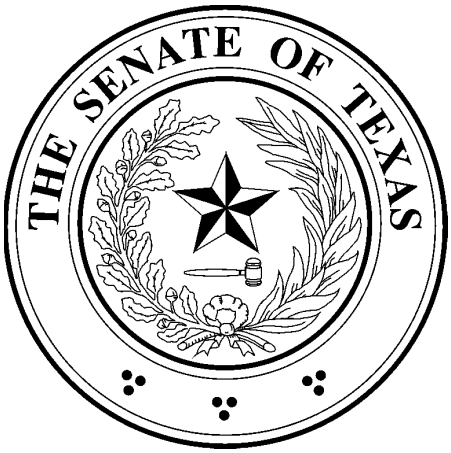
SENATE COMMITTEE ON
BUSINESS AND COMMERCE

Interim Report to the

89th Legislature



December 20, 2024

The Honorable Dan Patrick
Lieutenant Governor of Texas
P.O. Box 12068
Austin, Texas 78711

Dear Governor Patrick:

In response to your interim charges assigned to the Senate Committee on Business and Commerce, this report contains recommendations of the Committee. We appreciate your leadership and the opportunity to inform legislation to be proposed in the 89th Legislative Session that may address issues of utmost importance to the state.

Respectfully,

Senator Charles Schwertner, Chair

Senator Phil King, Vice-Chair

Senator Brian Birdwell

Senator Donna Campbell

Senator Brandon Creighton

Senator Nathan Johnson

Senator Lois Kolkhorst

Senator José Menéndez

Senator Mayes Middleton

Senator Robert Nichols

Dean Judith Zaffirini

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SENATE COMMITTEE ON BUSINESS AND COMMERCE INTERIM CHARGES

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2. **Texas Energy Fund**: Review and report on the impact of Senate Bill 2627, the Powering Texas Forward Act, as passed by the 88th Legislature, which established the Texas Energy Fund (TEF) to provide grants and loans to finance the construction, maintenance, modernization, and operation of electric facilities in Texas.

3. **Innovative Power Generation**: Explore emerging technologies with the potential to add new dispatchable power to our electric grid including, but not limited, to small modular nuclear reactors, advanced batteries, and new developments in hydrogen and geothermal resources. Identify and recommend regulatory and policy actions required to deploy emerging technologies within the state's electric grid.

4. **Transmitting Texas Power**: Identify the future electric transmission and distribution system needs of the state and recommend ways to reduce barriers to constructing the necessary electric infrastructure to support the growing demand and changes in technology. Review and make any necessary recommendations to enhance legislation passed during the 88th legislative session, including the status of projects to improve the safety and resiliency of the transmission system, as well as the effect of current and future projects on consumer costs.

5. **Managing Texas Sized Growth**: Evaluate the state's ability to keep pace with increasing electricity demand related to population growth and energy intensive technologies such as electric vehicles and data centers. Recommend ways to increase reliability via demand-side response programs. Study ERCOT's forecasting methodology and recommend ways to increase transparency. Monitor ongoing efforts at the Public Utility Commission related to energy efficiency programs and distributed energy resources, including the implementation of Senate Bill 1699, 88th Legislature.

6. **Impact of Bitcoin Mining on the Texas Electric Grid**: Study the impact of energy-intensive cryptocurrency mining facilities on the Texas electric grid. Report on whether any changes should be made to ERCOT demand response programs and large flexible load registration requirements to limit the impact of these facilities on system reliability and consumer costs.

7. **Addressing the Rising Cost of Insurance**: Assess the impact of rising property and casualty insurance costs on Texas property owners, real estate lenders, and commercial and industrial development. Identify ways to increase consumer transparency to better inform coverage decisions and make recommendations to ensure a competitive and affordable insurance market for consumers.

8. **Artificial Intelligence**: Examine the development and utilization of artificial intelligence (AI). Evaluate the implications of AI adoption across the public and private sectors. Make recommendations for a responsible regulatory framework for AI development, including data privacy, industry standards, consumer protections, risk mitigation, and compliance processes. Propose any necessary changes to state law to protect the Texas radio, television, music, and film industries against unauthorized use by AI. Monitor the findings of the Texas Artificial Intelligence Advisory Council.

9. **Non-Compete Agreements**: Examine the impact of the Federal Trade Commission's final rule on non-compete agreements on Texas employers including, but not limited to, contractual exceptions and limitations on independent contractors, for-profit and non-profit businesses, and senior executives. Identify ways to address balancing legitimate business interests of employers while also protecting employment mobility, increasing innovation, and fostering new business formation. Report on whether any changes should be made to existing law on the criteria, procedures, and remedies on enforcing non-compete and alternative agreements.

SENATE COMMITTEE ON BUSINESS AND COMMERCE INTERIM HEARINGS

June 12, 2024, *E1.028*
The Committee took invited and public testimony on Charge Nos. 1, 4, and 6.

August 27, 2024, *E1.012*
The Committee took invited and public testimony on Charge Nos. 2 and 8.

October 1, 2024, *E1.028*
The Committee took invited and public testimony on Charge Nos. 3, 5, 7, and 9.

INTERIM CHARGE DISCUSSIONS AND RECOMMENDATIONS

CHARGE NO. 1

Electricity Market Design: Assess state efforts to provide incentives for new thermal generation. Review and report on the state of the electricity market in Texas and issues impacting the reliability and resiliency of the Texas electric grid. Consider rulemaking related to wholesale market design, including the impact of these changes on grid reliability, market revenues, costs to consumers, and the efficiency of operations. Examine and report on the direct and indirect impacts that variable resources, such as wind and solar, have on grid resiliency, consumer prices, and market uncertainty. Monitor the implementation of House Bill 1500, 88th Legislature.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on June 12, 2024, and considered testimony from witnesses.

Discussion

In 2021, the 87th Texas Legislature passed sweeping reforms to strengthen the stability and resiliency of the Electric Reliability Council of Texas (ERCOT) grid, while also refining the market design principles that guide reliability, transparency, and efficiency. Senate Bill 3 introduced sweeping changes into the Texas electric system – notably, requiring critical power facilities to weatherize – and over the course of recent summer and winter season demands, those changes have proven effective in ensuring reliability.

With a market design blueprint in place, the 88th Legislature shifted its focus to record-breaking electricity demand. Extreme heat contributed to 49 new demand records in ERCOT during the summer of 2023, the highest of which was 85.7 gigawatts (GW).[1] To keep pace with increasing electricity demands, lawmakers and industry regulators contemplated various proposals to incentivize production and improve the optimization of resources. One such proposal, discussed later in this report, was the Texas Energy Fund, which passed into law to accelerate the development of dispatchable power essential to meeting growing demand.

The 88th Legislature also passed House Bill 1500, the omnibus Public Utility Commission of Texas (PUC) Sunset bill, which makes important administrative and governance changes to improve agency operations, while also adding substantive programs and standards to strengthen the electricity market. These programs aim to support grid stability while maintaining the state's commitment to an energy-only framework.

The Business and Commerce Committee hearing on June 12, 2024 examined the impact of recent legislation and its influence on the direction of the Texas electricity market. ERCOT and the PUC discussed the implementation status of various market design initiatives, metrics, and studies, including:

[1] Potomac Economics, *2023 State of the Market Report for the ERCOT Electricity Markets,* 8. (May 2024). https://www.potomaceconomics.com/wp-content/uploads/2024/05/2023-State-of-the-Market-Report_Final_060624.pdf.

- Real-Time Co-Optimization (RTC): Scheduled to go live on December 5, 2025, RTC aims to optimize the dispatch of resources and ancillary services, reducing costs and enhancing efficiency.
- Reliability Unit Commitment (RUC): ERCOT's use of the RUC process prompted comments of concern at the hearing regarding the negative impact of frequent RUC activity on the longevity of power plants, the overall cost to the market, and the economic disincentive for plants to self-commit.
- Dispatchable Reliability Reserve Service (DRRS): House Bill 1500 created DRRS as a new standalone ancillary service product for the procurement of certain dispatchable generation resources during periods of operational uncertainty. DRRS is slated for implementation in 2026.
- Performance Credit Mechanism (PCM): House Bill 1500 also defines guidance and guardrails for a "reliability program," currently proposed as the PCM, that would provide additional revenue to generators available during peak demand times. The PCM remains under evaluation, with ERCOT recommending that "additional refinements to the PCM's design could be considered for the PCM to have a more substantive impact."[2] Stakeholders and the Committee emphasized language in House Bill 1500 that clearly defines critical guardrails, stressing that any program must align with these rules for it to be implemented. Members also reiterated that the PUC is *permitted* but not *required* to adopt a reliability program. Questions were also raised as to whether the PCM or a similar program was necessary, given the combination of TEF loans, growing demand from large loads, and new revenue streams such as the DRRS, which are intended to specifically compensate thermal generation resources.
- ERCOT Contingency Reserve Service (ECRS): A recently deployed ancillary service product, ECRS has sparked debate around over-procurement and artificial shortages. The Committee questioned the cost impact of ECRS on consumers.

Testimony discussed the importance of ancillary services for reliability, but the Committee highlighted the need for careful study of the costs and benefits to ensure ancillary services deliver measurable value. Members also questioned the necessity or redundancy of the PCM given substantial capital already flowing in the market. Members reiterated that Texas remains firmly committed to its energy-only market design, with no plans to transition to a capacity market.

The Committee also heard testimony on key topics, including:

- Load Growth: ERCOT forecasted peak demand to nearly double from 85 GWs in 2020 to 150 GWs by 2030, driven by industrial electrification, AI data centers, cryptocurrency, and hydrogen production.[3] The Permian Basin alone is projected to add 24 GW, rivaling the Houston area's energy demand.[4]
- Transmission: The rapid growth from large loads is creating urgency in aligning transmission and generation planning. This topic is highlighted in a later charge.
- Affordability: Members and witnesses discussed the cost impact of recently implemented and proposed market decisions on consumers. Members expressed concern over balancing the need for reliability with affordability, especially for residential users.

[2] Electric Reliability Council of Texas. *ERCOT Assessment of Performance Credit Mechanism Costs and Effects.* (December 2024).
[3] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (June 12, 2024) (Statement of Pablo Vegas, Chief Executive Officer, Electric Reliability Council of Texas).
[4] Id.

The Committee highlighted the contributions of the Independent Market Monitor (IMM) and the Office of Public Utility Counsel (OPUC) in pursuing transparency, providing important perspectives on the electricity market, and representing the consumer voice as new rules and regulations are considered.

Conclusion and Recommendations

Today, the Texas electricity market is widely regarded as the most robust in the world. With the integration of new emerging technologies and market dynamics, regulators must remain focused on prioritizing reliability and resiliency, and ensuring affordable power for all. To that end, the Committee recommends:

- If the PUC exercises the option to implement the PCM or a similar reliability program, it must adhere to the legislative guardrails as defined by House Bill 1500.
- The OPUC and IMM's access to the data and ability to conduct thorough analyses is critical for ensuring transparency and accountability in market operations. The Legislature should consider providing OPUC with additional resources to enhance the agency's data verification and analytics capabilities. This will better position OPUC to independently validate the impact of proposed changes to Texas consumers.

CHARGE NO. 2

Texas Energy Fund: Review and report on the impact of Senate Bill 2627, the Powering Texas Forward Act, as passed by the 88th Legislature, which established the Texas Energy Fund (TEF) to provide grants and loans to finance the construction, maintenance, modernization, and operation of electric facilities in Texas.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on August 27, 2024, and considered testimony from witnesses.

Discussion

In 2022, Texas joined California as the only other state with a population of more than 30 million.[5] Texas' population is booming and shows no signs of slowing down. At the same time, Texas' economy is growing rapidly, particularly across energy-intensive industries. With more families and businesses relying on the Texas grid for power, more generation resources are needed to keep pace with demand.

The 88th Texas Legislature passed Senate Bill 2627 and Senate Joint Resolution 93, the Powering Texas Forward Act, which created the Texas Energy Fund (TEF) as a dedicated grant and loan program to finance the construction, maintenance, modernization, and operation of new electric generating facilities in Texas. A key feature of the TEF is its focus on the development of 10,000 megawatts (MW) of thermal generation, which is essential to addressing the state's growing energy needs while providing firm power needed to balance the variability of renewable resources. The 88th Legislature appropriated an initial $5 billion to the TEF, and in November 2023, Texas voters ratified the creation of the state energy fund by passing Proposition 7.

The Public Utility Commission of Texas (PUC) and Deloitte, the contractor hired to administer the fund, oversee the execution of four TEF programs. Each of these programs target specific energy needs within Texas:

- ERCOT Dispatchable Generation Loan and Bonus Programs: Loans and completion bonuses support the construction of 10,000 MWs of dispatchable thermal generation within the ERCOT region. Funding is only available for facilities added to ERCOT's Capacity, Demand, and Reserves (CDR) Report after June 1, 2023.
    - In-ERCOT Loan Program: Loans support new construction of dispatchable generation facilities of at least 100 MWs.
    - Completion Bonus Grants: Bonuses awarded to new construction of dispatchable generation facilities of at least 100 MWs that are interconnected and operational prior to June 1, 2029. The bonuses are awarded based on the timeframe by which the new facility comes online and are paid out over a 10-year period.
- Outside ERCOT Grant Program: Grants support transmission and distribution infrastructure and electric facility modernization, weatherization, reliability and resiliency enhancements, and vegetation management.

[5] Texas Comptroller of Public Accounts. *The Future of Texas Power.* (September 2024). https://comptroller.texas.gov/economy/fiscal-notes/industry/2024/energy-demand/.

- Texas Backup Power Package Program: Grants or loans to support design, procurement, installation, and use of backup power packages for certain critical facilities.

On June 1, 2024, the PUC announced that the In-ERCOT Loan Program received 125 Notices of Intent, representing 55,908 MWs of proposals to construct dispatchable generation projects in Texas.[6] On July 29, 2024, the PUC announced it received 72 loan applications representing more than 38,379 MWs and $24.41 billion in requests.[7] PUC Commissioners ultimately selected 17 generation projects for final due diligence review.

All 11 members of the Senate Business and Commerce Committee signed a letter to the PUC in advance of the August 27, 2024 hearing, emphasizing its position that "a diverse portfolio of investment opportunities supports healthy competition necessary for a robust ERCOT market."[8] The letter reiterated the importance of a transparent, prudent review as qualified projects and sponsors advance through the due diligence process.

During the hearing, several members raised questions about transparency in the TEF project selection process, and emphasized the program contractor's responsibility and fiduciary duty in maintaining the integrity of the TEF programs. Members also emphasized the importance of ensuring a diverse pool of grant and loan recipients, reflecting various project sizes, geographical locations, and technological approaches to contributing reliable power to the grid. Concerns were raised regarding the 10,000 MW cap limit, with some suggesting that decoupling the loan and completion bonus program would allow new facilities coming online that are not utilizing the loan program to better access completion bonus funding.

After the Business and Commerce Committee hearing, a joint House and Senate Texas Energy Fund Advisory Committee held a separate public hearing to discuss concerns and propose solutions regarding the TEF contractor's initial application screening process, focusing on a potentially fraudulent project application that was initially selected for due diligence review but later rejected due to the concerns raised. At the instruction of legislators, the contractor issued a commitment to return 10 percent of its professional fees back to the state.[9] The Senate Business and Commerce Committee has continued to work with the PUC to ensure its stewardship of the TEF program meets the expectations of both the Legislature and Texas voters.

Conclusion and Recommendations

The TEF is paramount to long-term grid reliability and resiliency. Therefore, the Committee recommends:

- Given the overwhelming response to the In-ERCOT Loan Program, the Legislature should appropriate the remaining $5 billion to fully capitalize the TEF at its intended $10 billion.
- The PUC's TEF administrator and its contractor must ensure rigorous review of sponsor and project information, and identify any criteria for disqualification without delaying the opportunity for other

[6] Press Release, Public Utility Commission of Texas, Public Utility Commission of Texas Sees Strong Industry Response to Texas Energy Fund Loan Program (June 1, 2024).
[7] Press Release, Public Utility Commission of Texas, Public Utility Commission of Texas Receives 72 Applications for Texas Energy Fund Loan Program (July 29, 2024).
[8] Letter from the Senate Committee on Business & Commerce to the Public Utility Commission of Texas (August 7, 2024).
[9] Letter from Deloitte Consulting LLP to the Public Utility Commission of Texas (October 8, 2024).

projects to participate in the TEF. Any project that is denied during the due diligence phase must be expeditiously replaced with another well-qualified application.

CHARGE NO. 3

Innovative Power Generation: Explore emerging technologies with the potential to add new dispatchable power to our electric grid including, but not limited, to small modular nuclear reactors, advanced batteries, and new developments in hydrogen and geothermal resources. Identify and recommend regulatory and policy actions required to deploy emerging technologies within the state's electric grid.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on October 1, 2024, and considered testimony from witnesses.

Discussion

Texas is synonymous with power production and generates more electricity than any other state.[10] With its abundant natural resources, Texas can leverage a diverse fuel mix to support grid reliability. And with the retirement of older power plants, the urgency to accelerate the deployment of innovative power technologies – such as geothermal, advanced battery storage, hydrogen, and nuclear – has become increasingly relevant to meeting the state's growing energy demands.

Testimony at the October 1, 2024 hearing discussed ways Texas can lead the field in developing and deploying innovative power technologies:

- Geothermal: Geothermal energy, which aligns with Texas's oil and gas expertise, is capable of providing reliable, dispatchable power, especially in remote areas. Witnesses promoted geothermal energy as a reliable, 24/7 dispatchable resource. Current geothermal projects show promising scalability and grid integration. The Committee highlighted the need for quicker permitting processes to expand geothermal capabilities.
- Batteries: Energy storage resources have proven critical for grid stability, particularly in managing the intermittency of renewables like wind and solar. Although technology is advancing to four-hour duration projects, batteries in the field today typically operate for one to two hours and are therefore not capable of long-duration deployment needed during extended peak demand periods.[11] Further, members raised questions about safely disposing decommissioned battery materials, and introducing permits and other necessary regulations to prevent liabilities from falling on local communities.
- Nuclear: New nuclear technologies are stable and provide consistent power, can achieve higher fuel efficiency, and require a small area footprint, among many benefits. Witnesses highlighted the safety and efficiency of new nuclear designs compared to traditional nuclear power plants. Small modular reactors (SMRs), for example, offer a safer and more adaptable form of nuclear energy. Witnesses discussed Texas' potential to lead in nuclear power, but noted federal licensing processes and timelines still hinder nuclear expansion. Members previewed the Texas Advanced Nuclear Reactor Working Group report

[10] U.S. Energy Information Administration. *Texas State Profile and Energy Estimates*. https://www.eia.gov/state/?sid=TX#:~:text=In%202023%2C%20Texas%20produced%20more,of%20energy%20to%20other%20states.

[11] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (October 1, 2024) (Statement of Mark Stover, Texas Solar+Storage Association).

recommendations for accelerating the development of the nuclear industry in Texas. The Working Group's report was published on November 18, 2024, and highlighted strategies involving streamlined permitting, targeting nuclear research and a skilled workforce, and creating dedicated funding programs for development, siting, and supply chain readiness.[12]

- Hydrogen: Limited discussion on hydrogen power centered on its zero-emissions profile. Members expressed optimism about its role in decarbonizing the grid. However, hydrogen's expensive processes and conversion losses present early challenges in its development and adoption.

These energy resources, each at different developmental stages, could collectively support Texas' long-term energy needs if implemented strategically.

Conclusion and Recommendations

Texas has become a center for research and development of emerging power resources and is well-positioned to expand its nuclear, geothermal, and hydrogen production, as well as energy storage capabilities. However, regulatory improvements and strategic investments will be crucial in the coming years. The Committee emphasized creating a balanced policy approach to support these technologies, and recommends:

- Continued stakeholder engagement is needed to advance policies that thoroughly address core issues stalling nuclear deployment, including reducing lengthy regulatory hurdles, and bridging gaps between research and commercialization.
- Adopt battery decommissioning standards to address safety and logistical challenges associated with the end-of-life management of these systems.
- Explore educational programs and other ways to build a skilled workforce for all emerging technologies, ensuring that Texas remains a leader in energy innovation.

[12] Texas Advanced Nuclear Reactor Working Group. *Deploying a World-Renowned Advanced Nuclear Industry in Texas. Considerations and Recommendations for Action*. (November 2024).

CHARGE NO. 4

Transmitting Texas Power: Identify the future electric transmission and distribution system needs of the state and recommend ways to reduce barriers to constructing the necessary electric infrastructure to support the growing demand and changes in technology. Review and make any necessary recommendations to enhance legislation passed during the 88th Legislative Session, including the status of projects to improve the safety and resiliency of the transmission system, as well as the effect of current and future projects on consumer costs.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on June 12, 2024, and considered testimony from witnesses.

Discussion

Texas boasts one of the most expansive and rapidly growing electric grids in the United States. Despite Texas's ability to build transmission faster than most states – averaging three to six years compared to seven to 13 years elsewhere – Texas' transmission infrastructure remains bottlenecked. [13] The Electric Reliability Council of Texas (ERCOT) currently has over $14 billion in transmission projects under various stages of planning and construction to address the growing needs of the state.[14] And while investments in infrastructure seem promising for the state's economy, significant load growth across Texas has placed pressure on the transmission system.

In 2023, the Legislature prioritized transmission infrastructure with the passage of House Bill 5066, which required the PUC to direct ERCOT to develop a reliability plan for the Permian Basin region to extend transmission service to areas where mineral interests have been found. House Bill 5066 streamlines the process for addressing load growth and grid congestion by permitting transmission service providers (TSPs) to justify new projects through a letter attesting to projected load, rather than requiring a signed customer agreement. This alternative process allows for expedited approvals for new transmission projects. Testimony at the June 12, 2024 hearing discussed the attestation process, with members considering the need for a more detailed or standardized reporting of projects to mitigate inconsistencies or double-counting across TSPs. Members stressed the importance of accurate and validated load data to prevent overestimating growth and overbuilding infrastructure.

The hearing also discussed Texas' pressing need for more transmission capacity, especially in fast-growth regions and areas with developing large loads. ERCOT reported a significant anticipated increase in electricity demand, reaching around 150,000 megawatts (MW) by 2030.[15] In fact, the forecasted load studied under House Bill 5066 found the expected load in the Permian Basin alone was estimated to be 43 percent higher than the anticipated load described in a 2023 study of the same region. To accommodate growth, ERCOT discussed the implementation of 765-kilovolt (kV) transmission lines as part of their Regional Transmission Plan (RTP). ERCOT has studied options for replacing areas of 345 kV infrastructure with a 765 kV "backbone."

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[13] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (June 12, 2024) (Statement of Commissioner Lori Cobos, Public Utility Commission of Texas).

[14] Id.

[15] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (June 12, 2024) (Statement of Pablo Vegas, Chief Executive Officer, Electric Reliability Council of Texas).

Further, stakeholders discussed how energy-intensive industries like cryptocurrency mining and AI data centers are driving the need for new transmission lines. They also highlighted the impact of new construction on transmission costs, and suggested regulators consider all options for reducing cost impacts on residential and small businesses. Protecting these consumer classes from skyrocketing transmission costs is especially important given the discussion around the need for a potential statewide transmission buildout. The Independent Market Monitor (IMM) similarly noted in its recent report that the current transmission cost allocation method (known as 4CP) provides incentives for large loads to behave in ways that limit their exposure to transmission cost recovery, without reducing the need for new transmission investments.[16] Witnesses and members discussed transparency around transmission costs, which currently comprise 30 percent to 40 percent of a customer's electricity bills, and suggested legislative solutions may be needed to address cost allocation.[17]

In addition to reliability planning, the 88th Legislature passed a major resiliency planning bill, House Bill 2555, which takes a forward-looking approach to transmission hardening and development. Specifically, the bill allows electric utilities to file comprehensive resiliency or investment plans for PUC approval. Early investments address system vulnerabilities, and help mitigate more costly repairs and upgrades. To that end, witnesses mentioned that Texas currently does not have basic standards for pole inspections, repairs, reinforcements, or replacements. Incorporating more comprehensive pole standards will enhance system reliability, improve safety, and extend the lifespan of critical infrastructure. Witnesses pointed out that as the state prepares for major disasters, like wildfires and hurricanes, continued legislative focus on transmission hardening will be critical.

Conclusion and Recommendations

Texas must prioritize transmission development and ensure that new projects can be implemented efficiently and cost-effectively. Importantly, strict review must be given to large-scale development that could impose a financial burden on everyday Texans. As such, the Committee recommends:

- Continue assessing the development of new transmission projects in alleviating congestion and supporting growth, but prioritize greater accuracy in load forecasts and commitments from large loads, such as cryptocurrency mining and data centers, to ensure infrastructure investments align with substantiated growth.
- The PUC should complete an independent analysis of the direct and indirect costs associated with transitioning to 765 kV higher voltage transmission lines.
- Direct the PUC to increase transparency regarding the impact of new transmission costs on customer rates, including approved resiliency plans and interim cost recovery filings, by providing this information in an accessible and easy to understand format.
- Consider measures that cap or limit the percentage of transmission costs passed on to small consumers by ensuring that industries with significant electricity demands bear a fair portion of their actual costs.
- Authorize the PUC to establish standards for hardening poles, particularly in coastal and high-risk areas. These standards should consider preventative measures to extend the lifespan of poles, and levels of remediation or replacement for degraded infrastructure.

[16] Potomac Economics. *2023 State of the Market Report for the ERCOT Electricity Market, 22.* (May 2024). https://www.potomaceconomics.com/wp-content/uploads/2024/05/2023-State-of-the-Market-Report_Final_060624.pdf.

[17] Hearing before S. Comm. on Business & Commerce, (June 12, 2024) (Testimony by Commissioner Lori Cobos, Public Utility Commission of Texas).

CHARGE NO. 5

Managing Texas Sized Growth: Evaluate the state's ability to keep pace with increasing electricity demand related to population growth and energy intensive technologies such as electric vehicles and data centers. Recommend ways to increase reliability via demand-side response programs. Study ERCOT's forecasting methodology and recommend ways to increase transparency. Monitor ongoing efforts at the Public Utility Commission related to energy efficiency programs and distributed energy resources, including the implementation of Senate Bill 1699, 88th Legislature.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on October 1, 2024, and considered testimony from witnesses.

Discussion

With one of the largest economies in the world, a reliable and resilient grid is critical to supporting a state the size of Texas. Rapid economic and population growth is driving unprecedented demand for electricity, especially from an influx of energy-intensive technologies that require significant, sustained power.

The Electric Reliability Council of Texas (ERCOT) testified at the June 12, 2024 hearing that electricity demand in Texas could reach 150,000 megawatts (MW) by 2030.[18] This forecasted load growth is driven by the expansion and electrification of industrial, manufacturing, oil and gas, and high tech industries. The state's business-friendly environment and competitive electricity rates make Texas an ideal hub for large loads.

Still, the accelerated pace at which large loads are flocking to Texas creates risks that must be addressed with an updated regulatory framework. Data centers, for example, operate continuously with a non-flexible load profile, and require a dependable and uninterrupted power supply. Further, data centers do not typically participate in demand response programs, which can pose significant challenges as ERCOT must balance supply and demand in an increasingly complex energy landscape.

Witnesses discussed a number of factors to consider as the Legislature approaches options to support managing large load growth. First, witnesses discussed improving the load interconnection processes by implementing fees or deposits to reduce speculative applications. Witnesses also emphasized the need for large loads to provide ERCOT with more detailed profile data, enabling greater visibility that ensures ERCOT can manage resource adequacy and maintain system stability. Other potential solutions could include requiring data centers to maintain onsite backup generation that could be utilized during certain emergency periods.

While the majority of witnesses were in overall agreement that Texas is seeing exponential load growth, concerns were raised around the certainty of ERCOT's expected load growth numbers. Relatedly, members discussed a need for regular updates to ERCOT's demand forecasts, with more scrutiny upfront so that prospective load data

[18] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (June 12, 2024) (Statement of Pablo Vegas, Chief Executive Officer, Electric Reliability Council of Texas).

does not lead to inaccurate forecasting. Witnesses added that accurate forecasting is imperative because Texas will likely see even more rapid load growth in future years, requiring planning for a substantial amount of new generation, and an expansion of or upgrades to the existing transmission system.

Witnesses continued discussions from the June 12, 2024 hearing regarding the proposed extra high-voltage (EHV) transmission to transport power more efficiently. However, the Committee cautioned against a quick adoption of EHV lines outside of the legislative process, due to the significant investment and regulatory planning required. Members stressed a need to reevaluate the current process for apportioning transmission costs as the Legislature considers new transmission infrastructure.

Finally, witnesses testified about the benefits of aggregated distributed energy resource programs that combine small-scale energy resources, such as batteries and smart appliances. As stakeholders work to enhance telemetry and improve the ability of distributed energy resources to respond to dispatch signals effectively, this technology has the ability to contribute capacity to the system and serve as a unique tool for grid management.

Conclusion and Recommendations

By managing growth challenges with a forward-looking approach, Texas can continue to meet its growing electricity needs while maintaining reliability, affordability, and economic competitiveness. The Committee recommends:

- While any new regulations must preserve Texas' business-friendly environment, the state should ensure grid regulators have visibility into large load profiles and behaviors, which could be achieved by enhancing existing registration requirements.
- Require large loads to offset their impact on the grid by adding on-site power systems or participating in programs to curtail electricity usage during peak demand periods.

CHARGE NO. 6

Impact of Bitcoin Mining on the Texas Electric Grid: Study the impact of energy-intensive cryptocurrency mining facilities on the Texas electric grid. Report on whether any changes should be made to ERCOT demand response programs and large flexible load registration requirements to limit the impact of these facilities on system reliability and consumer costs.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on June 12, 2024, and considered testimony from witnesses.

Discussion

Cryptocurrency mining has become one of the fastest-growing electricity loads in Texas, driven by the state's competitive electricity rates and business-friendly environment. The mobility of mining facilities presents challenges for ERCOT – 90 percent of the country's cryptocurrency mines can be constructed in six to 12 months – and grid regulators must now plan for the unpredictability of new cryptocurrency loads as mining is projected to quadruple in Texas by 2030.[19] In addition, cryptocurrency facilities can typically turn off and back on rapidly, which can create uncertainty for transmission operators and ERCOT. Some of these facilities are registered in ERCOT's Controllable Load Resource (CLR) program – registration is required for a load to be able to participate and earn money in the real-time energy market and for ancillary services – but the program is voluntary and higher registration would provide ERCOT with more predictability.

Cryptocurrency facilities require large-scale power to run servers, and because they are highly flexible, they frequently adjust their energy consumption in response to market price fluctuations and to avoid paying transmission costs. During periods of peak prices, mining operations can scale back or turn off, freeing up power for the grid. While this price-responsive behavior can provide benefits, it also introduces instability. Further, cryptocurrency miners can participate in ERCOT programs that allow them to resell pre-purchased electricity back into the market. While cryptocurrency miners state that their ability to curtail quickly offers a vital service to the grid, concerns have been raised that the intensive power demands required at mining operations plays an outsized role in creating the strains on the grid these companies then are incentivized to solve. The unique ability for bitcoin miners to leverage certain financial perks within the Texas electricity market, combined with their demand on the system, has raised questions as to whether these activities benefit the broader Texas customer base, or primarily serve to increase profits for mining companies, and, thus is a continued topic of discussion at the Capitol. [20]

ERCOT estimates 40,000 megawatts (MW) of cryptocurrency mining or large flexible loads are currently in the

[19] Reuters. "AI's Race for US Energy Butts up against Bitcoin Mining." *Reuters*, August 28, 2024. https://www.reuters.com/technology/artificial-intelligence/ais-race-us-energy-butts-up-against-bitcoin-mining-2024-08-28/.

[20] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (June 12, 2024) (Statement of Brian Morgenstern, Head of Public Policy, Riot Platforms Inc.).

interconnection queue.[21] In other words, the need for transparency in ownership and operation of cryptocurrency mining facilities is critical for ERCOT planning. During the hearing, members expressed concern over the risk of overbuilding infrastructure to meet miners' needs, only for those facilities to shut down and relocate, leaving Texas ratepayers to cover stranded costs. Additional visibility into how (and how long) these loads participate in the ERCOT market is important to evaluating the potential grid impacts.

Conclusion and Recommendations

The rise of cryptocurrency mining and other large flexible loads presents a new set of challenges and opportunities for the Texas electric grid. To address the unique demands of these operations, the Committee supports the following recommendations:

- The Legislature should further evaluate how cryptocurrency miners are profiting from conditions in the ERCOT market or acting as "energy traders," and consider closing loopholes that allow these companies to leverage financial perks for private benefit.
- The Legislature should also consider enhancing reporting requirements to give the state greater knowledge of the ownership of cryptocurrency facilities and ensure these facilities do not pose a risk to the grid.

[21] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (June 12, 2024) (Statement of Woody Rickerson, Senior Vice President and Chief Operating Officer, Electric Reliability Council of Texas).

CHARGE NO. 7

Addressing the Rising Cost of Insurance: Assess the impact of rising property and casualty insurance costs on Texas property owners, real estate lenders, and commercial and industrial development. Identify ways to increase consumer transparency to better inform coverage decisions and make recommendations to ensure a competitive and affordable insurance market for consumers.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on October 1, 2024, and considered testimony from witnesses.

Discussion

The Property and Casualty Insurance industry is vital to the Texas economy, offering coverage to protect homes, vehicles, businesses, and other assets from financial losses. The Texas Department of Insurance (TDI) reports that Texas has the second largest insurance market in the nation, and the fifth largest in the world, with $290 billion in premiums in 2023.[22] The increasing rates seen in recent years are driven by extreme weather, rising inflation and labor expenses, supply chain disruptions, and reinsurance. In 2023, there were 16 disasters in Texas that cost $1 billion or more, a new state high for billion-dollar disasters in a single year.[23] Since the 2003 Insurance Market Reforms, Texas has experienced a level of elasticity and incremental changes in rates. However, the landscape has shifted; Texas, along with the rest of the nation, is now experiencing a hard market, prompting policyholders to shop around more extensively for coverage options. A 2023 Consumer Reports survey of its members revealed that only 13 percent of respondents regularly shop for new coverage.[24] This suggests a potential disconnect between policyholder expectations and what carriers are offering in terms of coverage options.

The Committee examined rate increases by discussing market pressures and perspectives of state agencies, insurance carriers, and related industries. TDI provided testimony on the current state of the market, and addressed pricing and availability concerns. In 2024, four carriers officially left the state, directly impacting 11,000 homeowners.[25] This statistic does not take into account targeted nonrenewals and specific underwriting guidelines that fall below the threshold that carriers are required to inform TDI of when pulling business from the state. The Texas Fair Access to Insurance Requirements (FAIR) Plan was created in 1995 to address residential property insurance policy concerns in underserved areas and operates as an insurer of last resort. A good indicator of the health of a market can be measured by FAIR Plan exposure rates. With this in mind, FAIR plan policy counts totaled 91,841 as of June 2024, a significant uptick from the 72,626 policies reported shortly before in December 2023.[26] Despite this concerning trend, TDI maintains that the state's insurance market does not have an availability problem, but rather a pricing issue. Homeowners in Texas saw an average rate change increase of 21.1

[22] Hearing before S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (October 1, 2024) (Statement of Cassie Brown, Commissioner, Texas Department of Insurance).
[23] National Centers for Environmental Information (NCEI), *U.S. Billion-Dollar Weather and Climate Disasters (2024).* https://www.ncei.noaa.gov/access/billions/state-summary/TX.
[24] "Best Homeowners Insurance Buying Guide," Consumer Reports.
[25] Brown, Statement to Committee.
[26] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (October 1, 2024) (Written testimony of Commissioner Cassie Brown, TDI).

percent for 2023, compared to 10.8 percent in 2022. In that same time frame, personal auto average rate change increased by 25.5 percent.[27]

The Office of Public Insurance Counsel (OPIC) represents the interest of Texas consumers in insurance matters and is tasked with reviewing rates, rules, and policy forms. OPIC manages the Policy Comparison Tool, which helps consumers compare policies and coverages while shopping for insurance. Concerns have been raised about outdated data and prices changing too quickly for the tool to stay current.

As of October 2024, TDI reviewed 1,313 rate filings, with 107 filings withdrawn by carriers and 78 rejected purely for administrative discrepancies.[28] The agencies reported on their timelines for rate reviews, while members asked questions on the thoroughness of these reviews and their impact on Texans. Along with the availability and timeliness of data on coverage options, there is also concern about the lack of transparency consumers face regarding the factors insurance carriers use to determine rates and reinsurance premium increases. Members questioned reporting practices for insurance company investment income when TDI looks at rate filings.

Instead of lower rates, policyholders are encountering more tradeoffs within their coverage options, like increased deductibles and actual cash value in lieu of replacement cash value. Insurers are adjusting their underwriting guidelines, resulting in nonrenewals and slower policy decision timelines, rather than a full withdrawal from targeted regions. Progressive Insurance made headlines in 2024 when they decided to restrict new homeowners' business in the state, after reporting that 40 percent of their recent storm losses were credited to Texas.[29]

There are various factors that contribute to maintaining stability in the insurance market, and striking a balance between allowing insurers to effectively respond to sudden shifts in risk while not exposing policyholders to unjust practices is critical. The Texas insurance market presents both unique challenges and opportunities for carriers, who must contend with exposure and concentrated risk to reap the benefits of a marketplace with upwards of thirty million people.

Supply chain and labor shortages have led to the average cost to build homes going up. As small businesses, builders take out general liability insurance policies that protect against lawsuits and other claims arising from operations. They also have to budget for builders' risk insurance which insures a structure while under construction. This policy is often required to comply with government or banking regulations and can be a significant driver to pricing homes beyond prospective buyers' budget.

The Texas Mortgage Bankers Association (TMBA) reported that their lenders reported of insurers refusing to replace roofs in areas routinely hit by hail, hurricanes, or tornadoes. Similarly, some member lenders say that rather than rescinding coverage, carriers are declining to issue or quote policies from the outset, citing the age or condition of a roof as the primary reason. Carriers are offering policies with less coverage that leave lenders, servicers, and asset owners exposed. A home that was built and insured at a certain value will often see the forecasted cost to repair it surge beyond its original coverage. In some cases, there might not be continuity of coverage as carriers decline to cover a property they would have in the past.

[27] Letter from Cassie Brown, Commissioner, TDI, to Senate Committee on Business & Commerce (October 18, 2024).
[28] Commissioner Brown, Letter to Committee (October 18, 2024).
[29] The Progressive Corporation. *2024 Second Quarter Report.*

Texas currently operates under a file and use system, where insurance companies file their proposed rates with TDI, but are allowed to begin using the new rates immediately or after a short waiting period. TDI reviews the filed rates to ensure they are not excessive, inadequate, or unfairly discriminatory. During this process, TDI analyzes evidence and may request additional documentation to ensure the rates are actuarially sound. This system is appealing to insurers because they are afforded the flexibility to adjust rates in response to market conditions. The disadvantage, as members pointed out, is that if rates are not reviewed immediately, consumers may temporarily pay higher premiums until the filed rates are deemed excessive. This reactive environment can also lead to unexpected rate spikes for policyholders, often with reduced coverage in their policies. The Committee expressed interest in exploring the benefits of alternative systems and considering ways to improve Texas' existing file and use system for additional efficiency, transparency, and reliability.

Other major rate filing systems include prior approval and flex rating. Prior approval requires insurance companies to get explicit approval from a state's insurance regulator before implementing any new rates or rate changes. This can protect consumers from large rate fluctuations and unjust pricing practices. However, it can create artificial pricing in a slower marketplace, lead to less availability, and increase administrative costs that could be passed on to policyholders. Flex rating utilizes a hybrid approach that combines elements of both prior approval and file and use systems. Insurers can change their rates within a predetermined range, commonly referred to as a flex band, without prior approval. If an insurer wants to increase rates beyond the flex band, they must get approval from the state regulator.[30] This provides a certain degree of flexibility for carriers to be responsive to the market while implementing guardrails to protect against extreme rate increases without proper review. This could, however, increase the frequency of rate changes for consumers, albeit in smaller increments.

As insurance premiums fluctuate, it is incumbent on TDI to regularly evaluate the appropriate balance in Texas' rate review process to ensure consumers are protected, and can access affordable and adequate coverage. The Committee explored potential structural and organizational changes to TDI, aimed at improving the agency's responsiveness to consumer needs and industry practices. One such idea that members and witnesses discussed was transitioning TDI from its current single-commissioner structure to three-commissioner leadership model. Several large state agencies, such as the Public Utility Commission (PUC), Texas Workforce Commission (TWC), and Texas Commission on Environmental Quality (TCEQ), already operate under a multi-commissioner framework.

Conclusion and Recommendations

Insights from the Committee's discussion highlight the need to improve TDI's operations and better align with industry demands, and place particular emphasis on adopting best practices for policyholders throughout Texas. The Legislature is recommended to consider the following:

- Evaluate organizational changes within TDI to enhance decision-making and facilitate better discussions with marketplace participants.
- Require TDI to monitor and analyze insurance carrier trends and thresholds regarding nonrenewals and coverage reductions.

[30] National Association of Insurance Commissioners, *Property and Casualty Insurance Industry 2024 Market Trends*, https://content.naic.org/sites/default/files/pfr-24.pdf.

- Implement guardrails to protect against unfair pricing practices, which could include, but is not limited to, rate filings and premiums assessed to policyholders.
- Support the efforts of both TDI and OPIC to improve notice to policyholders about rate changes, coverage reductions, and comparison-shopping tools.

CHARGE NO. 8

Artificial Intelligence: Examine the development and utilization of artificial intelligence (AI). Evaluate the implications of AI adoption across the public and private sectors. Make recommendations for a responsible regulatory framework for AI development, including data privacy, industry standards, consumer protections, risk mitigation, and compliance processes. Propose any necessary changes to state law to protect the Texas radio, television, music, and film industries against unauthorized use by AI. Monitor the findings of the Texas Artificial Intelligence Advisory Council.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on August 27, 2024, and considered testimony from witnesses.

Discussion

Significant advancements in the innovation and application of artificial intelligence (AI) systems outpace the development of laws and guidelines to regulate its use, creating oversight gaps at both the state and federal level. The U.S. Department of State defines AI systems as "a machine-based system that can, for a given set of human-defined objectives, make predictions, recommendations or decisions influencing real or virtual environments."[31]

The European Union (EU) passed the AI Act, a comprehensive regulatory framework aimed at ensuring the safe and ethical use of AI. It categorizes AI applications by risk-level, from high-risk and threatening or exploitative uses, to low-risk applications, such as interactive AI-powered games. It also establishes compliance requirements and set standards for transparency and accountability.[32] In the United States, 45 states introduced legislation in 2024, targeting specific AI regulations and aiming to extend oversight beyond existing privacy and intellectual property laws. [33] Colorado's Artificial Intelligence Act (CAIA), for example, which is set to take effect in February 2026, is modeled after the EU's risk-based approach and is the first comprehensive state law addressing AI. With an emphasis on consumer protection and risk management, the CAIA seeks to provide guidelines on mitigating algorithmic discrimination and ensuring responsible deployment.[34] Meanwhile, Connecticut and California have met challenges in passing state-based legislation due to the complexities of regulating AI technology.

In Texas, state agencies have started to purchase and employ AI systems to streamline internal processes and improve their outreach services. These applications have grown more extensive, and agencies' requests have become extremely nuanced, further highlighting the need for greater oversight. In 2023, the Texas Legislature passed House Bill 2060, establishing the Artificial Intelligence Advisory Council (AIAC) to study and monitor

[31] H.R.6216 - 116th Congress (2019-2020): National Artificial Intelligence Initiative Act of 2020. https://www.congress.gov/bill/116th-congress/house-bill/6216.
[32] European Commission, *Artificial Intelligence Act*, COM, 2021 OJ (206) final.
[33] "Artificial Intelligence 2024 Legislation," NCSL, September 2024, https://www.ncsl.org/technology-and-communication/artificial-intelligence-2024-legislation.
[34] Colorado General Assembly. Senate Bill 205: Colorado Artificial Intelligence Act. Passed May 2024, (effective February 1, 2026).

artificial intelligence systems developed, employed, or procured by state agencies.[35] They were tasked with assessing the need for a state code of ethics and guidelines necessary to protect the liberty, finances, livelihood, and privacy of Texas residents.

AI technologies' ability to influence data and decision-making underscores the need for enhanced visibility into these systems to ensure accurate, fair, and transparent operations. To that end, the Committee expressed concerns over data privacy, the integrity of AI-produced data, and the risks of "poisoned data" sourcing state and federal AI systems.[36] Members also expressed concern over broader cybersecurity concerns associated with increased uses of AI. There are instances of foreign actors collecting data from social media, and stealing intellectual property and sensitive health care information. Domestically, the spread of unfettered misinformation and disinformation to the public at large, affects election integrity and more generally, trust in the government processes.

State agencies testified on their internal uses of AI for increased efficiency, securing contracts for AI systems, managing associated risks, and monitoring industry trends observed as regulatory bodies. The Department of Information Resources (DIR) provided an update on their work with the AIAC, and gave an overview of DIR's advisory role in vetting prospective vendors and guiding state agencies through new technology deployments.

The Texas Workforce Commission (TWC) testified on their various use cases, beginning with a chatbot to field unemployment benefit inquiries, and more recently, on proposed initiatives designed to help employers develop job postings. TWC discussed data security and emphasized the controlled handling of sensitive information. While new technologies have the potential to revolutionize how workforce data is optimized, there are risks related to potential biases from AI-driven decisions, further highlighting the importance of human reviews.

The Texas Office of the Attorney General (OAG) discussed their collaboration with law enforcement to combat AI-related copyright violations, pursue cases involving the creation and distribution of AI-generated child sexual abuse material, and ensure compliance with consumer protection laws. Additionally, the OAG has a Consumer Protection Division that tackles deceptive business practices involving the misuse and illegal acquisition of data, which can corrupt AI systems and have detrimental effects.

The Texas Department of Insurance (TDI) reviewed agency regulations and trends on industry uses of AI, noting that 70 percent of insurers are actively exploring AI capabilities within homeowners' insurance.[37] As insurance companies become increasingly reliant on AI, it is being integrated into essential processes like underwriting and claims management. Members cautioned against an overreliance on AI-generated models that may unfairly discriminate against consumers, particularly in terms of pricing and coverage decisions. TDI discussed its authority to require insurers to explain AI data sources powering underwriting guidelines and ensure accuracy of third-party data. While the agency can pursue actions against carriers if the data creates an adverse outcome for policyholders, developing a set of standards to ensure responsible deployment of AI and compliance parameters might be necessary.

[35] Texas Legislature. *House Bill 2060, 88th Regular Session (2023)*. Enrolled version.
[36] Hearing before S. Comm. on Business & Commerce, (August 27, 2024) (Statement of Dr. Drew Hamilton, Texas A&M Cybersecurity Center).
[37] Hearing before S. Comm. on Business & Commerce, (August 27, 2024) (Statement of Commissioner Cassie Brown, Texas Department of Insurance).

Representatives from the private sector provided their perspective on the need for an AI regulatory framework that balances innovation with privacy and responsible application. As AI becomes more integrated into business practices, protecting customers from unchecked AI misuses by private and third-party entities presents a significant challenge. Witnesses emphasized the importance of best practices to ensure advances in AI align with ethical considerations. To that end, internal governance should include accountability measures, such as regular audits, transparency reports, and mechanisms for consumers to challenge AI-driven decisions. For consumers to trust AI, they need to understand how it works and how AI might influence decision-making.

Further, AI usage in certain critical fields may necessitate additional accountability, transparency, and consumer protections. Namely, the integration of AI in healthcare raises questions about accountability and liability where diagnostic algorithms affect patient care. Healthcare representatives mentioned that AI tools should adhere to the same strict accountability standards expected of professionals in the medical field.[38] For example, protecting patient information and compliance with the Health Insurance Portability and Accountability Act (HIPAA) must extend to AI programs. Additionally, AI has the potential to significantly impact the patient-provider relationship, particularly if patients feel that decisions are being made solely by machines rather than humans. To allay concerns, physicians must retain oversight of medical AI tools and ensure the data used to train systems represents the appropriate patient populations.

Creative industry representatives offered other perspectives on the use of AI across radio, television, music, and film industries. The film and motion picture industry representative expressed both optimism and caution over AI's role in filmmaking. While AI offers a tool to enhance films and make production more efficient, there are concerns that AI could negatively affect an actor's ability to work and control their likeness. Witnesses also discussed the need for disclosing AI use to preserve public trust in the content they consume, such as when editorial liberties are taken during political advertisements.

Similarly, music representatives voiced support for robust protections against AI's unauthorized use of an artist's name, image, likeness, and voice, noting that such misuse could jeopardize artists' livelihood, fan relationships, and legacy. In Texas, the right of publicity is a property right that safeguards against the unsanctioned commercial use of a deceased individual's identity.[39] As technology advances and digital replicas become difficult to discern, Texas needs to consider stronger guardrails against unlawful exploitation of the individuals within the creative industry whose livelihoods depend on controlling commercial access to their work.

Ultimately, AI can be used for great good but if left unchecked, can lead to great harm. Certain unacceptable and prohibited uses endanger consumer transparency and undermine public trust. As AI technologies integrate into everyday life, promoting ethical utilization practices is of paramount importance. It is essential to establish standards that curb system biases, algorithmic discrimination, and data exploitation. Routine audits are critical to ensure that AI systems operate fairly, particularly in sensitive applications like hiring, lending, and insurance, where biased outputs could have serious consequences.

Data privacy is also vital. Consumers should have clear, actionable rights to control how their data is collected, used, and shared in AI. This includes disclosures and notices, empowering individuals to be informed if they are

[38] Hearing before S. Comm. on Business & Commerce, (August 27, 2024) (Statement of Dr. Zeke Silva, Texas Medical Association).
[39] Callie Baker, *Misappropriation and Right of Publicity*, Texas Music Office. (September 2011). https://gov.texas.gov/music/page/misappropriation_and_right_of_publicity.

interacting with an AI system rather than a human. Moreover, it is important for consumers to understand if their data is being used to train AI models, with transparent consent protocols in place. Building trust in AI systems means prioritizing fairness, transparency, and user control to ensure these technologies serve society responsibly.

Conclusion and Recommendations

Texas must pursue comprehensive model legislation and adopt a balanced approach to regulating AI that puts guardrails in place without stifling innovation. The Legislature can work towards this goal in the following ways:

- Create an Ethical Code of Conduct for state agencies that promotes accountability and responsible uses of AI systems. Direct DIR to set standards for certifying AI systems that contract with agencies.
- Direct each state agency to publish a biennial report detailing the AI systems deployed by the agency, including the data inputs and decision-making processes.
- Require deployers of AI systems and work products to disclose when and how the technology is being used.
- Require bias audits for all AI algorithms used in critical sectors, such as healthcare, financial services, employment, and insurance. This could include regular assessments to ensure AI systems are free from biases along with a public disclosure requirement for companies to share the results of these audits.
- Ensure individuals impacted by AI-driven decisions have the ability to appeal the decision and request a human review.
- Define the role of developers and deployers to distinguish liability in cases where AI systems cause harm.
- Enhance protections for representatives in the radio, television, music, and film industries to prevent the unauthorized commercial use of their identities.

CHARGE NO. 9

Non-Compete Agreements: Examine the impact of the Federal Trade Commission's final rule on non-compete agreements on Texas employers including, but not limited to, contractual exceptions and limitations on independent contractors, for-profit and non-profit businesses, and senior executives. Identify ways to address balancing legitimate business interests of employers while also protecting employment mobility, increasing innovation, and fostering new business formation. Report on whether any changes should be made to existing law on the criteria, procedures, and remedies on enforcing non-compete and alternative agreements.

Testimony

The Senate Business and Commerce Committee ("Committee") held a public hearing on October 1, 2024, and considered testimony from witnesses.

Discussion

Traditionally, each state has established its own framework for determining whether a non-compete agreement is binding, leaving the courts to enforce these agreements on a case-by-case basis. However, in recent years, several states have proposed or passed legislation to limit or invalidate burdensome non-compete agreements.

In January 2023, the Federal Trade Commission (FTC) proposed a sweeping rule to ban non-compete agreements, characterizing them as "a widespread and often exploitative practice that suppresses wages, hampers innovation, and blocks entrepreneurs from starting new businesses."[40] However, on August 20, 2024, a U.S. district court judge enjoined the FTC's rule, concluding that the FTC lacked the authority to regulate unfair methods of competition through substantive rulemaking. While the rule remains in flux and state laws continue to govern non-compete agreements, the lack of consistency and shifting positions regarding these contracts present challenges to both businesses and employees.

To better assess the impact of non-compete agreements on the Texas economy and workforce, the Committee conducted an in-depth review of the state's workforce and the use of non-compete or alternative agreements across various industries. In doing so, the Committee aimed to evaluate the balance between employee rights and employer protections, while continuing to foster innovation and strengthen economic growth.

The Texas Workforce Commission (TWC) provided testimony on the state's current workforce, detailing both employment and unemployment statistics, as well as areas facing labor shortages. TWC described the job market as active and competitive, emphasizing Texas's favorable business climate. However, despite overall activity in the job market, employee shortages remain in some industries, including healthcare. To address these challenges, TWC emphasized strategic efforts on upscaling and rescaling initiatives, aiming to equip professionals with the essential skills needed to meet evolving industry demands.

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[40] Federal Trade Commission, *FTC Proposes Rule to Ban Noncompete Clauses, Which Hurt Workers and Harm Competition*. (January 5, 2023). https://www.ftc.gov/news-events/news/press-releases/2023/01/ftc-proposes-rule-ban-noncompete-clauses-which-hurt-workers-harm-competition.

The National Federation of Independent Business (NFIB) stressed the importance of state rather than federal-level regulation of non-compete agreements to ensure policies remain aligned with the unique business and labor needs of each state. NFIB contended "elected representatives are the proper individuals to debate and impose restrictions; they can ascertain what policies industries, workers, and employers require in their state."[41]

A legal expert in the technology industry discussed how non-compete agreements may negatively impact their industry, as non-competes are frequently included in employment contracts as a legal default rather than a necessity. Other contracting options, such as non-disclosure agreements, non-solicitation agreements, and intellectual property protections may be sufficient to safeguard proprietary information and business relations, without affecting employee mobility and job creation. Accordingly, major tech companies, such as Microsoft and Space X, do not use non-compete agreements, suggesting that legislation addressing non-compete agreements in the technology industry may be unnecessary and even counterproductive.

Conversely, a representative from the healthcare industry highlighted critical concerns specific to the use of non-compete agreements among physicians and other healthcare practitioners. Recent data shows these agreements affect 37 percent to 45 percent of physicians.[42] Stakeholders suggest the rigid application of non-competes in certain medical contracts restricts the freedom and ability of providers to provide patient care, contributing to healthcare shortages, especially in rural and underserved areas of the state. Physicians and other healthcare practitioners who are bound by non-compete agreements may also find it more difficult to negotiate competitive salaries, leading to job dissatisfaction, frustration, burnout, and feelings of being trapped in their current position.

In general, the Committee questioned whether non-compete agreements are being misused as coercive tools. Members heard of cases where these agreements exploit a job seeker's unequal bargaining power, compelling them to accept terms that create conditions akin to indentured servitude. Employees often lack clear information about the existence or enforceability of a non-compete agreement as part of their employment contract. In many cases, employees decide to leave their profession altogether rather than pursuing expensive litigation challenging the agreement. Members discussed the need for transparency, reasonable limitations, and safeguards against excessive restrictions on employees. They discussed legislative solutions to tailor regulations to specific industries, and exceptions in cases involving the sale of a business or a merger and acquisition.

More specifically, testimony recognized the disproportionate affect of non-compete agreements on the healthcare industry. As such, witnesses proposed targeted reforms, such as limiting non-compete agreements to one year post-employment, establishing clear geographic boundaries, and implementing exceptions for circumstances that involve public interest, such as in medically underserved areas.[43] According to the Health Professions Council's May 2024 projections, Texas continues to face a significant physician shortage, with an estimated 11 percent to 14 percent unmet demand for all physicians over the next 12 years.[44] Critical shortages underscore the need for non-compete reform to safeguard both the accessibility and quality of healthcare for Texas residents. By

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[41] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (October 1, 2024) (Statement of Jeff Burdett, National Federation of Independent Business).

[42] Andis Robeznieks, *AMA Backs Effort to Ban Many Physician Noncompete Provisions*. (June 13, 2023). https://www.ama-assn.org/medical-residents/transition-resident-attending/ama-backs-effort-ban-many-physician-noncompete.

[43] Hearing Before the S. Comm. on Business & Commerce, 2023 Leg., 88th Interim (October 1, 2024) (Written testimony of Dr. Tilden Childs, Texas Medical Association).

[44] Texas Department of State Health Services, *Workforce Supply and Demand Projections*. https://healthdata.dshs.texas.gov/dashboard/health-care-workforce/hprc/workforce-supply-and-demand-projections.

addressing these needs, Texas can protect healthcare providers, and strengthen the overall quality and accessibility of care for patients.

Conclusion and Recommendations

In light of the ongoing healthcare labor shortage and recent federal court rulings surrounding the Federal Trade Commission's Final Non-Compete Rule, it is incumbent on Texas lawmakers to take action. As such, the Committee recommends the Legislature consider:

- Establish clear and consistent criteria for the enforcement of non-compete agreements in the healthcare industry to protect healthcare providers' autonomy and freedom to provide care without undue interference.