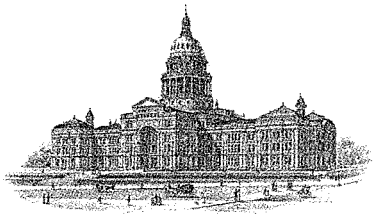
The Senate of The State of Texas



TROY FRASER

PREPARED STATEMENT OF
TROY FRASER
TEXAS STATE SENATOR

Pedernales Electric Cooperative

Before the House Committee on Oversight & Government Reform
June 26, 2008

Mr. Chairman, Members of the Committee, I would like to thank you for this opportunity to brief you on Pedernales Electric Cooperative.

I currently serve as Chairman of the Texas Senate Committee on Business and Commerce and have oversight of the electric industry. I am also a member of Pedernales Electric Cooperative.

I want to emphasize that I have been and continue to be a strong supporter of rural electric cooperatives. These cooperatives brought electricity to many parts of Texas and the nation that no other company wanted to serve.

The beauty of the electric cooperative system is that cooperatives are designed so that the member-owners can determine how best to run the system through the

P.O. Box 12068 ★ Austin, Texas 78711 ★ (512) 463-0124 ★ Dial 711 For Relay Calls

election of a board of directors. If members do not like the policies set by the board of directors, they can and should vote them out of office.

Prior to 1995, the Public Utility Commission of Texas had general supervisory authority and rate setting authority over electric cooperatives even though these entities were democratically controlled.

In 1995, the Texas Legislature allowed cooperatives to opt out of retail rate regulation by a majority vote of its members and the vast majority of the 66 distribution cooperatives did just that. In 1999, the Legislature deregulated cooperatives as to rates, general PUC supervisory authority and public interest review of a sale or merger.

We believed that state regulation of cooperatives was redundant because the cooperatives were democratically controlled. Also, deregulating these cooperatives allowed them to save thousands of dollars on regulatory hearings and processes - savings that could be passed on to the members.

I want to be clear that I believe that the best way to control a cooperative is through the democratic participation of its members. What we need to do as elected officials is to ensure that members have a voice and have the ability to know how and why a board of directors is making decisions.

However, the members of Pedernales Electric Cooperative have raised many concerns over the past year that they did not have a voice in their cooperative. Many of these customers are also my constituents.

Late last spring, my constituents began contacting my office to complain about the closed nature of the board of directors. Specifically, concerns were raised over the nomination and election process, the lack of transparency by the board of directors and senior management by prohibiting members from accessing cooperative information and board meetings, the failure of the cooperative to return excess profits by paying Capitol Credits, and the level of compensation and benefits received by board members and senior management.

In May 2006, a group of Pedernales members filed a civil lawsuit against the cooperative and the board of directors making the same claims I just mentioned. Basically, the members were suing themselves over perceived wrongdoing by the cooperative and the board. A settlement in the lawsuit has been reached, but has been appealed by two members of the cooperative.

This lawsuit, the watchful eye of the media and legislative scrutiny have led to an ongoing criminal investigation by the District Attorney with the assistance of the Texas Attorney General's Office.

It became apparent that the inability to elect anyone except the board's handpicked candidates allowed the Pedernales Electric Cooperative's Board of Directors to become a self-governed entity with no way to be controlled. And with no one able to look over their shoulders, abuses occurred. Examples of the excess abound.

First, the president of the board not only received the perks of being a board member, he also paid himself $190,000 annually as an employee, making him

eligible for retirement benefits with no real job duties. He currently is receiving over $10,000 a month in retirement benefits - all paid by the cooperative.

The General Manager was paid a $375,000 annual salary. In addition, the board secretly voted to give him an additional $2 million in deferred compensation over five years and a $375,000 signing bonus. None of this additional pay was disclosed to the members. And, it is alleged that the board falsified the 990 report to the IRS in 2004 by not reporting the general manager's total compensation and bonuses.

We know that the PEC board paid themselves excessive salaries and benefits - totaling over $1 million per year. All board members, including non-voting members, were given free lifetime health insurance for themselves and all dependents, and free $3,000 physicals for members and spouses at the Cooper Clinic Health Spa in Dallas. The board also created policies allowing for retiring board members to receive emeritus status with compensation of $1500 per month for life, in addition to the free lifetime health insurance for both member and dependents.

The board, senior management and their spouses or girlfriends traveled first class and stayed in luxury hotels - such as the Ritz Carlton, Four Seasons, Anatole Hilton - when traveling on cooperative business with no oversight or approval process.

$700,000 in credit card bills were paid without any approval process of whether those expenses were legitimate cooperative business - - such as $20,000 for furniture and several $2,300 restaurant tabs that included meals and alcohol.

Additionally, most large cooperative expenditures were not competitively bid and the value for those expenditures is not known.

Compounding these abuses, board meetings were not publicized or open to the members, so members could not know how and why decisions were being made. I personally attempted to enter a board meeting on January 3, 2008, and was denied entrance.

I could go on, but the fact is that if Pedernales Electric Cooperative had a true and open election process, these excesses probably would not have occurred.

Texas removed regulatory oversight over cooperatives in 1999 because it was redundant. We thought the members could determine how to run the cooperative through the election process - - if the members were unhappy with the decisions of the board of directors, they could and should vote them out of office.

This failure to have true and honest elections at Pedernales Electric Cooperative is the primary reason why the Senate Committee on Business and Commerce is taking another look at all electric cooperatives to make sure what happened at PEC is not happening in other parts of our state.

There have been reforms at Pedernales Electric Cooperative over the past year. These reforms have created a more democratic system and gives the members a voice. This voluntary compliance is encouraging because my preference is always to allow for local control. Pedernales Electric Cooperative just had its first open election last weekend with five new directors elected. This is a great first step on the path toward openness.

But if a cooperative board does not or will not remove the barriers for members to be involved, the state could be forced to address these issues through legislative action. I expect that the issues of requiring electric cooperatives to comply with open meetings and open records laws, plus mandating fair and open elections, will be addressed in the next legislative session.

I appreciate that Congress also is studying the issue of electric cooperatives. However, I want to assure each one of you that Texas is not asleep at the wheel and we are actively looking into the issue as our legislative session approaches. Please know that Texas will exercise its authority to regulate these entities at a state-level if necessary.

Thank you again for allowing me to be here today. I would be happy to answer any questions.