COUNCILMEMBER CHRIS CATE
CITY OF SAN DIEGO
SIXTH DISTRICT

MEMORANDUM

DATE: **July 28, 2020**

TO: **Mayor Kevin L. Faulconer**

FROM: **Councilmember Chris Cate**

SUBJECT: **Electric and Gas Franchise Agreement**

The City of San Diego is currently in the process of making a major decision on a new franchise agreement for electric and gas services. The current franchise agreement with San Diego Gas & Electric (SDG&E) was signed in 1970 and now, after fifty years, it is set to expire in January 2021. This represents a unique opportunity to negotiate a new agreement with a provider, one that is in the best interest of the City and San Diego ratepayers.

On July 16, 2020, the Environment Committee had the opportunity to hear from City staff, review the consultant reports from NewGen Strategies & Solutions and JVJ Pacific Consulting, LLC, (JVJ) and provide feedback on the proposed terms for the Invitation to Bid (ITB). Since I do not serve on that Committee, I am providing my thoughts, comments, and suggestions in this memorandum. I appreciate the opportunity to ask questions and provide my input, and I look forward to having a robust discussion at full City Council.

Minimum Bid & Fees

1. The minimum bid amount has increased significantly since the franchise agreement from 1970. The \$62 million minimum bid is much higher than the \$50,000 required back in 1970. Are there other cities who have required such a high minimum bid amount other than Long Beach?
2. The JVJ report also recommends that the minimum bid be paid out of shareholder funds and not charged to ratepayers. Is there precedent in requiring how and from what funding sources minimum bids should be paid?
3. As discussed at the July 16th Environment Committee meeting and included in the final motion that passed, the terms of payment should be modified so that potential bidders are able to meet the minimum bid requirement by utilizing a combination of cash and services

during the life of the agreement. Services may include infrastructure and capital improvement projects that would otherwise be paid for by the City, such as utility undergrounding, electric vehicle charging stations, median improvements, and energy efficiency projects for the City. I support this modification as recommended at the Environment Committee.

4. Undergrounding utilities is extremely important to residents. As such, the ITB should encourage potential bidders to propose ideas to strengthen and streamline undergrounding.
5. The proposed terms include a half-percent increase for the gas franchise fee. If one of the goals is ratepayer savings and relief, why would we propose to increase the gas franchise fee likely resulting in higher gas rates for ratepayers? If the purpose of the increased gas fee is to identify more funding for our Climate Action Plan, is there a way to negotiate for funding sources that would not result in higher rates for customers? There is no rationale for increasing the gas franchise fee by a half-percent.
6. The "take it or leave it" approach to this ITB does not allow for the negotiation of the best agreement for San Diego. The City should have the opportunity to see and review all bids, there should be an ability to negotiate creative elements to satisfy the needs and requirements of the City, and Council should have the ability to adopt a contract that provides the best value to the City and its residents.
7. The consultants did not recommend pursuing municipalization, yet the Staff Report outlined a "take it or leave it" approach putting the City at risk of not receiving quality bids. Should this happen and/or bidders not agree to the negotiated terms, the consultants then recommend municipalization. However, municipalization has inordinate costs and high risks associated with it. For this reason alone, the City should be wary of proceeding towards municipalization.

<u>Agreement</u>

1. <u>Length of Agreement:</u> In order to maximize the investments made by the utility company into the City and the community, the proposed term for the franchise agreement should be at least 25 years. Many factors can change within this time frame, including technological advances, increased construction costs, and more. A 25-year term is significantly shorter than the current 50-year agreement with SDG&E, but it is still long enough to encourage the successful bidder to invest in San Diego. In addition, if the proposed term is extended to 25 years, would the City be able to negotiate for more investments from the potential bidders, thereby creating better value for the City and its residents?

2. <u>Right to Purchase Clause:</u> Regarding the "Right to Purchase" clause, who would select the appraisers? Would it be the City or the Franchisee? Are there other cities, in addition to Stockton and Long Beach, who have this same type of clause? Can staff provide more specific information on how this process would work?

3. <u>Purchasing Office:</u> The proposed terms require the main purchasing office of the utility company be located within City limits to capture sales tax revenue. Would this be in conflict with the other cities who may be within the same service area? For example, if SDG&E won the bid and was servicing areas outside San Diego's city limits, could they be required to make all purchases within the City of San Diego limits, even though their service area covers more than just the City?

4. No Additional Fees: There was some discussion at the July 16th Environment Committee meeting regarding the creation of a Climate Equity Fund to be funded by an annual fee paid by the successful bidder over and above the fees currently included in the proposed terms. We should not impose additional fees than what is already outlined in the current proposed terms. Funding for projects within the low opportunity areas, as identified by the City's Climate Equity Index, can and should be prioritized through the normal budget process using the funds collected from the existing electric and gas franchise fees.

5. Oversight: The terms include periodic performance audits by third-party auditors providing for transparency and to ensure both parties are complying with the terms of the agreement. Although regular audits are usually a necessary tool to ensure good governance, utility oversight is normally reserved for the CPUC. Would these proposed audits conflict with the CPUC's authority? In addition to routine audits, I am also supportive of establishing a dispute resolution process within the agreement to avoid the potentially high cost of litigation between the utility and the City.

6. Severability: It is my understanding the CPUC needs to approve the final agreement. If the CPUC has any issues regarding elements of the agreement, what impact would that have on the overall franchise agreement?

Cost

1. Should the City choose municipalization, what are the start-up costs associated with it? How would that impact the City's General Fund?
2. The estimated range regarding capital costs to sever the SDG&E system is extremely large. The difference between the lower and upper bound is $2.23 billion. This range is too broad for the City when it comes to weighing the costs, benefits, and risks of municipalization. If the recommendation from JVJ is to municipalize if bidders don't take the proposal without material changes, we need better information to help inform our decision.

Risk

1. Even if the low and base costs scenarios hold true for municipal acquisition, there is potentially a significant amount of risk to realize some level of lower customer rates. Its worthy to note that the City has seldom pursued major projects and completed them under a "low cost" scenario.
2. The JVJ's recommendation that the City proceed with municipalization should the proposed franchises not be accepted without material changes by bidders is overly aggressive and premature. It would not be in the City or ratepayers' best interest to immediately proceed down the route of municipalization with such unknown costs and liabilities, particularly if reasonable negotiations can be made with the bidders that is agreeable to all parties.

Miscellaneous Questions:

1. JVJ's reports repeatedly cite the City of Long Beach in justifying certain proposed terms. Long Beach is cited numerous times, either as the sole example or one of just a couple

cities, in justifying certain proposed terms. Is it wise to propose terms based on the example of just one city?

2. During the Environment Committee meeting, it was presented that the City may choose to manage the distribution of revenues from Public Purpose Programs. Has staff evaluated the feasibility of managing these programs? If so, how much additional staff would be needed?
3. In the Staff Report there are multiple references to "external stakeholders" who were a part of the franchise agreement discussions. Who are these "external stakeholders"? What conclusions did they reach?
4. SDG&E asserts that should the City choose municipalization, the CCA JPA - San Diego Community Power (SDCP) - would be no longer be necessary. How does this agreement fit with SDCP?

Cc: Andrea Tevlin, Independent Budget Analyst