

Agenda Report

April 26, 1999

To: City Council
Through: Deregulation Committee
From: City Manager
Subject: Public Hearing on 1) approval of a Direct Access phase-in schedule commencing on January 1, 2000 for all customer classes and to be completed by July 1, 2002; 2) approval of nonbypassable generation-related transition charges, which are allowed under Public Utilities Code Section 9603; 3) approval of Direct Access Regulation No. 22; 4) direct the City Attorney to prepare an amendment to the Light and Power Rate Ordinance establishing a "Direct Access Energy Credit," a "Direct Access Meter" charge, and "Virtual Direct Access Energy" rates.

RECOMMENDATION:

It is recommended that the City Council 1) approve a Direct Access phase-in schedule commencing on January 1, 2000 for all customer classes and to be completed by July 1, 2002; 2) deem the Stranded Investment Surcharge and the uneconomic portion of the Energy Cost Adjustment Charge to be nonbypassable generation-related transition charges, which are allowed under Public Utilities Code Section 9603(b); 3) approve the Direct Access Service Regulation No. 22, attached in substantially final form, to govern the implementation of Direct Access in Pasadena; and 4) direct the City Attorney to prepare an amendment to the Light and Power Rate Ordinance establishing a "Direct Access Energy Credit" and a "Direct Access Meter Charge," for Direct Access customers that choose an alternate energy service provider, and "Virtual Direct Access" rates for Pasadena energy customers that choose market based rate options.

BACKGROUND:

At a public hearing held on November 18, 1996, the City Council approved "Direct Access between electricity suppliers and Pasadena's electric customers in accordance with a phase-in schedule to be adopted at a later time" (Attachment A). Staff has prepared Direct Access Service Regulation No. 22 (Attachment 1) and the above recommendations to offer Pasadena's electricity customers a choice of energy service providers starting January 1, 2000.

The Pasadena Water and Power Department currently provides both the electrical energy (energy) and the distribution network necessary to deliver the energy to the customer's site (distribution). Electric deregulation in California currently applies only to the energy part of the electric industry. Pasadena will continue to provide **all** customers with safe, reliable, and low-cost distribution services, while allowing a choice of energy service providers (ESP). Of course, the Water and Power Department will continue to be an ESP in Pasadena, and it will have to compete for the patronage of its current energy customers. This competition among ESPs should lead to lower energy prices for Pasadena customers.

Electric deregulation was established in California through AB1890, which was signed into law in September 1996. AB1890 focused on investor-owned utilities (IOU) that are regulated by the California Public Utilities Commission, but it did have several sections that were applicable to publicly owned utilities such as Pasadena. The subject recommendations fulfill our obligations under state law and confirm Pasadena's authority to collect nonbypassable transition charges for generation-related stranded costs.

DIRECT ACCESS PLAN

Staff retained the services of R. W. Beck Inc. to assist in the development of a Direct Access plan. The recommended Direct Access Service Regulation No. 22 will serve as the plan for Direct Access in Pasadena. Regulation No. 22 is presented as Attachment 1, and a Direct Access Policy Discussion paper, which addresses the pros and cons of the Direct Access issues, is presented as Attachment 2. The following is a summary of the key features contained in Regulation No. 22:

1. **Phase-in Schedule:** The Water and Power Department will start accepting DASR applications on January 1, 2000 with Direct Access service scheduled to start on March 31, 2000. All customer classes will be eligible for Direct Access subject to metering and billing infrastructure limitations, which will be removed prior to July 1, 2002. This phase-in schedule is in compliance with phase-in requirements of Public Utilities Code Section 9602(b) (AB1890 was incorporated

into the Public Utilities Code), because Direct Access starts less than two years after the start of the phase-in for electric corporations (IOUs), and the phase-in is scheduled for completion prior to December 31, 2010.

2. **Nonbypassable Competition Transition Charges (CTC):** Pasadena's rates currently include a Stranded Investment Surcharge (SIS), i.e. Municipal Code Section 13.04.176, which is indeed a nonbypassable transition charge established to accumulate sufficient funds necessary to offset post July 1, 2002 (future) uneconomic (stranded) energy costs. Current uneconomic costs are paid through the Energy Cost Adjustment Charge (ECAC), i.e. Municipal Code Section 13.04.170. The subject recommendation would deem the SIS and the uneconomic portion of the ECAC to be generation-related transition charges as authorized by Public Utilities Code Section 9603 (a).

The purpose of the SIS is to fund the Reserve for Stranded Investment, as defined in Section 13.04.175, which will be used to pay for the City's above market costs after the CTCs expire on June 30, 2002. The SIS rate is based on the present value of the difference between the City's prudently-incurred costs of electricity from its generation-related assets/obligations and the local market price of electricity as established by a regional power pool approved by the Federal Energy Regulatory Commission (Section 13.04.175 B). These generation-related assets/obligations were approved prior to August 15, 1996 as required by Public Utilities Code Section 9604(c). The approval and expiration dates for these assets/obligations are presented in Attachments 3 and 4.

The ECAC is a rate designed to recover Pasadena's costs for fuel and purchased power. If the ECAC rate results in an over collection of costs then it is adjusted to return these funds to the ratepayers through a lower ECAC rate, and vice versa. Direct Access customers would continue to pay the ECAC, but the subject recommendation would initiate the establishment of a Direct Access Energy Credit which they would receive based on the local price of electricity as established by a regional power pool approved by the Federal Energy Regulatory Commission and their hourly usage. The subject recommendation would deem the difference between the ECAC and the Direct Access Energy Credit to be the uneconomic portion of costs associated with generation assets and obligations approved prior to August 15, 1996, as required by Public Utilities Code Section 9604(c).

This public hearing is held in accordance with Public Utilities Code Section 9603(b) to ensure the validity of these state-sanctioned CTCs.

3. **Direct Access Energy Credit:** Direct Access customers will continue to pay the currently established Pasadena electric rates, including ECAC, less a Direct Access Energy Credit as described in Item 2 above.

4. **Direct Access Meter Charge:** The subject recommendation would initiate the establishment of a Direct Access Meter Charge which would be charged only to Direct Access customers to cover the cost of the interval demand meters specified in the proposed Regulation No. 22. Interval meters record customer usage on at least an hourly basis as compared to the cumulative meters that only record total cumulative usage. The Direct Access Energy Credit will be based on hourly market prices and the hourly customer usage is required to issue an accurate credit and provide accurate price signals.
5. **Virtual Direct Access Energy Rates:** The subject recommendation would initiate the establishment of Virtual Direct Access Energy rates that would allow Pasadena energy customers to contract for various types of market based rates. Virtual Direct Access Customers would be subject to CTCs like other Direct Access customers, but they would be offered a choice of market-based rates provided by Pasadena. These market-based rates could be tied to market indices, float with caps and/or floors, or fixed for a period of time. Some rate options may be more volatile than the traditional average rates, however these rates would provide time-of-use price signals, which may benefit certain customers that can change their usage patterns. Virtual Direct Access customers would be required to pay the Direct Access Meter Charge and receive the Direct Access Energy Credit, described above as Items 3 and 4. They would also be required to select a Virtual Direct Access Energy Rate for the time period associated with the rate program.
6. **Separate Billing:** Under the proposed Regulation No. 22, Direct Access customers would receive a bill for energy from their chosen ESP and a bill for distribution services from Pasadena, including CTCs as described above. This separate billing recommendation is expected to greatly reduce credit risk to Pasadena and the number of disputes processed by Pasadena staff.
7. **ESP Approval:** Under the proposed Regulation No. 22, It is recommended that Pasadena limit its involvement in the ESP approval process to issuing a business license to any ESP whose certification/registration is in good standing with the state. If disputes or other problems reach an unreasonable level for any licensee, the license could be withdrawn. The City is not currently positioned to take on a greater regulatory role. The business license would require the ESP to accept mediation and arbitration provisions.
8. **Independent System Operator (ISO) Participation:** AB1890 established an ISO to ensure the reliable supply of electricity to all customers in a deregulated environment. On July 13, 1998 City Council approved Pasadena's participation in the ISO as a Utility Distribution Company (UDC), a Participating Generator, and a Scheduling Coordinator (SC). Pasadena's recommended direct access plan fully utilizes the ISO infrastructure and protocols to facilitate direct access in Pasadena,

as shown in Attachment 5. Pasadena will be the UDC for **all** electric customers in Pasadena. The ISO will ensure a reliable energy supply for **all** Pasadena customers, regardless of their ESP choice. Pasadena will be the SC for Pasadena energy customers only. The ESPs serving Direct Access customers in Pasadena will be required to use third party SCs. This simplifies Pasadena's role to serving only "core" customers and reduces ESP credit risk to Pasadena.

The above items represent the key policy provisions contained in Regulation No. 22. Other operational issues not discussed here are also contained in Regulation No. 22 as presented in substantial final form as Attachment 1.

FISCAL IMPACT:

While Direct Access is expected to have only a minor impact on revenues to the Light and Power Fund during the transition period ending June 30, 2002, due to the collection of CTCs, gross revenues are expected to decrease significantly in the post transition period for the following reasons:

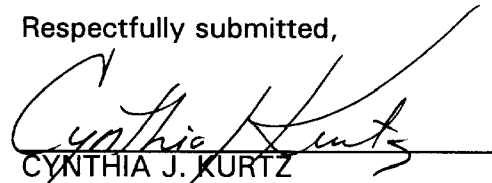
1. Pasadena's price for electricity will be lowered approximately 35.5% (system-wide average which may vary by rate class) to compete in a competitive market without a CTC.
2. While retaining all distribution customers, Pasadena will likely lose energy customers to other ESPs thus reducing gross revenues.

The Water and Power Department has developed a financial plan to accommodate this loss of gross revenue while maintaining excellent service to its remaining customers at market based rates. This plan includes the funding of the Reserve for Stranded Investment through a combination of cost savings and the Stranded Investment Surcharge. This financial plan was originally approved by City Council on November 18, 1996 and it is revised annually as part of the budget process.


The projected \$32.6 million reduction in gross revenue will reduce the base on which the general fund transfer and Utility Users Tax are calculated. The General Fund Transfer and Utility Users Tax are expected to be reduced by approximately \$1.6 million and \$2.5 million, respectively. Revenue from the Street Lights and Traffic Signals Tax (\$3.6 million per year) and the Underground Utility Special Activity Surtax (\$670,000 per year) are also expected to decrease. The total impact of this revenue reduction on the General Fund is projected at \$8.37 million.

The new costs associated with the interval demand meters required for direct access customers will be borne by the customers requesting direct access.

Respectfully submitted,


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