

DRAFT

UTILITIES ADVISORY COMMISSION MINUTES OF MARCH 7, 2007

CALL TO ORDER

Chairman Melton called to order at 7:00 pm the regular scheduled meeting of the Utilities Advisory Commission.

Present: John Melton, Dexter Dawes, George Bechtel.

ORAL COMMUNICATIONS

NONE

APPROVAL OF THE MINUTES

Approval of the minutes of Feb. 7 and Special Meeting of Feb. 12:

Bechtel: Moved approval, Melton Seconded.

AGENDA REVIEW

It was requested that Item #3 on the agenda be moved to Item #1.

Dawes had two items of concern:

- 1) There seems to be a disconnect between projected reserves on pg. 3 versus the 5 year forecast.

2) Question on Item #1: Regarding the cost risk encapsulated for each of the reserves. For example, why on the gas side is 25% unhedged, and yet our risk is only 1.7 million (in the text it shrinks to 1.8 million). This seems very small given the huge changes in pricing in gas.

It was agreed that these questions would be addressed later in the meeting.

REPORT FROM COMMISSION MEETINGS/EVENTS

NONE

UTILITIES DIRECTOR REPORT

Tom Auzenne, Assistant Director, Customer Support Services, presented the Director's report in the absence of Valerie Fong:

- 1) The Emergency Water & Storage Final EIR was approved by Council on March 5.

- 2) The City of Palo Alto Utilities' Residential Energy Assistance Program (REAP) was selected by California Municipal Utilities Association (CMUA) to receive an award in the Community Service Resource Efficiency category for a small Utility.

- 3) On Feb 12 the Council approved a new set of master agreements with gas suppliers to facilitate the city's natural gas laddering purchase strategy. We now have six suppliers, an increase from the previous three. The suppliers are: ConocoPhillips, Coral Energy, Sempra Energy, BP Energy, JPMorgan Chase, and Powerex. Council is scheduled to review and possibly approve a new set of electric master agreements in the Apr/May timeframe.

- 4) Hydro conditions for this season continue to be below average in the Sierra. Melton asked if the percentage of 70 – 75% percent below average that he had read in the newspaper was correct. Shiva Swaminathan said yes, the CVP system is at 70 – 75% and the Collierville area is slightly less at 70%.

UNFINISHED BUSINESS

Two items of unfinished business:

- 1) Rosenbaum had inquired as to what the overhead costs were on a percentage basis for the PA Green Program. Tom answered that 4% of the average 11.4% cost per kWh goes to overhead (marketing and administration). This is 4% of green power, not of all sales.

- 2) A request was made for clarification of cost drivers at the February Commission meeting. Shiva Swaminathan, Senior Resource Planner, made a presentation outlining the individual cost drivers in the electric and gas supply budgets. In answer to a question by Commissioner Bechtel, it was explained that the \$2 million budget on supply funded incentives comprised of energy efficiency incentives, SB1 solar incentives, and local cogeneration incentives. Cost of PA Green purchases were also included in this category. Commissioners thanked staff for the presentation.

NEW BUSINESS

ITEM 1: INFORMATION ITEM: (ITEM 3 ON AGENDA)

Quarterly Risk Management Report

Karl Van Orsdol, Manager, Energy Risk, summarized the results from the Quarterly Risk Management Report for Second Quarter of FY 07/08. He noted that the City's market exposure was low, down to \$11.3 million dollars for electricity and no exposure for gas. The credit rating of the City's counterparties is excellent. Van Orsdol also noted that the Value at Risk for the gas portfolio was now within the benchmark figure of 10% of end of year Supply Reserve Levels, due largely to a slow increase in the last two quarters in the level of the Supply Reserve.

ITEM 2: INFORMATION ITEM: (ITEM 1 ON AGENDA)

Annual Risk Assessment for Reserves

Van Orsdol noted that the Annual Risk Assessment for Reserves represents a "mid-term" assessment of the risks faced by the City in managing its electric and gas portfolio. The Quarterly Report, just given, assesses the risks for the 12 months succeeding December 31, 2006. The

annual assessment assesses the risks for the 12 months following the end of the fiscal year, that is the twelve months of July 1, 2007 to June 30, 2008. The long term risks, 18 months to four years out, are estimated through an assessment of costs and serve as a starting point for minimum and maximum reserve levels. Because the potential volatility of prices and other exogenous events could dramatically alter the risk levels, the Annual Assessment could change during the year if required. The risk levels for electricity are within the minimum/maximum levels. For gas, the annual assessment was less than that estimated at the end of the fiscal year, although both were below the minimum levels. This strongly suggested that gas reserve levels will need to increase in the long term to cover risks.

ITEM 3: INFORMATION ITEM: (ITEM 2 ON AGENDA)

Revenue Requirement Changes FY2007-08 and FY2008-09

Water:

Lucie Hirmina, Manager, Utility Rates, explained that customer water usage has been flat or declining. San Francisco Public Utilities Commission (SFPUC) prices are the best estimate to date, but may still change. In addition, \$8.5 million will be returning from closed CIP projects to the WRSR, which will be used to fund a portion of the City Emergency Supply in FY 2008-09. The cost of the project including land is estimated to be approximately \$40 million.

UAC members had comments and concerns regarding projected magnitude of this funding and Tom Marshall, Assistant Director, Resource Management, explained that the figures are preliminary. The commissioners indicated that they will wait to see the final figures and the financing effect.

Another issue was raised by Melton about the timing of the increase in the wholesale water.

Hirmina stated that the reserve could handle a certain amount of change, but if it was a large increase, adjustments may have to be made later. The 10 percent increases for FY 2007-08 and 2008-09 reflect these uncertainties and the desire to have money in reserves to handle cost contingencies.

Auzenne provided information that in April, there will be a change in the rate structure for water and gas and a customer charge will be introduced to collect some of the fixed costs.

Melton agreed this was "the right way to go," and suggested that the entire distribution cost be fixed, as it does not vary with usage, "but it would be large".

Dawes asked whether other cities were proposing for their rate increases, or if it was too early to tell. Hirmina clarified that increases were projected, but the magnitudes were unknown at this time.

Bechtel raised the concern about General Fund Transfers from the Water Fund given the fact that sales are flat usage as a percentage of revenue in water comparing to Gas fund. Hirmina clarified that the method to calculate was not percentage of revenue, but currently a 3% annual increase from the prior fiscal year and that there is an RFP issued for another study.

Melton asked for further comments and hearing none moved to next item.

Gas:

Melton questioned if reserves were growing too rapidly, based on 9.5 and 9.1 percent increases for the next two years. Hirmina clarified that the FY 2007-08 the increase will be to cover distribution costs, while FY 2008-09 the increase will be for the supply FY 2008-09. Increases will be reviewed again next year.

Melton questioned why water rents were higher than in gas. Marshall and Auzenne clarified that water facilities occupy more land space than gas facilities.

Melton asked for further comments and hearing none moved to next item.

Wastewater:

Melton commented that there are no rate increases proposed for the next two years and Hirmina confirmed this.

Melton asked for further comments and hearing none moved to next item.

Electric:

Dawes questioned the level of increase, as E-SRSR level was dropping rapidly and would be below risk assessment levels in out-years. He noted that its level in FY 06-07 was high, and questioned if there is a chance for more wholesale revenue. Hirmina clarified that the future was uncertain, and the FY 2008-09 rate increase may change if hydro conditions or future risks change.

Bechtel questioned whether the Broadband RFP was being funded from Dark Fiber.

Marshall clarified it was coming from the General Fund.

No further questions on the electric.

Meeting adjourned at 8:45 p.m.

Respectfully submitted,

Melody Vega

City of Palo Alto Utilities