TO: HONORABLE CITY COUNCIL
FROM: CITY MANAGER DEPARTMENT: UTILITIES
DATE: JULY 8, 2002 CMR:284:02

SUBJECT: APPROVAL OF AMENDMENT NUMBER 2 TO CONTRACT NUMBER C2138656 TO INCREASE THE CONTRACT AMOUNT WITH FLYNN AND ASSOCIATES FOR ELECTRIC REGULATORY AND TECHNICAL ASSISTANCE BY $75,000 FOR FISCAL YEAR 2002-03 AND APPROVAL OF AGREEMENT WITH THE CITY OF ALAMEDA DOING BUSINESS AS POWER AND TELECOM FOR REIMBURSEMENT OF COSTS IN FISCAL YEAR 2001-02 AND FISCAL YEAR 2002-03

RECOMMENDATION

Staff recommends that Council authorize the Mayor to:

(1) Execute Amendment No. 2 to contract No. C2138656 with Flynn and Associates for related, additional but unforeseen assistance in electric regulatory and technical issues by $75,000 in FY 02-03; and

(2) Execute An Agreement with the City of Alameda (Agreement) that allows for the reimbursement of $75,000 for work done under the Flynn contract for work in FY 01-02 and up to $75,000 for work to be done under the Flynn contract in FY 02-03.

BACKGROUND

On April 16, 2001, a request for proposals (RFP) was sent to eighteen consulting firms known to offer expertise in regulatory and other technical areas. The RFP was seeking assistance to the City in three major areas: electric legislative and regulatory; gas legislative and regulatory; and market assessment. Five firms responded to the RFP with written proposals and the City’s selection panel interviewed four firms. Three firms were
selected to deliver the desired services. To assist in gas legislative and regulatory issues, Navigant Consulting Inc. and Interstate Gas Services, Inc. were retained. Flynn & Associates and Navigant Consulting were selected to provide services related to electric regulation and technical areas.

The City retained Flynn & Associates as the prime consultant to assist staff in the electric regulatory and technical area. The City signed a contract with Flynn & Associates (CMR:320:01) for a total contract amount of $430,000 ($150,000 in FY 01-02, $150,000 in FY 2002-03, and $130,000 in FY 2003-04).

Specifically, Flynn & Associates was hired to provide the services in the following task areas:

- **Task 1** – Monitor and analyze California Independent System Operator (CAISO), Federal Energy Regulatory Commission, California Energy Commission, and Pacific Gas and Electric grid planning proceedings and, based on discussion with staff, represent the City’s interest in these proceedings;
- **Task 2** – Assist City regulatory staff to develop strategies and positions to deal with critical issues related to these proceedings;
- **Task 3** – Assist City in its effort to improve reliability in the Greater Bay Area by joining with other municipal utilities, if feasible, and advocating the need for higher transmission planning standards and building of additional transmission facilities;
- **Task 4** – Assist City in developing long-term solutions for its transmission needs especially needed after the existing interconnection agreements (IA) expire (this would include any unforeseen regulatory proceedings(s) that may affect the City); and
- **Task 5** – Provide the City with miscellaneous electric regulatory consulting services.

Flynn & Associates satisfactorily provided the contracted services throughout 2001, but additional support was required to respond to changes and risks that the City was exposed to. The dynamic regulatory environment necessitated that Palo Alto protect its interest and seek coordination and cooperation with other similarly situated entities, such as the Northern California Power Agency (NCPA), Silicon Valley Power, and the Cities of Alameda and San Francisco. Additional regulatory issues in the areas of transmission reliability into the Bay Area and cost increases related to future electric market structure designs exposed the City to great risk. The statewide structural problems that led to extremely high market prices in 2000 and 2001 persist amid a lack of coherent state or national energy policy. Additional support from Flynn & Associates under Tasks 1 and 2 was sought to monitor, analyze, coordinate and intervene in additional issues and areas.

At the same time, the California Public Utilities Commission began to be interested in ensuring adequate transmission in the state, creating an opportunity to increase the City’s
ability to influence those decisions. These activities increased the need for support from Flynn & Associates under Tasks 3 and 4.

On March 18, 2002 the City amended the agreement with Flynn & Associates (CMR:177:02) and increased the contract amount by $150,000, of which $75,000 was to be utilized in FY 2001-02 and $75,000 was to be utilized in FY 2002-03.

DISCUSSION

Since 2001, the City has faced an increased level of regulatory challenges related to providing low-cost and reliable electric services to its customers. These include working with NCPA to find a replacement to the IA, and the California Independent System Operator’s Market Design 2002 proposal, which may expose the City to high local congestion costs. Therefore, the City needs additional resources to monitor the various proceedings affecting its electric utility business.

At the same time, the City realizes that there are many areas of common concern with other entities. Therefore, some of the work being performed under this contract also benefits the City of Alameda. Staff has negotiated an agreement with Alameda (Attachment B) to allow for reimbursement of the increase in contract costs being requested in this CMR.

RESOURCE IMPACT

Additional funds of $75,000 needed for this recommended increase will be absorbed within the Electric Fund operating budget. These funds and up to an additional $75,000 will be reimbursed through the agreement with Alameda. The net resource impact is therefore net revenue of $75,000 beyond the budgeted costs of the Flynn contract.

POLICY IMPLICATIONS

This recommendation is consistent with the Council approved Utilities Strategic Plan. Specifically, this recommendation supports Strategy 2; Prepare a supply cost advantage compared to the market price. Key tactics to support Strategy 2 are to “Investigate partnerships, alternative sources and projects to secure low-cost, reliable transmission for commodity supplies” and “To manage exposure to energy commodity price risk.”
ENVIRONMENTAL REVIEW

These services do not constitute a project for the purposes of the California Environmental Quality Act.

ATTACHMENTS

B: Agreement between City of Palo Alto and the City of Alameda
C: Amendment No. Two to Contract No. C2138656

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