IRP") and to write a Power Supply Request for Proposal ("RFP"). The IRP would make recommendations on future generation expansion plans and the Power Supply RFP would be used to evaluate proposals for from power providers. At BPUB's direction, the IRP utilized the Beck Forecast to project capacity needs with the addition of a 13.75% reserve margin.[7] A draft of the IRP, which identified key issues and recommendations, was completed in December.

At a special Board meeting in December 2011, BPUB discussed the key issues in the IRP and the presentation made by Tenaska earlier that month. Management emphasized imminent capacity shortages identified in the IRP as part of the presentation given before the Board. The Board also discussed expanding the IRP's scope to include an evaluation of the Project against alternative expansion options.[8]

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[3] The first increase took place April 1, 2013, and the final rate increase went into effect October 1, 2016.
[4] COB also approved an ordinance to establish a natural gas utility in 2012. In addition to supplying fuel to the Project, the Pipeline would eventually allow BPUB to provide natural gas to customers.
[5] Subscribing the plant means finding utility providers to commit to the purchase of a specific amount of electric generations under a long-term agreement.
[6] Load forecasts provide information on projected energy demand for a utility system.
[7] The reserve margin increased the projected electric generation need in order to have additional electricity available in the event of excessive demand, e.g., a heat wave that caused excessive power demands in order to cool homes and businesses.
[8] The final draft reflected revisions and additions based on BPUB requests to add four other alternatives for evaluation: Inlet Fogging of Silas Ray Unit 6/9, the Tenaska Alternative, and the Transmission Alternative.

Findings on Project Origins

The Beck Forecast projected steady growth rates that were higher than historical rates. The Forecast also noted that drivers of the forecast could deviate and recommended that the forecast be updated periodically, especially when projections of driving variables change. The Beck Forecast, produced at BPUB's request and expense, provided the means to compare the monthly forecast to the actual capacity demand over time and make forward-looking adjustments. BPUB elected not to perform these comparisons, and instead requested that the Beck Forecast be used without updates to complete the 2011 IRP.

The use of the original Forecast projections meant that Management intentionally ignored four years' worth of data in favor of outdated projections. B&V acknowledged that the Beck Forecast was potentially overstated due to changes in the economy and recommended an update. In addition to the energy demand projected by Beck, the 2011 IRP also added a reserve margin, which increased the projected capacity shortage. In interviews, Mr. Bruciak and Ms. Gilbert stated that the reserve margin was a requirement from ERCOT. Communication from ERCOT indicated that the Bruciak/Gilbert statements were false, and subsequent BPUB IRPs did not include a reserve margin.

Other issues noted include the following:

- Gas prices were projected to double by 2035, while natural gas supply in South Texas was projected to triple between 2012 and 2035. The simultaneous occurrence of these two events is contrary to the law of supply and demand.
- On and off peak prices for spot market purchases were predicted to increase by $100 over a 20-year period. This growth rate was substantially reduced in later IRPs.
- The IRP model did not appear to take into account the additional transmission capacity that ERCOT endorsed in January 2012 and Management was aware of months prior.

The IRP ranked various alternative project scenarios based on the cumulative costs.[9] The advantage of the two of the alternative scenarios was the ability to halt plans if variables such as gas prices and capacities differed from their assumed levels that drove the 2009 IRP projections. The price of gas was cited as one reason that Tenaska was unable to subscribe the remaining Capacity.

B&V was also contracted to conduct a power supply RFP and evaluate incoming proposals. A presentation prepared by B&V stated that the Tenaska Project looked good on the surface, but recommended comparing it to potential bids and further recommended a two-year action plan to address immediate needs. This presentation was not made to or shared with the Board, and Management's version favored the Project.

Management presentations appeared to downplay the risks of the Project and highlight the potential benefits. The Board voted to pursue the Project with Tenaska without soliciting alternative proposals. CRI concluded that Management's control over the narrative presented to the Board and COB directly influenced this decision.

B&V also completed a technical assessment[10] of the Project that concluded, among other things, that a lack of subscribers could cause the project to fail. Presentations made before the Board did not include this warning. We noted that the assessment was completed and presented after B&V was selected as a

[9] See footnote 8.

[10] The report assessed whether the costs and specifications were reasonable and the Project had potential to develop. The Report was not intended to evaluate the merits of building the Project.

consultant on the development of the Project. When the results were presented to the Board, B&V had been selected as power consultant and had an interest in the project moving forward.

With regard to the origins of the Project, we concluded that the IRP did not determine capacity needed, did not perform any analysis to determine if that forecast was still valid, and did not examine the underlying drivers of the forecast and compare to actual results over prior three years. Instead, at BPUB Management's direction, B&V used the Peak Demand from the 2009 Beck Forecast without changes and added a 13.75% reserve capacity margin. The resulting forecasted shortage was used by Management to demonstrate the need and push the Project forward.

We believe that the overemphasis of a capacity shortage that was artificially inflated was a key driver in the Board and COB approving this Project. When one considers the magnitude of the capital investment, it would have been prudent to make sure that all data sets and inputs are up to date and accurate and that the process to seek competitive proposals was performed. Yet, BPUB did not take advantage of its ability to review the Beck forecast on a monthly basis nor did it allow its independent engineer, B&V, to validate the accuracy of a key input to the IRP. Further, given the level of interference and manipulation of the narrative and the overall process, it is our opinion that Management intentionally misrepresented or omitted key information in order to ensure that the Project (and its related rate hikes) would be approved by the Board and ultimately the COB.

Project Events after January 2013

The contracts[11] for the project were executed January 25, 2013. Shortly thereafter, the Project was announced to the public. In order for the project to be built Tenaska needed to obtain commitments for the remaining 600MW of TGBS capacity, but were consistently unsuccessful. BPUB granted a number of extensions to allow Tenaska to market the plant.

The Board received almost monthly updates on the Project, including expected completion date, status of engineering studies, and updates on the Right of Way ("ROW") acquisition for the pipeline. There were multiple instances of either the Board, consultants, or City Commissioners questioning the Project delays, Project costs, and Project-related rate increases. Tenaska representatives, Management, the power consultant, and the mayor all recommended patience and regularly responded that the Project was "almost there." In exchange for BPUB's patience, Tenaska negotiated additional development reimbursements, the majority of which would only go into effect upon construction.

The majority of BPUB's expenses were related to legal and professional engineering services. BPUB also contracted with two companies to serve as power consultants, B&V and The Yzaguirre Group. The Yzaguirre group consultant was Max Yzaguirre ("Mr. Yzaguirre"), a former Enron executive with knowledge of the ERCOT market. B&V's contract, like most other professional services agreements, included a maximum contract price and required B&V to submit time records. Mr. Yzaguirre, on the other hand, was paid a monthly fee of $35,000 and was not required to keep time records. CRI concluded that this pay structure incentivized Mr. Yzaguirre to further the Project and avoid making any recommendation to terminate it, even if he believed it was no longer in COB's best interest.

When negotiations in the ERCOT market stalled, Tenaska set its sights on marketing the remaining power to Mexico. As part of an extension agreement, Tenaska began reimbursing BPUB for Mr. Yzaguirre's fees. In turn, Mr. Yzaguirre made an agreement with Tenaska to assist with its negotiations in Mexico. CRI

[11] The "contract" was a set of 11 Definitive Agreements.

concluded that Mr. Yzaguirre working on behalf of Tenaska while simultaneously under contract with BPUB as its strategic advisor and "independent set of eyes and ears" was a conflict of interest.

BPUB and COB held multiple joint sessions throughout the timeline of the project. CRI focused on two meetings in particular: November 17, 2015 and April 24, 2017. The November session was called to request that BPUB provide explanation as to why the rate increases were originally needed and why they were still necessary. Management's internal communication indicated that they met with individual city commissioners months prior to review and defend rate increases. This contradicted a statement made by Mr. Bruciak that he never met with city commissioners individually before meetings. Moreover, these activities may have skirted open meeting requirements.

CRI found that during the November 2015 session, BPUB intentionally presented outdated capacity projections and included the aforementioned reserve margin. It also overestimated peak demand in 2015, even though the peak demand had already passed.[12] The projected peak demand, with additional reserve margin, was nearly 100MW above actual data.[13] BPUB also presented an unrealistic 2018 COD to the Commission, despite knowing that the project was on indefinite hold due to the lack of subscribers.

In April 2017, COB again called upon BPUB to explain the status of the project. BPUB admitted that the project was on hold due to ERCOT market conditions but that it was actively marketing the project in Mexico. Commissioners expressed that they wanted to terminate the Agreements. Management recommended that COB wait for the results of the next IRP, which were to be released the following month, before making a decision. Management did not reveal that Mr. Yzaguirre's agreement had been terminated,[14] that Tenaska stated in a meeting that it did not feel the project was the best economic decision, and that Tenaska felt it owed BPUB nothing in terms of reimbursements. Both Mr. Bruciak and Mayor Tony Martinez had been present at the meeting with Tenaska in March, but neither communicated this to COB. The preliminary results of the 2017 IRP were also known to Management at the time of the April session but not disclosed to the Board or the Commission.

B&V was engaged to produce the 2017 IRP and completed it on May 1, 2017. Notably, projected capacity needs were much smaller than those included in the 2011 IRP, and the reserve margin was no longer included. Because B&V completed the load forecast within one year of the 2017 IRP, the data reflected was likely more current. The 2017 IRP ranked the Project last out of the four scenarios considered for power expansion, noting that the Project was the least economical of the four, also noting that Tenaska indicated it was not building the plant. However, the presentation on the IRP results given before the Board[15] only one week later stated that the TBGS was the best choice given current market conditions, ranking it the lowest CPWC. The same presentation was made to the COB on July 11, 2017, where Management and B&V misrepresented that the Tenaska Project was still the best and most efficient option.

As discussed in more detail in the Conflicts of Interest Section, this change in ranking was a direct result of Management's collusion with Tenaska, with the cooperation of B&V, to manipulate the outcome of the upcoming meeting with the Board and the Commission in what appears to be an attempt to mislead both governing bodies in order to keep the Project from being terminated.

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[12] In South Texas, peak demand is typically in the summer, as residents and business use more power to cool their homes and businesses. A presentation in November would have already had the actual data on peak demand.

[13] Peak demand in 2015 was 286MW. Management projected peak demand to be 334 MW or 380 MW with additional reserve margin, while still insisting the need was imminent.

[14] Because Mr. Yzaguirre was working with Tenaska on negotiations in Mexico, his termination indicated that negotiations in Mexico were not successful.

[15] The same ranking was also presented to COB in the August 2017 joint session.

Furthermore, while B&V may not have directed the changes, their participation is without question, especially given that the IRP PowerPoint, which was incorporated on their B&V PowerPoint template, was presented by B&V employee Craig Brown. However, B&V did not actually change the IRP, just the presentation.

Given the above, it is our opinion that the Presentation to the Joint Meeting of the Board and Commission held on July 11, 2017, reflected the product of intentional misrepresentations carried out with collusion between Management, Tenaska, and B&V.

The Board voted in December 2017 to terminate the extension agreement that allowed Tenaska an unlimited amount of time to market the plant. The new deadline to have financing in place was February 2019 and in order to do that, the plant had to be fully subscribed. BPUB knew this was an unlikely occurrence and ending the extension meant ending the project. Tenaska sent a notice that it was terminating the first agreement February 8, 2019. BPUB terminated the final Agreement in February 2020. COB and the public were formally notified of the terminated agreements in August 2020.

Conflicts of Interest

CRI found that Tenaska had undue influence on BPUB studies that furthered the Project, specifically its ability to manipulate the conclusions of the 2017 IRP presentation. BPUB has a decade's long relationship with Tenaska through Tenaska's energy services. Thus, when BPUB determined that it might be interested in partnering with a company to build a generation, they reached out through their connection at Tenaska Power Services instead of issuing an RFP as recommended in the 2011 IRP.

Management claims that they were unfamiliar with consultant Mr. Yzaguirre, and that he was recommended by Board members when Management provided a short list of potential firms. B&V was the firm Management recommended but the Board wanted both consultants and felt the size of the Project could accommodate both. We noted that Mr. Yzaguirre had an incentive to continue the Project as long as his pay structure was set up as a fixed monthly fee with an unlimited budget. Mr. Yzaguirre was directly involved in negotiations of extensions. It was not to his advantage to offer any guidance that the Project may not be successful. Further, once Mr. Yzaguirre became a Tenaska associate assisting with negotiations in Mexico, he had an obligation to Tenaska that directly conflicted with his obligations to BPUB.

B&V benefitted from a longstanding relationship with BPUB and was frequently on the shortlist of firms for professional service contracts. B&V was engaged to draft numerous studies and reports that would serve as the reported catalyst for the Project; make recommendations on the feasibility of the Project and whether BPUB should proceed; and serve as one of the power consultants. B&V also had a contract with a Tenaska affiliate to participate in the TBGS construction as well as participation in another Tenaska project.

Other Observations

Rate Increases

In April 2016, BPUB initiated a rate stabilization program to help lower customer bills by artificially reducing fuel purchase energy charges ("FPEC") to rates not seen in the previous ten years. The program was frequently cited by BPUB as a reason to keep the rate increases in place. BPUB had more control over the fuel stabilization program and could determine at any time that it was no longer fundable.[16]

BPUB also cited contractual obligations between 2015 and 2017 as reasons to keep the rate increases in place. Specifically, BPUB claimed that it could be penalized if it did not have the funding in place when Tenaska was ready to close on the Project. CRI concluded that this was a manipulation, as BPUB had not only accumulated surplus funds due to the delay in construction, but also that Tenaska had never shown progress in subscribing the plant. The likelihood that BPUB would be called on its obligation was low. COB could have also chosen to defer the rate increases until the Project was more certain.

Keeping the rate increase intact would have given BPUB flexibility in the use of funds. The rate stabilization fund was not codified and BPUB could, at any time, determine that it could no longer fund the program. BPUB's prediction of ending the program should the Commission reduce rates was realized when the COB voted to rescind the Tenaska related increases.

Management always highlighted the city transfer during discussions about rescinding or deferring rate increases, specifically cautioning Commissioners to consider the potential adverse impact on COB's budget if utility rates were lowered. Commissioners have confirmed that the city transfers are an important consideration. In addition to city transfer, BPUB drafted at least one memo proposing that it would assist with a COB capital project conditional on COB allowing the rate increases to proceed.

It is our opinion that, in an effort to hold on to a codified rate increase, BPUB concocted a plan to mask the increased energy charges on customer utility bills. BPUB artificially lowered the FPEC charge to an unrealistic figure then used it as a cudgel to keep the COB from rescinding rate increases.

It is also noteworthy that none of the revenue raised from the O&M portion of the rate increases was ever used for O&M. All of the revenue went to the Project, the equity fund, or the rate-stabilization program.

ROW Acquisition

BPUB delayed notifying the COB and the public about the status of the Project and its termination of the last Agreement in order to protect condemnation[17] proceedings. The justification given was that if holdouts learned that the principal reason for the pipeline no longer existed, they could contest condemnation on grounds that there was no longer a public purpose.

Management has defended the ROW acquisition, stating that it still had value even though the pipeline was no longer to be built. CRI determined through its review of internal communications that it was clear as early as mid-2015 that the project was unlikely to move forward and known by March 2017 that the TBGS would not be built. It appears that Management, Mayor Martinez, and others knowingly continued ROW acquisition under false pretenses.

Disposition of Funds

CRI was asked to review the disposition of funds associated with the Project, evaluate the propriety of expenditures, and quantify the amount invested in the Project. CRI found no evidence of fraud associated

[16] CRI also noted that the fuel subaccount had been funded in years before the Project rate increases, presumably from surplus funds.

[17] Condemnation is the acquisition of private property to serve a public purpose. If a property owner does not voluntarily accept an offer for the property, the matter can be taken up in court.

with payments to vendors and noted that with very few exceptions, documentation was provided and in line with BPUB procedures.

BPUB expended approximately $30.9 Million, the majority of which was for legal and professional engineering services. BPUP wrote off approximately $9.3 Million in Project related expenses and set aside $29 million in its Tenaska equity fund.

Conclusion

The pursuit of the Project was driven by a contrived capacity shortage described in the 2011 IRP, which was manufactured by Management through the addition of a reserve margin and the intentional use of an outdated and overstated load forecast. Subsequent presentations made before the Board and COB did not accurately reflect studies and were biased toward the Project or omitted pertinent facts. Given that the Board and City Commissioners are not energy experts, they were reliant on Management to aid their decision-making with regard to the Project.

Further, given the interference and manipulation of the narrative, it is our opinion that Management, with the participation of Mayor Martinez, intentionally misrepresented or omitted key information in order to ensure that the Project (and its related rate hikes) would be approved by the Board and the COB.

After the Project was initiated, BPUB agreed to multiple extensions even though Tenaska had failed to subscribe the plant capacity with even one energy provider besides BPUB. Presentations made by Management to COB did not accurately reflect the reality of the Project status. Because of this, Management was able to defend rate increases that were no longer necessary for a Project that would not be built.

Compounding the issue of Management's influence was that consultants, who were supposed to be independent and objective advisors, were heavily influenced by Management and/or had conflicts of interest that aligned them with Tenaska. CRI found that Mr. Yzaguirre benefitted from the continuance of the Project, and that B&V had a contract to work with Tenaska after the Project was constructed. The Board was not provided impartial guidance that would have permitted it to make informed decisions.

The Board had the ability to read the full reports upon which Management based its presentations. The Board also had the ability to terminate the extension agreements even if Management recommended patience. Given the amount of investment required, the Board should have been more skeptical and asked questions. While we did not find evidence that it intentionally misled COB, the Board was aware of the Project's impending demise in December 2017 when it voted to end the contract extensions. It failed to notify the Commission and the public until August 2020. Records indicated that delaying notification was at least in part to protect ROW proceedings.

We appreciate this opportunity to serve you.

Carr, Riggs & Ingram, L.L.C