TO:           HONORABLE CITY COUNCIL

ATTENTION:    FINANCE COMMITTEE

FROM:         CITY MANAGER        DEPARTMENT: UTILITIES

DATE:         OCTOBER 1, 2002          CMR: 398:02

SUBJECT:      REQUEST FOR THE APPROVAL OF ELECTRIC PORTFOLIO
              PLANNING GUIDELINES FOR THE LONG-TERM ELECTRIC
              ACQUISITION PLAN (LEAP)

RECOMMENDATION

The Utilities Advisory Commission and staff recommend that the City Council approve
seven Electric Portfolio Planning & Management Guidelines to guide staff in developing
and managing the City’s Long-term Electric Acquisition Plan (LEAP).

PROJECT DESCRIPTION

The City has taken a number of steps to meet the energy deficit expected to begin at the
start of 2005. The City Council approved four Primary Portfolio Planning Objectives on
November 13, 2001 (CMR:425:01) to guide the development of strategies to fill this
energy deficit:

1. Ensure low and stable electric supply rates for customers.
2. Provide superior financial performance to customers and the City by maintaining a
   supply portfolio cost advantage compared to market cost and the retail supply rate
   advantage compared to PG&E.
3. Enhance supply reliability to meet City and customer needs by pursuing
   opportunities including transmission system upgrades and local generation.
4. Balance environment, local reliability, rates and cost impacts when considering renewable resource and energy efficiency investments.

To further facilitate the development of specific recommendations to fill the post-2004 energy deficit, staff developed seven LEAP Planning & Management Guidelines based on the four Primary Objectives.

**BOARD/COMMISSION REVIEW AND RECOMMENDATIONS**

The UAC discussed six draft LEAP Guidelines at its June 5, 2002 meeting. The Commission’s input during that meeting was incorporated into developing seven guidelines for its consideration at its August 7, 2002 meeting. After making minor changes to the wording of the guidelines, the UAC unanimously supported the proposed LEAP Guidelines.

Guideline #6 relates to investments in renewable energy technologies. The guideline proposes that Palo Alto purchase an amount of new renewables equal to 10% of the total annual energy needs by the year 2008. One item that the UAC wished to bring to the attention of the Council is that the State of California’s definition of renewables excludes large hydroelectric power plants (of capacity greater than 30 MW). The UAC noted that the common-sense definition of renewables includes hydroelectric power and that, if this source were included in the calculation of renewables content in the electric portfolio, the renewables fraction for Palo Alto would be approximately 45% in an average hydro year even without new investments in renewables as required under Guideline #6.

**POLICY IMPLICATIONS AND UTILITIES STRATEGIC PLAN**


**RESOURCE IMPACT**

See Attachment B (UAC Report on the LEAP Guidelines) for resource impact. The risk of not approving the LEAP Guidelines at this time is that staff will not have the Council direction and parameters to guide the pursuit of resource acquisitions to fill the post-2004 resource deficit.

**ATTACHMENTS**

A. Proposed Long-term Electric Acquisition Plan Guidelines
B. August 7, 2002 Report to the UAC: Request for the Approval of Electric Portfolio Planning Guidelines for the Long-term Electric Acquisition Plan (LEAP)
C. Minutes from the August 7, 2002 UAC meeting
Proposed Long-term Electric Acquisition Plan (LEAP) Guidelines

**Guideline 1: Electric Portfolio Dependence on Western** – While maintaining the flexibility to adopt favorable ‘custom products’ offered by Western, manage a supply portfolio independent of Western beyond the Base Resource Contract.

**Guideline 2: Hydro Risk Management** – Manage hydro production risk by:
A. Planning for an average hydro year on a long-term basis;
B. Diversifying to fossil and/or renewable generation technologies; and
C. Maintaining adequate supply rate stabilization reserve.

**Guideline 3: Market Risk Management** – Manage market risk by adopting a portfolio strategy for electric supply procurement by:
A. Diversifying energy purchases across commitment date, start-date, duration, suppliers, pricing terms & fuel sources;
B. Targeting additional thermal plant ownership/investment commitment at ~25 MW but in no event more than 50 MW;
C. Maintaining a prudent exposure to changing market prices by:
   1. Procuring resources at fixed price for at most 90% of expected load for 2 or more years out, assuming average hydro conditions; and
   2. Procuring resources at fixed price for at most 75% of expected load for 5 or more years out, assuming average hydro conditions; and
D. Avoiding contract-based fixed price energy purchases (except for contracts for renewable resources) for durations greater than 10 years.

**Guideline 4: Reliable & Cost Effective Transmission Services** – Ensure the reliability of supply at fair and reasonable transmission cost by:
A. Supporting, through political and technical advocacy and/or direct investment, the upgrading of Bay Area transmission to improve reliability and relieve congestion;
B. Participating in transmission market design to ensure that market design results in workable competitive markets & equitable cost allocation;
C. Pursuing the option of forming and/or joining a Public Power Transmission Control Area to increase control over transmission operations and related costs; and
D. Ensuring PG&E honors the Stanislaus Commitments by providing to us firm-transmission rights or equivalent.

**Guideline 5: Local Generation** – Monitor the potential of local generation options to meet customer needs, improve local reliability, minimize congestion and wheeling charges, and stabilize/reduce costs.
Guideline 6: Renewable Portfolio Investments – The City shall continue to offer a renewable resource-based retail rate for all customers who want to voluntarily select an increased content of renewable energy. In addition to the voluntary program, the City shall invest in new renewable resources to meet the City’s sustainability goals while ensuring that the retail rate impact does not exceed 0.25 ¢/kWh on average. Pursue a target level of new renewable purchases of 10% of the expected portfolio load by 2008. The contracts for investment in renewable resources not to exceed 30 years in term.

Guideline 7: Electric Energy Efficiency Investments – Offer quality Public Benefits programs, utilizing funds collected through the 2.85% Public Benefits charge embedded in electric retail rates, to meet the resource efficiency needs of customers. Additional funding for cost-effective programs will be recommended as appropriate. Pursue these investments by:

A. Providing expertise, education and incentives to support cost-effective customer efficiency improvements;
B. Demonstrating renewable and/or alternative generation technologies and new efficiency alternatives; and
C. Providing rate assistance and efficiency programs to low-income customers.