



## CAPITAL CREDITS POLICY

Effective Date: TBD

### POLICY AT A GLANCE

PEC is committed to upholding the Cooperative Principle of **Member Economic Participation** by reinvesting in our operations and returning margins to our Members in the form of Capital Credits.

### SUBJECTS INCLUDED IN THIS POLICY

CEO Responsibilities	Board Responsibilities	Net Operating Margin Allocations	Adjustments
Net Operating Loss Allocation	Notice of Allocation	Capital Credit Retirements	Discounting of Allocated Capital Credits
Establishing a Capital Credits Beneficiary	Recoupment	Forfeiture of Capital Credits	Method of Payment
Minimum Amount	Records	Unclaimed Retired Capital Credits	



## 1. PURPOSE

The purpose of the Capital Credits Policy ("Policy") is to establish that the method and manner in which Pedernales Electric Cooperative, Inc. ("Cooperative" or "PEC") allocates and retires Patronage Capital is compliant with applicable laws, restrictions imposed by its debt financing covenants, and the Cooperative's [Articles of Incorporation](#) and [Bylaws](#). The allocation and retirement of Patronage Capital shall be just and reasonable, not unreasonably preferential, prejudicial, or discriminatory to the Cooperative's Members, and implemented in a way that maintains a healthy financial state for the Cooperative.

## 2. SCOPE

- 2.1. This Policy applies to all Members (including designees) who have Allocated Capital Credits, the Board of Directors ("Board"), and employees of the Cooperative.

## 3. POLICY AND IMPLEMENTATION

### 3.1. Chief Executive Officer ("CEO") Responsibilities

- 3.1.1. The CEO is responsible for:

- 3.1.1.1. Implementing this Policy and for developing the practices and procedures necessary to allocate Capital Credits and retire Allocated Capital Credits according to this Policy;
- 3.1.1.2. Recommending to the Board the manner, method, timing, and amount for allocating Capital Credits and retiring Allocated Capital Credits. Recommending revisions to this Policy to the Board when changes are believed to be in the best interest of the Cooperative; and
- 3.1.1.3. Developing and implementing a program to: (1) educate employees and Members about the role of Capital Credits in the cooperative business model; and (2) effectively inform employees and Members about annual allocations and retirements.

### 3.2. Board Responsibilities

- 3.2.1. The Board is responsible for:

- 3.2.1.1. Reviewing, discussing, and evaluating the CEO's recommendations regarding the allocation and retirement of Capital Credits;
- 3.2.1.2. Approving allocations of Capital Credits and retirements of Allocated Capital Credits;
- 3.2.1.3. Reviewing, discussing, and evaluating this Policy regularly;
- 3.2.1.4. Reviewing, discussing, and evaluating the CEO's recommendations for revisions of this Policy; and
- 3.2.1.5. Approving and directing revisions to this Policy.

### 3.3. Net Operating Margin Allocations

- 3.3.1. Each Member purchasing electricity or being billed for electric services or energy from the Cooperative will receive an allocation of the Net Operating Margins.
  - 3.3.1.1. Non-utility, Non-Operating Margins will not be included in the allocation of Net Operating Margins.



**3.3.2.** If the Board approves, the Cooperative may allocate Capital Credits or retire Allocated Capital Credits to the various Member Classes under different manners, methods, timing, and amounts, as long as the Cooperative, is not acting unreasonably preferential, prejudicial, or discriminatory. Furthermore, the Cooperative may discount Allocated Capital Credits when retiring credits prior to the Retirement Schedule.

**3.3.3.** In most cases, the dollar amount of electricity or energy purchased by the Member during a year over the total amount of electricity or energy purchased by the Members within a Member Class is calculated to determine that Member's Patronage Capital and resulting contribution to Net Operating Margins.

**3.3.4.** Other methods of allocating Net Operating Margins may be utilized to the extent that those methods are deemed to be just and reasonable, not unreasonably preferential, prejudicial, or discriminatory.

### **3.4. Adjustments**

**3.4.1.** Net Operating Margins may be adjusted for the net change in accrued unbilled revenue, made by the Cooperative during the fiscal year.

**3.4.2.** Prior to any allocation, the Cooperative shall review each Member's billing records to ensure that any Members with a net negative billing have been adjusted so that these Members do not receive a negative allocation of the Net Operating Margins.

### **3.5. Net Operating Loss Allocation**

**3.5.1.** If the Cooperative has a Net Operating Loss in a given year, that loss will not be allocated to Members. Instead, that loss will be rolled forward and combined with the positive Net Operating Margins in the succeeding year(s) and any remaining Net Operating Margins will then be allocated to the Members.

### **3.6. Notice of Allocation**

**3.6.1.** The Cooperative will notify each Member in writing of the amount allocated to the Member for the preceding fiscal year within approximately eight and one-half months following the end of the fiscal year.

### **3.7. Capital Credits Retirements**

**3.7.1.** Capital Credits Retirements will be made consistent with the assumptions and limitations contained in the approved Equity Management Plan. The Board will use the Equity Management Plan as the basis for its determination of whether a retirement of credits may result in an adverse financial impact to the Cooperative. The Board must make this determination prior to any Capital Credit Retirements.

**3.7.2.** All Capital Credits Retirements must comply with restrictions placed on PEC by its lenders, its Articles of Incorporation, its Bylaws, and state and federal law.

**3.7.3.** Each year, subject to the Board's determination as to the impact to the Cooperative, the Cooperative will implement its Capital Credits Retirement strategy on a systematic basis for that year which includes General Capital Credits Retirement and/or Special Capital Credits Retirements as described in Sections 3.8 and 3.9.

**3.7.4.** When retiring Allocated Capital Credits outside of the Retirement Schedule, either through General Capital Credits Retirements or Special Capital Credits Retirements, the Cooperative will pay the discounted (applying the Discount Factor), net present



value of the Capital Credits. The actual amount of the discount will be recorded in the systems and records of the Cooperative in the name of the Member.

- 3.7.4.1.** Members with an Active Account may refuse Allocated Capital Credits retired outside the Retirement Schedule and elect to defer a discounting of its Allocated Capital Credits until such date as the payment at full value would otherwise occur. Acceptance of the discounted retirement of Capital Credits shall be considered acceptance of the Discount Factor. Members with Inactive Accounts may not refuse Allocated Capital Credits.

### **3.8. General Capital Credits Retirements**

- 3.8.1.** In general, Allocated Capital Credits are retired in accordance with the Retirement Schedule as permitted by the financial health of the Cooperative consistent with Cooperative policies, but the Board may decide to retire credits under alternative schedules. Unless otherwise directed by the Board, Capital Credits are generally retired as follows:

- 3.8.1.1.** A portion of the General Capital Credits Retirements will be from the oldest outstanding year(s) for which allocations have been made that have not yet been retired. To the extent credits from the oldest outstanding year(s) being retired have been retained less than the prescribed period in the Retirement Schedule, the Discount Factor will be applied to those credit amounts being retired.
- 3.8.1.2.** A portion of the General Capital Credits Retirements will be made from the most recent year(s) for which allocations have been made that have not yet been retired. To the extent credits from the most recent year(s) being retired have been retained less than the prescribed period in the Retirement Schedule, the Discount Factor will be applied to those credit amounts being retired.
- 3.8.1.3.** For members with Active Accounts and unretired credit allocations, a portion of the General Capital Credits Retirements may be made from any other year(s). To the extent credits being retired have been retained less than the prescribed period in the Retirement Schedule, the Discount Factor will be applied to those credit amounts being retired.

### **3.9. Special Capital Credits Retirements**

- 3.9.1.** The Cooperative may retire Capital Credits outside the Retirement Schedule after considering the determination of the Cooperative's financial health.
  - 3.9.1.1.** Estates - The Cooperative may specially retire Capital Credits when the Cooperative receives proper notification that a Member who is a natural person has died. If a Capital Credits Beneficiary was not established, upon request by the appropriate representative of the Member and upon receipt of appropriate legal documentation, the Cooperative will pay the estate its remaining Allocated Capital Credits after application of the Discount Factor. See Section 3.10 of this Policy for information on establishing a Capital Credits Beneficiary.
  - 3.9.1.2.** Non-Natural Members - The Cooperative may specially retire Capital Credits when the Cooperative receives proper notification of the dissolution, liquidation, or cessation of existence of any Non-Natural Member. Upon request of the appropriate representative of the entity and receipt of



appropriate legal documentation, the Cooperative will pay the Non-Natural Member its remaining Allocated Capital Credits after application of the Discount Factor. A Non-Natural Member that has dissolved or otherwise ceased existence for the purposes of reorganizing will not be eligible for a Special Capital Credit Retirement under this section.

- 3.9.1.3.** Inactive Accounts - The Cooperative may specially retire Capital Credits of a former member when the former member has been disconnected and is no longer receiving electric service from PEC. In addition to retiring the historically Allocated Capital Credits, the Cooperative may estimate and allocate the current period's capital credit amount for a Member disconnecting from service using the prior year's allocation percentage. The Cooperative will pay the former member its Allocated Capital Credits after application of the Discount Factor.

### **3.10. Establishing a Capital Credits Beneficiary**

- 3.10.1.** A Capital Credits Beneficiary is either a natural person or the PEC Charity designated by a Member to receive the Member's Capital Credits Retirements.
- 3.10.2.** If a Member has designated a Capital Credits Beneficiary, through PEC's Capital Credits Beneficiary determination process, the Capital Credits Beneficiary may be eligible to receive the Member's Allocated Capital Credits as a Special Capital Credits Retirement or one or more General Capital Credits Retirement authorized by the Board.
- 3.10.3.** Upon a Member designating a natural person as a Capital Credits Beneficiary, and anytime thereafter, the Member may agree to a discounted retirement upon their death. If the Member does not agree to a discounted retirement for its Capital Credits Beneficiary, the Member's Allocated Capital Credits will be retired through one or more General Capital Credit Retirements.
- 3.10.4.** Upon designating the PEC Charity as a Capital Credits Beneficiary, and anytime thereafter, the Member may agree to a discounted retirement upon their death.

### **3.11. Discounting of Allocated Capital Credits**

- 3.11.1.** The discounting of Allocated Capital Credits is computed by first determining the current net present value of a retirement of Capital Credits that would otherwise have been made upon the Retirement Schedule based on the Cooperative's cost of equity capital.
- 3.11.2.** The amount of the Discounted Payment will be equal to the net present value considering the date that the payment of Capital Credits would have occurred based on the Retirement Schedule.
- 3.11.3.** This discounting of Allocated Capital Credits will apply to both General Capital Credits Retirements and Special Capital Credits Retirements made prior to the period prescribed in the Retirement Schedule.

### **3.12. Recoupment**

- 3.12.1.** If a Member has a balance due to the Cooperative, the Cooperative shall apply part or all of the Capital Credits being retired to the Member's account balance, unless other arrangements for payment have been made by the Member.

### **3.13. Forfeiture of Capital Credits**



- 3.13.1.** The Cooperative shall not enter into any agreements under which a Member forfeits the right to the allocation or retirement of Capital Credits. The discounting of Capital Credits as provided for in this Policy shall not be deemed a forfeiture.

**3.14. Method of Payment**

- 3.14.1.** The Cooperative will pay Members for retired Capital Credits by check, bill credits, or other electronic means, depending on what method the Board determines will be most effective, and in the Cooperative's best interest.

**3.15. Minimum Amount**

- 3.15.1.** The Cooperative shall not retire and pay Allocated Capital Credits in an amount less than ten dollars (\$10.00), unless the retirement and payment is for all remaining Capital Credits allocated to a former member. The Cooperative may notify a former member that the former member has Allocated Capital Credits in an amount less than ten dollars (\$10.00).

**3.16. Records**

- 3.16.1.** The Cooperative will keep complete records of the amount of unretired Capital Credits that have been allocated to each Member, along with a record of the retirements to that Member representing the five years preceding the oldest outstanding unretired year. This information will be available upon request to each Member. The Cooperative requires each Member with Allocated Capital Credits to keep the Cooperative informed of such Member's current mailing address in order that the Cooperative may retire Allocated Capital Credits efficiently.

**3.17. Unclaimed Retired Capital Credits**

- 3.17.1.** To the extent Retired Capital Credits are to be paid to Members via check, the Cooperative will send checks containing Retired Capital Credit amounts to the most current address listed on the Cooperative's records for those Members. If a Member has failed to claim or cash checks with Retired Capital Credit Amounts, the Cooperative will void any such unclaimed or uncashed check within 120 days of issuance.
- 3.17.2.** Notwithstanding Section 3.17.1 of this Policy, if the most current address listed in the Cooperative's records for a Member with Allocated Capital Credits being retired has been determined by the Cooperative to be non-deliverable with respect to that Member, the Cooperative will not send a check containing Retired Capital Credit amounts for the Member to that address. Members, including former Members, are encouraged to keep the Cooperative informed of their current mailing address to facilitate receiving Allocated Capital Credit amounts as credits are retired. If required by the Texas Property Code, the Cooperative will send notice to a Member's last known address before remitting unclaimed Retired Capital Credits to the State Comptroller's Officer pursuant to Section 3.17.3 of this Policy.
- 3.17.3.** When Retired Capital Credit amounts remain unclaimed after three years, those amounts may be remitted to the State Comptroller's Office in accordance with PEC's [Unclaimed Property Policy](#) and with Section 74.3013 of the Texas Property Code.





## 4. DEFINITIONS

- 4.1. **Active Account** – An account of a Member that is receiving electric service or energy from PEC.
- 4.2. **Allocated Capital Credits** – The amount of Capital Credits allocated to each Member appearing as an entry on the permanent financial records of the Cooperative that reflects a Member's equity in the Cooperative.
- 4.3. **Capital Credits** – A representation of each Member's share of the Cooperative's Net Operating Margins based upon each Member's purchases of electric service or energy, or as such Net Operating Margins may otherwise be allocated within a Member Class to a Member.
- 4.4. **Capital Credits Beneficiary** – A natural person or the PEC Charity designated by a Member to receive the Member's Capital Credit Retirements.
- 4.5. **Capital Credits Retirements (or Retired Capital Credits)** – The payment made to a Member or a designee based on Allocated Capital Credits at the time the Board declares a retirement of credits after determination of the Cooperative's financial health.
- 4.6. **Discount Factor** – The factor to be applied based upon the Cooperative's cost of equity capital rate and the Retirement Schedule and calculated in accordance with Section 3.11 of this Policy.
- 4.7. **Discount Payment** – The amount paid to the Member equal to the net present value based upon the Cooperative's cost of equity capital rate and the number of years remaining in the Retirement Schedule.
- 4.8. **Equity Management Plan** – The Cooperative's plan for equity stabilization as outlined in the Equity Management Plan Policy.
- 4.9. **General Capital Credits Retirements** – The Allocated Capital Credits retained by the Cooperative and retired in accordance with Section 3.8 of this Policy.
- 4.10. **Inactive Accounts** – A Member account that is no longer receiving electric service or energy from PEC, and whose membership fee has been applied to the final bill or refunded.
- 4.11. **Member** – As defined in PEC's Tariff and Business Rules, a Member is any Person or governmental entity that has applied for electric service and has paid the Cooperative's membership fee and agrees to be bound by the Cooperative's governing documents. Under this Policy, a Member may include a former Member.
- 4.12. **Member Class** – A group of Members with similar electric use service characteristics (e.g., residential, commercial, industrial) taking service under one or more rate schedules.
- 4.13. **Net Operating Margins** – The excess revenue remaining after all operating expenses and cost of capital, including but not limited to, cost of power, depreciation, interest, and taxes have been deducted from the Cooperative's total operating revenue.
- 4.14. **Net Operating Loss** – The lack of revenue remaining when revenues are less than the aggregate amount of all operating expenses and other costs, including but not limited to, cost of power, depreciation, interest, and taxes.
- 4.15. **Non-Natural Member** – A membership in PEC held by an organization, group or legal entity other than a natural person.



- 4.16. Non-Operating Margins** – The margins generated from activities that are not related to providing electric service or energy to Members including, without limitation, gain or loss on disposal of assets, realized monetary settlements, and any other activities that would not be considered related to providing electric services or energy.
- 4.17. Patronage Capital** – The capital component a Member furnishes the Cooperative through payment of amounts billed for electric services or energy.
- 4.18. PEC Charity** – A nonprofit organization established by PEC that Cooperative Members may designate as a beneficiary for Capital Credits.
- 4.19. Person** – Any natural person, organization, or legal entity.
- 4.20. Retirement Schedule** – An approximate thirty-year schedule for retirement of Capital Credits as determined by the Board.
- 4.21. Special Capital Credits Retirements** – The Allocated Capital Credits retained by the Cooperative and retired in accordance with Section 3.9 of this Policy.
- 4.22. Unclaimed Capital Credits** – A Member's financial interest in Allocated Capital Credits that is presumed abandoned under Texas law.

## 5. POLICY ENFORCEMENT

The Board oversees and enforces this Policy. The CEO, through the Policy Administrator, shall implement and comply with this Policy. Violations of this Policy may result in disciplinary action, up to and including, termination.

## 6. REFERENCES AND RELATED DOCUMENTS

Texas Property Code (Unclaimed Property Title 6)

[Articles of Incorporation](#)

[Bylaws](#)

[Texas Utilities Code Section 161.059](#)

[Texas Utilities Code Section 41.055](#)

[Equity Management Plan Policy](#)

[Unclaimed Property Policy](#)

[Tariff and Business Rules](#)

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Approver:	Board of Directors
Applies to:	All PEC members, former members, Board of Directors and employees
Policy Administrator:	Chief Financial Officer
Superseding effect:	This Policy supersedes all previous policies and memoranda concerning the subject matter. Only the Approver may authorize exceptions to this Policy.

