

I. EXECUTIVE SUMMARY

A. Objectives and scope

Daymark Energy Advisors (Daymark) was retained to perform an independent operational efficiency review of CPS Energy (CPSE). Daymark evaluated CPS Energy's performance from three perspectives: (1) financial health, (2) operational excellence, including both electric and gas operations, and (3) customer engagement, user experience, and services design. This report presents the results of Daymark's review.

B. Summary of findings and recommendations

This section presents Daymark's high-level findings and recommendations. Additional discussion, observations, and recommendations can be found in the corresponding subject area sections (IV., V., VI., VII.). In addition, for the convenience of the reader, a complete list of observations and recommendations is included as Appendix A.

CPS Energy organization-wide themes

Overall, our review of CPS Energy found a utility that is moving out of a reactive and into a proactive approach while facing resource constraints in many parts of the organization.

For many years, CPS Energy was able to offer competitive rates and strong electric reliability performance while avoiding rate increases through aggressive cost management and by realizing additional revenue through sales of surplus generated electricity into the Texas wholesale markets. Recently, however, responding to a combination of deferred expenditures, new investment needs to address reliability vulnerabilities revealed by Winter Storm Uri and decarbonization objectives, and staffing and financial challenges stemming from the pandemic, CPS Energy has begun a transition to a more proactive approach, making the first of a series of rate increase requests while it begins to rebuild staffing levels and take on deferred system upgrades and IT projects.

Daymark's survey of CPS Energy found a utility that is functioning well on many metrics, but that still faces a number of resource constraints, particularly in the area of staffing, and that has an ambitious list of programs and projects for the next five years and beyond. Working to ensure that staffing and other resources are adequate to allow CPS Energy to meet its goals while managing customer cost impacts is a central challenge CPS Energy faces across its organization.

Financial health

Despite forgoing base rate increases for eight years, CPS Energy has been successful in managing its financial health and maintaining acceptable financial metrics. However, the resulting lean organization and deferment of key initiatives such as replacement of its IT systems, coupled with disruptions relating to Winter Storm Uri and the pandemic, have created mounting cost pressures that require a transition to a cycle of more frequent base rate increases. In gaining approval for a 3.85% rate increase that took effect in March 2022, CPS Energy has communicated its plans to request regular rate increases approximately every two years at least through 2027.

Below are the highest-priority observations and recommendations for CPS Energy's financial health. In section IV. and Appendix A, Daymark presents additional recommendations and discusses all observations and recommendations in greater detail.

- CPS Energy is in stable financial position, with a debt capitalization ratio comparable to other peer utilities despite the growth in overdue customer accounts. CPS ENERGY and the CPS ENERGY Board of Trustees (the "Board") should continue their efforts in this area. If necessary, growth in overdue customer accounts should be considered in future rate increases.
- CPS Energy should work with the Board to build on *Vision 2027* to develop a medium- and long-term financial strategic planning process separate from the budget and rate request processes.

Operational excellence

In review of the operational excellence of CPS Energy, Daymark was charged with assessing historic operations, management, and sustaining and transition CPS Energy's workforce. Given that CPS Energy is both an electric and gas utility, Daymark approached this section by analyzing these two functions separately.

Through our review of such metrics against historic data and curated benchmarks, we observed a utility which operationally has achieved largely satisfactory outcomes over the period reviewed. Our analysis herein largely focuses on the core strategic challenges that our team perceived based on our review of files and procedures, discussions with management, and our industry experience. These strategic challenges, depending on how they are dealt with by CPS Energy, have the potential to worsen outcomes (e.g., experience greater frequencies/durations of service interruption or upward pressure on

rates), or, as we would hope, be dealt with in a way that increasingly positions CPS Energy as a model utility among its peers.

Below are the observations and recommendations for CPS Energy's operational excellence that Daymark deems as of the greatest prioritization. In section V., Daymark discusses all operations observations and recommendations in greater detail.

Electric operations

- Utilize circuit-level and root cause type reliability data to refine system investment strategy and document within the Reliability and Power Quality Report.
- Undertake an analysis of contracted resource usage within the electric operational units; we suggest one goal of such a review to be the establishment of decision criteria pertaining to outsourcing strategy.
- The Board and management should establish metrics which allow management and stakeholders to track the achievement of benefits that the grid modernization / OT / SCADA set of investments are intended to deliver.
- Resolve technological barriers to acting on circuit-level asset condition work orders.
- Develop a major outage restoration plan to establish necessary investments, practices, and procedures.
- Expand the justification and benefits descriptions for balancing O&M and non-critical projects within capital planning process.
- CPS Energy staff are actively engaged in ERCOT (Electric Reliability Council of Texas) stakeholder processes; however, CPS Energy should consider whether there are ways to enhance internal processes to ensure CPS Energy reaps the full potential benefit of this engagement.

Gas operations

- Develop a more formal written winter season management plan, including investments, practices and procedures, and automated reporting to executive management.
- Establish an additional gas operation Tier 1 Metric that tracks industry standard leaks that remain open for repair at year end, with the objective that this will be limited to those identified within the last 45 days.
- Investigate adding to Gas division staff to support new customer interconnection and leak repair efforts.

- Develop and/or partner with workforce organizations to create an in-house training program to attract more junior employees cost-effectively.

Customer engagement

In review of customer engagement at CPS Energy, Daymark analyzed CPS Energy's customer outreach product and services, stakeholder engagement, and use of stakeholder feedback.

The customer organization in several departments function with high energy and passion for helping each customer. CPS Energy has a wide breadth of programs in place that target a broad range of their customer base, including programs for energy efficiency and renewables, demand response programs, financial assistance programs, and outreach initiatives. In general, we observed a CPS Energy team that is highly sensitive in responding to new customer needs presented to them, and they have developed an expansive array of programs that serve many customers. However, CPS Energy's prioritization of customer assistance and outreach programs is very reactive to outside guidance, including guidance from government officials and requests from community leadership. As a result, CPS Energy's efforts can be characterized as reactive, rather than as strategically designed, and informed by in-depth customer analyses, which are necessary to develop programs that are truly customer-driven. Below are the recommendations for CPS Energy's customer engagement. In section VI., Daymark presents additional discussion and recommendations and discusses all observations and recommendations in greater detail.

- Establish a three to five-year plan for customer engagement budget, staffing, and improved data gathering and analytics.
- Commit to Enterprise Resource Planning (ERP) specifications that support the tasks necessary to improve customer data gathering, storage, and analytics.
- Rework customer satisfaction related surveys to make detailed customer segmentation analysis possible.
- Integrate energy efficiency, customer sited renewables, energy burden programs into resource planning processes and rate design to determine right-size funding while assuring energy equity.

The Enterprise Resource Planning transition

CPS Energy is embarking on a major effort to procure and implement new Enterprise Resource Planning (ERP) software to replace end-of-life software the currently supports vital CPS Energy functions, including customer account management, human resources,

and procurement. Based on Daymark's review, we support CPS Energy's transition to a new ERP system and believe that CPS has taken and/or is planning many positive steps to manage risk; however, for this kind of project, risk continues to be a central concern. In section VII., we review some key ERP risks, and the steps CPS Energy is taking to manage them, and make some additional recommendations related to risk management.

- CPS Energy's existing end-of-life software and systems are hindering operational efficiency and make internal controls more difficult to implement and monitor. The Board of Trustees should exercise due diligence in its oversight to help to make the transition successful.