

PRESENTED AT

2021 Gas and Power Institute

October 14, 2021

Houston, Texas

**Contracting Strategies and Examples
from
Winter Storm Uri**

James M. Pappenfus

Author Contact Information:

James M. Pappenfus

Reed Smith LLP

Houston, Texas

jpappenfus@reedsmith.com

713.469.3800

I. Introduction

Winter Storm Uri impacted the energy infrastructure throughout large portions of Texas in February 2021, particularly the infrastructure within the ERCOT power region. Power generation and natural gas infrastructure failure precipitated rolling blackouts and curtailments throughout the state. Lives were lost. Businesses floundered and many found themselves in bankruptcy. The issues and topics for discussion related to Winter Storm Uri could support a stand-alone semester-long course at many of Texas' law schools. This paper will focus only a smaller, discrete set of legal issues facing parties to power and/or gas contracts during and after the storm. Those issues relate to performance under power and gas contracts and excuses to performance set forth in those contracts. The issues considered here relate only to contractual rights, and so any doctrines of excuse, impossibility, or otherwise under common law or statute (for example, under the UCC) are out of scope for this paper and are not discussed.

II. Power

This paper uses as an example a wind power generation facility operating in ERCOT (the “**Example Power Transactions**”). The Example Power Transactions are a “virtual power purchase agreement.” The facility sells merchant into ERCOT (at the real-time settlement price at the node), but is hedged by selling physical power at the hub under a long-term, fixed price ISDA transaction. The ISDA transaction is for “Firm (LD)” energy and obligates the generator to sell physical volumes corresponding to actual generation at the facility, with a guaranteed minimum volume.¹ In ordinary course operations, this structure should expose the generator to operational risk related to the production guaranty, and congestion risk between the price at the node (where it sells its generation merchant into ERCOT) and the price at the hub (where it buys quantities to resell to the buyer under the ISDA). The operational risk is managed operationally and by appropriately sizing the liquidated damages payable for failing to satisfy the production guaranty. The congestion risk can be managed in a variety of ways in accordance with the parties' deal and financing structure.

Winter Storm Uri flipped ordinary course operation on its head. Imagine that, as a result of the storm, a significant number of wind turbines iced over and were incapable of operation. Imagine further that the access roads to the base of each tower were impassable due to ice and snow, meaning that crews were unable to access and repair the de-icing equipment. Accordingly, actual generation at the facility was well below the production guaranty. Did the parties intend for these circumstances to constitute force majeure so as to excuse the generator's obligation to satisfy the production guaranty, or must the generator purchase, and then deliver volumes at the hub necessary to satisfy its minimum delivery obligation? If it fails to do so, is it excused under the terms of the

¹ Unless modified by the parties, the ISDA Power Annex defines “Product” by reference to Schedule P of the EEI Master Power Purchase and Sale Agreement (hereinafter Schedule P). Schedule P defines Firm (LD) as follows:

“Firm (LD)” means, with respect to a Transaction, that either Party shall be relieved of its obligations to sell and deliver or purchase and receive without liability only to the extent that, and for the period during which, such performance is prevented by Force Majeure. In the absence of Force Majeure, the Party to which performance is owed shall be entitled to receive from the Party which failed to deliver/receive an amount determined pursuant to [the terms related to liquidated damages for failure to deliver or receive].

Firm (LD) product definition? Below we analyze the Example Power Transactions from the perspective of the product definitions and the application of force majeure circumstances.

A. Product Definitions

A significant number of issues and disputes in the wake of Winter Storm Uri relate to a party's rights and obligations with respect to performance—delivery and receipt of power. For example, a seller's ability to excuse performance can depend on whether the contract calls for unit contingent or firm delivery. These complications can become clearer and the parties' intent evidenced by clear descriptions and definitions of the product that is being bought and sold.

Product definitions under common master agreements and PPAs accomplish several things. For one, they present options to buyers and sellers in a way that establishes the parties' intent to allocate performance risk. That intent is both express (via the selection of a product) and implied (via the exclusion of the products not selected). The implied intent (via exclusion) is stronger under the master agreements, as voluminous addenda and product definition documents provide a menu of options for sophisticated parties. Next, product definitions in master agreements can aid in drafting bespoke PPA terms where there may be gap risk between the terms of back-to-back agreements and a parties' desire to pass risk up or down the chain of title. For example, a PPA offtaker buying power at the node and then selling the power under an ISDA at a distant delivery point may consider aligning the PPA product description with the ISDA product that is being sold at some further delivery point.

All of this is to say that the selection of a Product, and the careful drafting of a bespoke PPA product description, should be a party's first and primary method of understanding and mitigating the risk that Winter Storm Uri-type events can create exposure under trading documents.

B. Force Majeure

1. Generally

The concept of force majeure, and parties' rights upon the occurrence of force majeure, are closely related to (and in many cases, intertwined with) the product definitions or other description of a party's delivery or receipt obligations. During and after Winter Storm Uri, force majeure became the first instinct for many parties seeking an excuse to performance when deals became uneconomic. The viability of such legal strategies varies widely and is based on circumstances, including the extent to which parties adhered to contractual requirements with respect to declaring, describing, or otherwise mitigating the force majeure event.

The question of whether force majeure may legally excuse a party's performance is, not surprisingly, complex and dependent on the facts of a given situation and the contract underpinning a deal. As a general proposition, force majeure clauses are contractual provisions that guard against unforeseeable risks.² However, from a practical perspective, for standard-form power master agreements, where the delivery obligation is Firm, force majeure essentially only excuses

² See Calamari and Perillo on Contracts § 13.19, 6th ed. (West 2009).

Find the full text of this and thousands of other resources from leading experts in dozens of legal practice areas in the [UT Law CLE eLibrary \(utcle.org/elibrary\)](https://utcle.org/elibrary)

Title search: Contracting Strategies and Examples from Winter Storm Uri

Also available as part of the eCourse

[Methods for Hedging: Reducing Market Exposure to the Uri Storm Conditions for Gas and Power](#)

First appeared as part of the conference materials for the
2021 Gas and Power Institute session

"Methods for Hedging that Reduced Market Exposure to the Uri Storm Conditions for Both Gas and Power"