1.

December 7, 2009

TO: City Council

FROM: Anne Montgomery, City Manager

SUBJECT: Review of Power Purchase Agreement and Consideration of Whether to Exercise Withdrawal Rights from the Marin Energy Authority

BACKGROUND: The Marin Energy Authority ("MEA") was formed in December 2008 as a joint powers authority made up of the County of Marin and eight cities and towns, including the City of Mill Valley, to study, promote, develop, conduct, operate and manage energy and energy-related climate change programs. The MEA seeks to address climate change and the requirements of AB 32 by reducing energy related greenhouse gas emissions. The first priority of the MEA is to consider the implementation of a community choice aggregation program authorized by state law under which the MEA may secure an energy supply for customers within its jurisdiction. This program is known as Marin Clean Energy. In order to obtain this energy supply, the MEA conducted a RFP process for a full requirements energy provider who would at the minimum provide 25% of its energy supply as state certified renewable energy and also offer a deep green option for MEA customers consisting of 100% renewable energy. At this time, the state law standard for renewable energy is 20%. Twelve proposals were received with three of the proposers selected for contract negotiations.

The City Council has received briefings from Dawn Weisz, Interim Director of the Marin Energy Authority ("MEA") on the negotiation of a proposed Power Purchase Agreement by the MEA with Shell Energy North America ("SENA") or such other full requirements energy provider finally selected by the MEA Board. On November 5, 2009, the MEA Board of Directors approved the release of a final draft contract for the purchase of energy for the proposed Marin Clean Energy program for the ninety-day review period contemplated by Section 7.1.1.1 of the Marin Energy Authority Joint Powers Authority Agreement.

The draft contract was delivered to the City on November 6 in a contract package that included an overview summarizing the Power Purchase Agreement (the "PPA") which is attached. The PPA consists of three parts: the industry standard Edison Electric Institute (EEI) Master Power Purchase and Sale Agreement, the Cover Sheet that modifies specified terms of the Master Agreement, and the Confirmation that sets forth the commercial terms of the energy purchase. The PPA is the result of extensive negotiations and review by the MEA Board, the Board's Ad Hoc Contract Committee, staff, technical and legal consultants and the City Manager peer review.

In order to provide an independent review of the adequacy of the PPA and any potential risks associated with it, the Marin City Managers retained MRW & Associates to review the PPA and provide any recommendations. The final report of MRW, dated November

20, 2009 is attached for the Council's review. MRW concluded that it did not find any fatal flaws with the PPA, but identified certain financial risks to the MEA or its customers (not to its individual members) and made recommended changes to the PPA to address these risks.

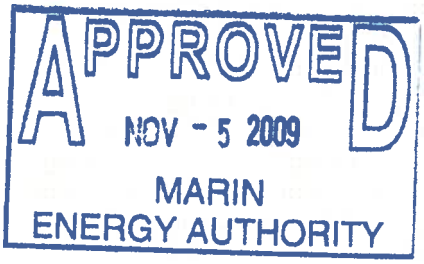
The City of Mill Valley will not be a party to the PPA. Under the Joint Powers Agreement executed by the City and the other eight parties forming the MEA, the MEA is a separate legal entity from its members. The contractual obligations and debts of the MEA are not obligations or liabilities of the member agencies. Further, Section 25 of the Cover Letter states that the MEA shall solely be responsible for all debts, obligations and liabilities accruing and arising out of the PPA and that the energy provider agrees that it shall have no rights and shall not make any claim, take any actions or assert any remedies against any of the MEA members in connection with the PPA or any transactions resulting from the PPA.

Section 7.1.1.1 of the Joint Powers Agreement requires the MEA to provide a copy of the proposed PPA to each member at least 90 days prior to the final consideration of such agreement by the Board. This 90-day review period was designed to allow each member to review the terms of the PPA and decide whether to remain a member of the MEA and participate in the Marin Clean Energy program or withdraw from the MEA. By withdrawing from the MEA, the City and its residents would not be able to participate in Marin Clean Energy.

The MEA currently has scheduled the final consideration of the PPA on February 4. 2009. At that time the MEA Board will decide whether to approve and execute the PPA. Under Section 7.1.1.1, a member must give 30 days advance written notice of its election to withdraw prior to the execution of the PPA by the MEA. Thus, under the current schedule, if the City of Mill Valley wishes to withdraw from the MEA prior to the implementation of the Marin Clean Energy program, it must provide its written notice of withdrawal by January 4, 2010.

No action is required to be taken by the City Council at this time. However, if the Council wishes to withdraw from the MEA before the execution of the PPA, it must elect at a public meeting to withdraw by no later than January 4, 2010.

marin energy
authority



November 5, 2009

TO: Marin Energy Authority Board

FROM: Dawn Weisz, Interim Director

RE: Resolution Affirming the Board's Policy that Program Agreement 1 Will Only be Approved if Customer Costs for the Light Green Energy Product Can Be At Or Below PG&E's Projected Cost. (Agenda Item #C-3, revised)

ATTACHMENTS: Resolution

Dear Board Members:

At the October 1, 2009 meeting of your Board, staff was asked to prepare a resolution affirming the Board's policy decision to set customer costs for the Light Green energy product at or below PG&E's projected costs for customers. The attached resolution is in response to this request and provides that the Board will not approve the draft power purchase agreement (referred to as Program Agreement 1) currently scheduled for approval on February 4, 2010 unless the customer costs for the Light Green energy product can be at or below PG&E's projected costs.

Recommendation: Approve resolution.

RESOLUTION NO. 2009-_____

A RESOLUTION OF THE BOARD OF DIRECTORS OF THE MARIN ENERGY AUTHORITY AFFIRMING THAT PROGRAM AGREEMENT 1 WILL ONLY BE APPROVED IF CUSTOMER COSTS FOR THE LIGHT GREEN ENERGY PRODUCT CAN BE AT OR BELOW PG&E'S PROJECTED COSTS.

WHEREAS, the Marin Energy Authority ("MEA") is a joint powers authority established on December 19, 2008, and organized under the Joint Exercise of Powers Act (Government Code Section 6500 et seq.); and

WHEREAS, MEA members include the following Marin communities: the County of Marin, the City of Belvedere, the Town of Fairfax, the City of Mill Valley, the Town of Ross, the Town of San Anselmo, the City of San Rafael, the City of Sausalito and the Town of Tiburon; and

WHEREAS, the MEA Board has conducted an RFP process and a contract negotiation process for power purchase; and

WHEREAS, the MEA Board has developed a draft Power Purchase Agreement also known as "Program Agreement 1" with potential energy suppliers; and

WHEREAS, MEA technical advisors have determined that responses to the RFP included indicative costs that would allow the Marin Clean Energy program to offer the Light Green energy project at a customer cost that is at or below the projected PG&E customer cost; and

WHEREAS, MEA's mission is to provide renewable energy, cost stability and other customer benefits.

NOW, THEREFORE, BE IT RESOLVED, by the Board of Directors of the Marin Energy Authority that MEA will not approve and execute the Power Purchase Agreement known as "Program Agreement 1" with an energy supplier until confirmed pricing can be provided that will allow customer costs to be at or below PG&E project costs.

PASSED AND ADOPTED at a regular meeting of the Marin Energy Authority Board of Directors on this 5th day of November 2009, by the following vote:

	AYES	NOES	ABSTAIN	ABSENT
City of Belvedere				
Town of Fairfax				
County of Marin				
City of Mill Valley				
Town of Ross				
Town of San Anselmo				
City of San Rafael				
City of Sausalito				
Town of Tiburon				

CHAIR, MARIN ENERGY AUTHORITY BOARD

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MEMORANDUM

to: Chair and Board Members

cc: Dawn Weisz, Interim Director

from: Greg Stepanicich, General Counsel

date: November 5, 2009

subject: Amendments to JPA Agreement and Operating Rules and Regulations (Agenda item #6)

attached: Amendment No. 1 to Marin Energy Authority Joint Powers Authority Agreement

Marin Energy Authority Operating Rules and Regulations (As Amended)

Two amendments to the Joint Powers Authority Agreement and one amendment to the Operating Rules and Regulations are being proposed. These amendments provide further clarity to the protection of individual members from the obligations and liabilities of the Authority and establish a procedure for members to opt-out of programs not involving Community Choice Aggregation ("CCA") that require financial contributions from the members. These amendments have been reviewed by the Executive Committee which recommends their adoption by the Board.

The amendments are being presented to the Board for their initial review. If the Boards finds the amendments to be appropriate, either as proposed or modified based on Board direction, staff will present the amendments for adoption at the December 3 Board meeting.

Attached to this report is Amendment No. 1 to Marin Energy Authority Joint Powers Authority Agreement. Amendment No. 1 makes two amendments to the JPA Agreement by amending Section 2.3 and adding a new Section 4.11. The amendment to Section 2.3 takes existing language from Article VIII of the Operating Rules and Regulations. This additional language makes it clear that the debts, liabilities and obligations of the Authority shall not be applied to any member unless the governing body of the member agrees in writing to assume the Authority's debt, liability or obligation.

The new Section 4.11 establishes a procedure for the approval of programs not involving CCA that require financial contributions by individual members to become operational. Such programs can only be approved by a majority vote of the full membership of the Board subject to the right of any member who votes against the program to opt-out of the program and avoid the financial

MEMORANDUM

contribution. The Board must provide at least 45 days prior written notice to each member before it considers the program for adoption at a Board meeting. The Board also must provide written notice of the adoption of the program to each member within 5 days after the Board adoption. These notices are required to be sent to the governing body and the chief administrative officer, city manager or town manager of each member. Any member voting against the approval of the program may elect to op-out of participation in the program by providing written notice of this election to the Board within 30 days after the Board approves the program. By timely exercising the opt-out election, a member will not have any financial obligation or liability for the conduct of the program.

We also recommend that if the Board adds the new Section 4.11 to the JPA Agreement, it also add the same language to Article VII of the Operating Rules and Regulations. Attached are amended Operating Rules and Regulations that show by redlines the changes that would be made to Section 2(h) and Section 4 of Article VII.

Recommendation: Approve changes as recommended by the Executive Committee.

MARIN ENERGY AUTHORITY

OPERATING RULES AND REGULATIONS

(As Amended)

ARTICLE I

FORMATION

The Marin Energy Authority (the "Authority") was established on December 19, 2008 pursuant to the execution of the Marin Energy Authority Joint Powers Agreement (the "Agreement") by the County of Marin, the Town of Fairfax and the Town of Tiburon. The Initial Participants in the Authority who executed the Agreement within 180 days of the establishment of the Authority are the following:

The members of the Authority are referred to as Party or Parties in these Operating Rules and Regulations. As defined by the Agreement, these Operating Rules and Regulations consist of rules, regulations, policies, bylaws and procedures governing the operation of the Authority.

ARTICLE II

PURPOSES

The Authority is formed to study, promote, develop, conduct, operate, and manage energy and energy-related climate change programs, and to exercise all other powers necessary and incidental to accomplishing this purpose. These programs include but are not limited to the establishment of a Community Choice Aggregation Program known as Marin Clean Energy in accordance with the terms of the Agreement.

ARTICLE III

BOARD OF DIRECTORS

Section 1. The Authority shall be governed by a Board of Directors composed of one representative of each of the Parties. The Board may delegate specified functions or actions to the Executive Committee or other committees that may be established by the Board. The governing body of each Party shall appoint and designate in writing to the Authority one regular Director who shall be authorized to act for and on behalf of the Party on all matters within the power of the Authority. The governing body of each Party also shall appoint and designate in writing to the Authority one alternate Director who may vote on all matters when the regular Director is absent for a Board meeting. Both the Director and the Alternate Director shall be members of the governing body of the Party.

Section 2. Each Director and Alternate Director shall serve at the pleasure of the governing body of the Party that the Director represents and may be removed as Director or Alternate Director by such governing body at any time.

Section 3. A Director may be removed by the Board for cause. Cause shall be defined for the purposes of this section as follows:

a. Unexcused absences from three consecutive Board meetings.

b. Unauthorized disclosure of confidential information or documents from a closed session or the unauthorized disclosure of information or documents provided to the Director on a confidential basis and whose public disclosure may be harmful to the interests of the Authority.

Written notice shall be provided to the Director proposed for removal and the governing body that appointed such Director at least thirty days prior to the meeting at which the proposed removal will be considered by the Board. The notice shall state the grounds for removal, a brief summary of the supporting facts, and the date of the scheduled hearing on the removal. The Director proposed for removal shall be given an opportunity to be heard at the removal hearing and to submit any supporting oral or written evidence. A Director shall not be removed for cause from the Board unless two-thirds of all Directors (excluding the Director subject to removal) vote in favor of the removal.

Section 4. If at any time a vacancy occurs on the Board, for whatever reason, a replacement shall be appointed by the governing body of the subject Party to fill the position of the previous Director within ninety days of the date that such position becomes vacant.

ARTICLE IV

OFFICERS AND TERMS OF OFFICE

Section 1. There shall be a Chairperson, a Vice-Chairperson, a Secretary and a Treasurer.

a. Chairperson. The Chairperson of the Authority shall be a Director. Duties of the Chairperson are to supervise the preparation of the business agenda, preside over Authority meetings, and sign all ordinances, resolutions, contracts and correspondence adopted or authorized by the Board. The term of office of the Chairperson shall be for one year.

b. Vice-Chairperson. The Vice-Chairperson shall be a Director. The Vice-Chairperson shall perform the duties of Chairperson in the absence of such officer. The term of office of the Vice-Chairperson shall be for one year.

c. Secretary. The Secretary will supervise the preparation of the meeting minutes and the maintenance of the records of the Authority. The term of the Secretary shall be for one year. The Secretary does not need to be a Director.

d. Treasurer and Auditor. The Treasurer shall have custody of all the money of the Authority and shall have all of the duties and responsibilities specified in Government Code Section 6505.5. The Treasurer shall report directly to the Board and shall comply with the requirements of treasurers of incorporated municipalities. The positions of Treasurer and Auditor may be combined into one position known as the

Treasurer/Auditor of the Authority. Neither the Treasurer nor the Auditor needs to be a Director. The term of the Treasurer and Auditor shall be for one year. The Board may transfer the responsibilities of the Treasurer and Auditor to any person or entity permitted by law.

e. Initial Terms of Office. Notwithstanding the one-year term generally established for officers above, the terms of the initial officers elected by the Board shall not expire until the annual meeting of the Board held in June 2010.

f. No Term Limits. There are no limits on the numbers of terms that an officer of the Authority may serve.

g. Removal. An officer of the Board shall be subject to removal with or without cause at any time by a majority vote of the full Board.

h. Committees. The Executive Committee and all other Committees of the Board shall be selected as provided by Sections 4.6 and 4.7 of the Agreement. Each duly established Committee may establish any Standing or Ad Hoc Committees determined to be appropriate or necessary. The duties and authority of all Committees shall be subject to the approval and direction of the Board.

i. Committee of the Whole. To allow full participation by Board members at meetings of Standing Committees, each Standing Committee meeting except the Executive Committee also shall be noticed as a "Committee of the Whole" meeting. In the event that a quorum of Board members are present at a Standing Committee meeting, the Standing Committee will automatically convert into a Committee of the Whole. Likewise, if there is no longer a quorum of the Board present, then the Committee of the Whole will automatically convert back into a Standing Committee. The chair of the Standing Committee will serve as Chair of the Committee of the Whole. Any item acted upon by the Committee of the Whole will be considered advisory to the Board of Directors and require consideration and action by the Board of Directors at a noticed Board meeting before adoption or approval of the item.

The agenda for each Standing Committee, other than the Executive Committee, shall include the following statement:

> "This Committee may be attended by Board Members who do not serve on this Committee. In the event that a quorum of the entire Board is present, this Committee shall act as a Committee of the Whole. Any item acted upon by the Committee of the Whole will be considered advisory to the Board of Directors and require consideration and action by the Board of Directors at a noticed Board meeting before adoption or approval of the item."

ARTICLE V

MEETINGS

Section 1. Commencing in 2010, an annual meeting of the Board shall be held in June of each year to elect the officers of the Authority. The Board by resolution shall establish the date, time and meeting location of all regular meetings of the Board. Special meetings may be called upon the request of a majority of the members of the Board or by the Chairperson.

Section 2. The meetings of the Board, the Executive Committee and all other committees established by the Board shall be governed by the provisions of the Ralph M. Brown Act (Government Code Section 54950 et seq.).

ARTICLE VII

VOTING

Section 1. Voting on Authority matters shall be held in accordance with the requirements of Sections 4.9 and 4.10 of the Agreement.

Section 2. Under Section 4.10 of the Agreement, each member of the Board shall have one vote on general administrative matters and energy programs not involving Community Choice Aggregation unless otherwise provided by the Agreement or these Operating Rules and Regulations. Unless the Agreement or these Operating Rules and Regulations require a two-thirds vote, action on these items shall be determined by a majority vote of the quorum present and voting on the item except for the following matters which shall be approved only by a majority vote of the full membership of the Board:

a. The approval of the issuance of bonds or any other financing even if program revenues pay for such financing.

b. The hiring of an Executive Director and General Counsel.

c. The appointment or removal of an officer.

d. The adoption of the Annual Budget.

e. The adoption of an ordinance.

f. The initiation of litigation where the Authority will be the plaintiff, petitioner or cross complainant or cross petitioner.

g. The adoption and amendment of the Operating Rules and Regulations.

h. The approval of any program or other activity requiring financial contributions by individual Parties subject to the right of any Party who votes

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against the program or activity to opt-out of such program or activity pursuant to Section 4 of this Article.

Section 3. The approval of an Administrative Services Agreement under Section 4.13 of the Agreement for planning, implementing, operating and administering the CCA Program shall be subject to the voting requirements of Section 4.9 of the Agreement.

Section 4. The Board shall provide at least 45 days prior written notice to each Party before it considers a program or activity for adoption at a Board meeting not involving CCA that requires financial contributions by individual Parties. Such notice shall be provided to the governing body and the chief administrative officer, city manager or town manager of each Party. The Board also shall provide written notice of such program or activity adoption to the above-described officials of each Party within 5 days after the Board adopts the program or activity. Any Party voting against the approval of such program or activity may elect to opt-out of participation in the program or activity by providing written notice of this election to the Board within 30 days after the program or activity is approved by the Board. Upon timely exercising its opt-out election, a Party shall not have any financial obligation or any liability whatsoever for the conduct or operation of such program or activity.

Deleted: The voting requirements for the approval by the Board of any program or activity requiring financial contributions by the individual Parties shall be determined by future action of the Board. This action shall be in the form of an amendment to the Operating Rules and Regulations.

ARTICLE VIII

DEBTS, LIABILITIES AND OBLIGATIONS

As provided by Section 2.3 of the Agreement, the debts, liabilities and obligations of the Authority shall not be debts, liabilities or obligations of the individual Parties unless the governing board of a Party agrees in writing to assume any of the debts, liabilities or obligations of the Authority. A Party who has not agreed to assume an Authority debt, liability or obligation shall not be responsible in any way for such debt, liability or obligation even if a majority of the Parties agree to assume the debt, liability or obligation of the Authority.

ARTICLE IX

AMENDMENTS

These Operating Rules and Regulations may be amended by a majority vote of the full membership of the Board but only after such amendment has been proposed at a regular meeting and acted upon at the next or later regular meeting of the Board for final adoption. The proposed amendment shall not be finally acted upon unless each member of the Board has received written notice of the amendment at least 10 days prior to the date of the meeting at which final action on the amendment is to be taken. The notice shall include the full text of the proposed amendment.

AMENDMENT NO. 1 TO MARIN ENERGY AUTHORITY JOINT POWERS AUTHORITY AGREEMENT

1. Section 2.3 of the Marin Energy Authority Joint Powers Authority Agreement is hereby amended to read:

"**2.3 Formation**. There is formed as of the Effective Date a public agency named the Marin Energy Authority. Pursuant to Sections 6506 and 6507 of the Act, the Authority is a public agency separate from the Parties. The debts, liabilities or obligations of the Authority shall not be debts, liabilities or obligations of the individual Parties unless the governing board of a Party agrees in writing to assume any of the debts, liabilities or obligations of the Authority. A Party who has not agreed to assume an Authority debt, liability or obligation shall not be responsible in any way for such debt, liability or obligation even if a majority of the Parties agree to assume the debt, liability or obligation of the Authority. Notwithstanding Section 8.4 of this Agreement, this Section 2.3 may not be amended unless such amendment is approved by the governing board of each Party."

2. Section 4.11 of the Marin Energy Authority Joint Powers Authority Agreement is hereby renumbered as Section 4.12.

3. A new Section 4.11 is added to the Marin Energy Authority Joint Powers Authority Agreement to read:

"**4.11 Board Voting on Programs Not Involving CCA That Require Financial Contributions.** The approval of any program or other activity not involving CCA that requires financial contributions by individual Parties shall be approved only by a majority vote of the full membership of the Board subject to the right of any Party who votes against the program or activity to opt-out of such program or activity pursuant to this section. The Board shall provide at least 45 days prior written notice to each Party before it considers the program or activity for adoption at a Board meeting. Such notice shall be provided to the governing body and the chief administrative officer, city manager or town manager of each Party. The Board also shall provide written notice of such program or activity adoption to the above-described officials of each Party within 5 days after the Board adopts the program or activity. Any Party voting against the approval of a program or other activity of the Authority requiring financial contributions by individual Parties may elect to opt-out of participation in such program or activity by providing written notice of this election to the Board within 30 days after the program or activity is approved by the Board. Upon timely exercising its opt-out election, a Party shall not have any financial obligation or any liability whatsoever for the conduct or operation of such program or activity."

This Amendment No. 1 to Marin Energy Authority Joint Powers Authority Agreement was duly adopted by the Board of Directors in accordance with Section 8.4 of this Agreement on November 5, 2009.

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MRW & ASSOCIATES

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November 20, 2009

Marin Manager's Association
Attention: Matthew Hymel, Marin County Administrator
Peggy Curran, Tiburon Town Manager
Debbie Stutsman, San Anselmo Town Manager

Re: Analysis of Service Agreements and Financial Risk to MEA

Dear Mr. Hymel, Ms. Curran, and Ms. Stutsman:

As requested, MRW & Associates, LLC (MRW) reviewed copies of several documents being negotiated by the Marin Energy Authority (MEA) and Shell Energy North America (SENA)[1] related to SENA providing power to MEA for the period from 2010-2015.[2] The purpose of this examination was to identify risks faced by MEA, the member agencies that make up MEA, and the customers that would ultimately receive commodity electricity from MEA.

Based on our review, MRW does not find any fatal flaws with the Agreements. Nonetheless, we find that there are certain issues that would place financial risk[3] on MEA or its customers. We point out these risks and propose some suggested changes to the Agreements for two reasons: (1) so that policymakers can make informed decisions regarding the potential benefits and risks of the CCA (given the current form of the Agreements), and (2) to suggest ways that policymakers might choose to modify the agreements to address these risks.

It is important to understand MRW's scope of work for this assignment. Our review focused on identifying potential risks associated with the CCA program rather than enumerating the benefits of the CCA. MEA, in its Business Plan and other documents, has laid out these potential benefits. Some of these potential benefits include:

- Providing residents and businesses of Marin the opportunity to purchase 100% green power.

[1] MEA has not yet decided that SENA will be the supplier to MEA. However, SENA is in the "first position" and, as a result, MEA and SENA are negotiating the Agreements. In the memorandum, we use SENA and supplier interchangeably.
[2] MEA is considering forming Marin Clean Energy, a Community Choice Aggregation (CCA) program. For simplicity, this memo refers to MEA.
[3] By financial risk we mean the risk that customers would pay more for power than they would have otherwise had they remained with PG&E, or that MEA incur costs greater than its revenues. We note that there is, of course, upside risk—that MEA consistently provides power at a cost less than PG&E, which is MEA's intent.

- Assisting local governments meet state greenhouse gas reduction compliance requirements.
- Over the long run, potentially providing power at costs comparable to, or less than, PG&E.
- Insulating Marin power users from volatile natural gas and power commodity markets through the use of renewable energy.
- Providing local control over power procurement and ratemaking decisions.

We do not dispute these potential benefits, nor do we attempt to weigh these potential benefits against the potential risks we identify here. Such an analysis is unavoidably subjective and is more appropriately done by local policymakers, who better understand the values and concerns of their constituents. While we make some recommendations regarding possible changes to the Agreements (or potential MEA policies), creative thinkers may also come up with alternatives that address the issues in ways that better meet Marin's policy goals and risk preferences.

Approach

MRW received copies of various draft documents from MEA. The documents (jointly, the Agreements) were[4]:

- Master Power Purchase & Sale Agreement, Edison Electric Institute
- Cover Sheet, Master Power Purchase & Sale Agreement (Cover Sheet)
- Confirmation, Master Power Purchase & Sale Agreement (Confirmation)

The Edison Electric Institute Master Power Purchase & Sale Agreement is an industry standard agreement used in numerous wholesale power transactions (which is what MEA and SENA are negotiating). The proposed Cover Sheet specifies choices regarding options in the Master Power Purchase & Sales Agreement and also establishes other broad changes that define the overall goals and boundaries of the agreement. The Confirmation defines terms and conditions specific to the initial power purchase by MEA from the supplier.[5]

MRW reviewed the draft Agreements in order to understand the services SENA would provide to MEA, the allocation of risks between the two entities, and the risks that the member agencies and MEA's customers would face.[6] MRW also reviewed a presentation by MEA that outlined the key attributes of the Agreements and the goals of MEA.[7]

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[4] MRW is aware of five versions of the Agreements. The first version of the Agreement was provided to MRW by MEA. The second version is found on MEA's website: http://www.marinenergyauthority.org/key.cfm. The third version of the Agreement was a confidential draft developed by SENA and provided to MEA on October 28, 2009. A fourth version was a confidential draft provided to MRW on November 2, 2009. A fifth, the draft final Agreement, was provided via email and is dated November 5, 2009.

[5] As discussed below, MEA will sign other Confirmations with the supplier when MEA makes additional purchases.

[6] MRW cannot provide a legal opinion of the Agreements. Instead, MRW's review was based on our professional judgment and experience.

[7] http://www.marinenergyauthority.org/PDF/MEA_Presentation.pdf.

After completing our initial review of version 1 of the Agreements, MRW held several extensive conversations with representatives of MEA to clarify questions MRW had regarding the Agreements and to understand MEA's perspective regarding specific provisions of the Agreements. Conversations were also held following MRW's review of the third and fifth version of the Agreements.

MRW also requested that MEA perform several *pro forma* financial analyses using MEA's proprietary financial model so that MRW could understand the effect that different assumptions would have on the financial performance of MEA. MRW reviewed the results of these sensitivity analyses.

During the engagement, MRW found MEA staff to be responsive to our requests for information and analysis. MRW also found MEA staff to be willing to address with SENA issues identified by MRW in the draft Agreements. MRW appreciates the difficulty MEA staff faces in trying to negotiate favorable terms and conditions with SENA and to finalize the Agreements while responding to questions and concerns raised by MRW.[8]

Risks and Issues with the Agreements

MRW's initial review of the Agreements (version 1) identified a number of issues and concerns. Some of these concerns were eliminated by MEA explaining and clarifying the language of the Agreements. Others were explicitly addressed in subsequent drafts of the Agreements. We discuss below the remaining issues with the Agreements that were not clarified by MEA or addressed in subsequent drafts.

1. **Basis Risk from Point of Supply to Point of Delivery.** Under the Agreements, SENA prices its product at the Supply Point ("NP15 EZ GEN HUB"), which is a supply point in the California power market. However, MEA receives the power at the Delivery Point ("PG&E LOAD AGGREGATION POINT"). This means that MEA is responsible for all costs to deliver power from the Supply Point to the Delivery Point. MEA indicates that this risk is mitigated because MEA will receive a *pro rata* amount of Congestion Revenue Rights (CRRs) from PG&E. However, these CRRs are not all applicable to deliveries from MEA's Supply Point to its Delivery Point. MEA also states that it will purchase other CRRs to mitigate the risk of congestion between the Supply Point and Delivery Point. MEA estimates that the congestion costs between the Supply and Delivery points to be $1-$2 per MWh. These costs represent only a few percent of MEA's overall costs. However given that the current wholesale market framework in California has existed only since April 1, 2009, there is relatively little data on the volatility of either CRRs or the price differentials between the proposed Supply and Delivery Points in the Agreement.

[8] In addition, MRW has had prior professional experience with MEA's technical advisors, Navigant Consulting, and its counsel addressing the power agreements, Milbank, Tweed, Hadley & McCloy, LLP, and has found their work to be excellent.

Recommendation: While the CRRs that will be allocated to MEA upon CCA formation may be valuable, MRW believes that MEA should focus on providing clean electricity at low, stable prices to its customers and not be distracted by attempting to extract the maximum value out of the CRRs allocated to it by PG&E. Also, unless otherwise specified, CRRs are only valid for one year. Thus, under the current approach, MEA will have to purchase additional CRRs in the future, regardless of the CRRs it receives from PG&E. Given the relatively limited amount of information regarding the volatility of CRRs prices between the Supply and Delivery points, there is some risk that future CRR costs may exceed MEA's estimated costs. Therefore, we recommend that MEA explore the cost of having its supplier price its power at the Delivery Point, rather than having MEA bear the risk of delivery charges between the Supply Point and the Delivery Point. One possible way to do this would be to request pricing from potential suppliers at both the Supply Point and the Delivery Point. With that information, MEA can make an informed choice as to whether the potential revenues gained by retaining and selling unused CRRs plus the future risk of price volatility of CRRs is superior to transferring the allocated CRRs to SENA and having SENA bear the congestion cost risk between the Supply and Delivery Points.

2. **Uncertainty in customer loads.** Under its current schedule, MEA plans to sign the Agreements in early February 2010 for service of its Phase I loads, which MEA characterizes as about 20% of its ultimate potential load. At that time, MEA must either specify the quantity of renewable and non-renewable energy and other services that it will receive from the supplier or establish some other mechanism whereby its Phase I loads are met. This is a concern because if MEA over-procures, then it will have to resell its excess supplies into the market (at unknown prices) and could face significant costs (or gains) from those sales. On the other hand, if MEA under-procures, then it needs to purchase power in the future at unknown rates, which could be higher (or lower) than the fixed prices to be specified in the Agreement in February 2010.

   Recommendation: Phase I will consist of the government load of the member agencies plus some unspecified non-governmental load. Given that only around 10% of the Phase I load will be that of the MEA member agencies (which MEA assumes will not opt-out), the uncertainty in Phase I customer load is only slightly less than for Phase II. Nonetheless, MRW recommends that MEA consider ways to address the uncertainty associated with the level of opt outs. MRW suggests three approaches:

   - MEA could require its supplier to provide MEA's entire Phase I load, regardless of the level of opt-outs, at a fixed price. Under this approach, the supplier bears all volume risk rather than MEA having to pre-specify load and facing the risk of under- or over-procuring, as is currently the case in the Agreements;
   - MEA could request fixed pricing for two tranches of energy. The load for the first tranche would be much less than the expected Phase I load and would be specified prior to contract signing. The load for the second tranche would be specified after the end of the opt-out period (when MEA would have a much better idea of its total Phase I load requirements). The Supplier would, in essence, be selling MEA an option to adjust the

quantity of load in the second tranche; and

- MEA could request pricing quotes for different "deadbands" around its expected Phase I load. That is, the supplier would provide all needed power, as long as the actual load fell within the expected load plus or minus some percentage. In this case, only if the usage fell outside of that plus-or-minus band would MEA be responsible for buying or selling the excess power.

With these three pricing options, MEA decision-makers can then weigh the additional cost of having the supplier bear all the risk of load uncertainty versus the cost of MEA bearing a certain amount of the risk of the actual loads deviating significantly from the expected load.

In addition to the issues identified above, there are several outstanding issues in the Confirmation that are less important. These are addressed in Attachment 1.

Risks and Issues Facing MEA That Are Independent of the Agreements

In addition to reviewing the draft Agreements, MRW was also asked to assess, at a high level, any additional risks the MEA CCA might face. Below are MRW's findings.

1. **Uncertainty in PG&E Exit Fees.** Depending upon its ratemaking policies, MEA or MEA's customers may face financial risks due to the level of exit fees they will pay to PG&E. Under base case assumptions, the overall level of exit fees during the five-year term of the Agreements is modest, averaging 0.3¢/kWh.[9] However, if wholesale power prices are significantly (33%) lower than currently forecast (driven down by natural gas prices lower than assumed under MEA's base case), exit fees can increase by nearly an order of magnitude, up to 2.5¢/kWh. At the same time, lower gas/power prices would also reduce PG&E's rates relative to base case assumptions. Since MEA proposes to purchase power from SENA at fixed prices,[10] its costs would not decrease with lower gas/power prices. [11] Thus, under a substantially lower gas/power price scenario, MEA customers could pay between 12%-15% more than the forecasted level of PG&E rates.[12,13] Alternatively, if MEA chose to bear the CRS price risk, it would have to have credit, reserves or hedging mechanisms in place to keep its light green customers' overall electricity rates at or below PG&E's.[14]

   In assessing this risk, the key questions are: "How likely is it that gas and power prices will be below that forecasted by MEA, and for how long would such low prices would persist?"

[9] All cost and rate values presented here are based on pro forma analyses provided to MRW by MEA.
[10] The Phase I agreements reviewed here present a fixed-price product. We assume, consistent with MEA's pro forma analysis, that Phase II would likewise be at a fixed price.
[11] See discussion below regarding MEA costs that are not necessarily fixed.
[12] Percentage based on all-in rate (i.e., includes all applicable PG&E transmission and distribution charges in addition to MEA power charges and PG&E exit fees).
[13] Assumes that MEA does not mitigate CRS risk.
[14] Value based on full, post-Phase II loads.

While a quantitative assessment of power and gas price volatility is beyond the scope of this assignment, power and gas prices assumed in the low price sensitivity case have occurred in the past ten years, and given the historical volatility of the natural gas market, have a finite chance of occurring again in the next five years. Nonetheless, extraordinarily low prices are not likely to persist for multiple years in a row, meaning that a prolonged period—more than a year—of adverse market conditions is remote.

Recommendation: MEA, as a market participant, is better suited to mitigate the risk of low gas prices than are individual customers. MRW recommends that MEA explore establishing some form of hedge against high exit fees (i.e., a hedge against very low gas prices) so as to shield MEA customers from this market risk. Such action would also reduce the overall volatility of MEA customers' power prices, which is one of the stated benefits of participation in MEA.

2. **Need to Establish an MEA Departing Load Fee.** MEA's Business Plan assumes that MEA will construct renewable supply sources starting in 2011, with an expected online date of 2014. To undertake this construction program, MEA would issue debt (as is typically the case for other utilities). This effort would allow MEA to increase its level of renewable resources beyond the level assumed in the Agreements and would form the basis for MEA's renewable portfolio after the end of the Agreements. The Agreements allow MEA to undertake such a development program. MEA has indicated to MRW that it would only undertake such a construction program if it appeared to be cost-effective at the time the decision was being made. MRW believes that if MEA adds its own resources then that action has certain consequences: (1) SENA would likely have to liquidate some portion of the resources that it procured for MEA under the Agreements, with MEA customers being responsible for any losses (or benefiting from any gains) resulting from those sales and (2) MEA would have fixed debt service obligations to pay for its renewable resources. If MEA customers choose to leave MEA's service after the end of the opt-out period, then either the departing customers must pay a "Departing Load Fee" to MEA or the electric rates for remaining customers would increase.

   Note that customers choosing not to receive power from MEA during the opt-out period (two months prior to MEA providing power to two months after MEA starts providing power) **would not** be subject to any MEA Departing Load Fee. The is Departing Load Fee would be only applicable to customers who did not opt out during the four month opt-out window and then subsequently, at some later date, chose to take electric service from someone other than MEA.[15]

   Recommendation: MEA has indicated to MRW that it expects to establish a Departing Load Fee using an approach consistent with the method used by PG&E. MRW believes that MEA needs to adopt a clear policy stating (1) that it will charge a Departing Load Fee to customers that depart MEA service and (2) how MEA will determine that fee. This is critical in the case

[15] Also note that if an MEA customer returns to PG&E service after the end of the opt-out period, that customer would not continue to pay Exit Fees to PG&E; they would only have to pay Departing Load Fees to MEA.

where MEA owns its own resources.[16] MRW believes that MEA should include this policy in the Implementation Plan that it files with the California Public Utilities Commission (CPUC).

3. **CCA bonding obligation:** CCAs must post a bond that would be sufficient to cover the costs to PG&E of having to unexpectedly serve the former CCA customers in the event of CCA failure. A settlement agreement at the CPUC set forth a complex formula for calculating the required bond level. This formula is recalculated biannually so as to account for prevailing wholesale power market conditions. If the wholesale power market is unusually high (above average retail rates), then the bond amount increases to cover the cost PG&E would incur to serve the returned customers. For MEA, this could be on the order of a few million dollars, which is ten times more than is shown in the MEA budget provided to MRW. However, the high power prices that would cause a high bond requirement would also depress PG&E's exit fee and would also raise PG&E rates, which would in turn likely provide MEA sufficient headroom to handle the higher bonding requirement and keep its customers' overall costs competitive with what they would have paid had they remained with PG&E.

   Recommendation: Although MEA might face significantly higher bond requirements than shown in the budget provided to MRW, it would occur in circumstances when MEA should have the ability to cover it without undue financial stress.

Additional Policy Considerations

1. **Meaning of "Projection" to meet or beat PG&E rate.** MEA has stated that one of the benefits for customers is "Costs at or below PG&E."[17] In discussions with MRW, MEA has clarified that this condition is based on comparing the ***projected*** overall costs of MEA assuming power supply by a third party over the term of the Agreements against MEA's costs assuming power supply was provided by PG&E at MEA's forecast of PG&E's tariffed generation rate. In other words, the following inequality must occur for MEA to sign the Agreements:

   MEA Power Supply Costs + Customer Exit Fees + MEA Overhead $\leq$ PG&E Gen Rate[18]

   Of course, all of the above factors are somewhat uncertain, although MEA Power Supply Costs are less uncertain than the other factors.

   Recommendation: MRW is concerned that customers might misinterpret MEA's statements regarding the rates for the Light Green product. To avoid that, MRW recommends that MEA make it very clear that such a commitment is based on reasonable commercial efforts. This

[16] MRW believes that an exit fee policy is needed even if MEA does not develop its own renewable supply options.
[17] MEA presentation, October 2009, p. 12.
[18] MEA Power Supply Costs, Customer Exit Fees, MEA Overheads, and PG&E Gen Rate are all forecasted values in early February 2010.

would provide MEA with the flexibility it may need to meet its other policy goals (e.g., greenhouse gas reductions, greater levels of renewables, local control) even if, in one particular year or another, market pricing turns against MEA, resulting in costs to MEA customers being higher than if they were PG&E customers.

2. **Clarify MEA's rate design policies.** MEA informs MRW that it plans to keep its rate design consistent with PG&E's rate design in MEA's first year of operation. This will simplify comparisons between MEA's rates and PG&E's generation rate. However, MEA has not yet clarified how it plans to design rates after the first year of operation.

   Recommendation: MRW believes that clarification regarding rate design policies is needed. This is not to say that it is necessary to restrict MEA's rate design at the present time. However, a policy statement regarding how MEA plans to design rates would provide customers with a better understanding of how their rates might look under MEA and allow for more informed decision-making.

Points of Information

1. **MEA plans to procure power in two separate transactions: one for power to serve the Phase I load (beginning on or about June 1 2010) and one for power to serve the Phase II load (at a later date no sooner than January 1, 2011).** This means that either prices will differ for Phase I and Phase II customers or Phase I customers will have their rates change at the onset of Phase II. The Agreements being considered in this analysis only pertain to the Phase I load. According to MEA, it intends to negotiate a separate Confirmation agreement[19] with its Phase I supplier when MEA is ready to start Phase II. MEA envisions this negotiation to address primarily price but also "may consider slight revisions to the Confirm for Phase II to the extent our better information (about opt outs, operations streamlining, other lessons learned) requires revision."[20] The pro forma financial analysis provided to MRW shows the Phase II load being served on January 1, 2012, however MEA has said that depending upon market conditions, it intends to remain flexible as to the start date of Phase II, moving it forward or backward by a year (or more) so as to take best advantage of pricing in the power markets. This phase-in approach has both positive and negative aspects.[21] Since power prices are volatile, it is likely that the prices MEA receives from its supplier for Phase II will differ from its pricing for Phase I. If power prices do differ, MEA will need to decide whether it establishes similar rates for all customers or sets rates for its Phase II customers

[19] The Confirmation contains prices, quantities, and other important aspects of the agreement between MEA and its supplier.
[20] Email communication, Elizabeth Rasmussen to Mark Fulmer November 5, 2009.
[21] The positive aspects include simplifying the initial startup of MEA and negotiating a new agreement based on better understanding of opt-out risk. Negative aspects include possibly re-opening issues that were settled in Phase I, seeing wholesale power prices prior to Phase II that do not allow MEA to proceed (because its rates would not meet or beat PG&E's rates at that time) and having to negotiate with a supplier that has great deal of negotiating leverage.

different than for its Phase I customers.[22] **The phase-in approach has both benefits and risks but, on balance, it appears to be a reasonable strategy. MRW recommends that MEA limit the issues in the Confirmation that it revisits when establishing Phase II pricing and consider accepting pricing proposals from alternate suppliers.**

2. **The Agreements depend, in part, on the Scheduling Coordinator Agreement, which is not yet finalized.** The Agreements refer in several places to the Scheduling Coordinator Agreement (SC Agreement). MEA and SENA are just beginning to negotiate the terms of the SC Agreement. MEA believes that it will finalize the SC Agreement in November 2009 and also believes that the SC Agreement will not significantly affect the relative risk allocation in the Agreements. **Until MEA finalizes the SC Agreement, the degree to which costs and risks are ultimately allocated between MEA and SENA is unresolved.**

3. **Although relatively small, some MEA costs are uncertain.** MEA indicates that "Five year energy pricing will be known prior to contract signing."[23] SENA's pricing will include Resource Adequacy, non-renewable energy, RPS-compliant renewable energy, and other renewable energy. SENA's pricing will also cover power scheduling and forecasting services provided by SENA. However, SENA's pricing explicitly does not include ancillary services, net supply costs outside of the pre-determined Balanced Monthly Usage, distribution losses, and any net costs incurred by SENA to unwind positions if MEA decides to bring on its own resources. **In other words, since SENA's price is not all-inclusive, customers should be advised that there are certain costs that are not "known prior to contract signing." However, MRW expects that these "uncertain" costs will be relatively small. Also, MEA has included estimates for costs not included in SENA's price in its financial models.**

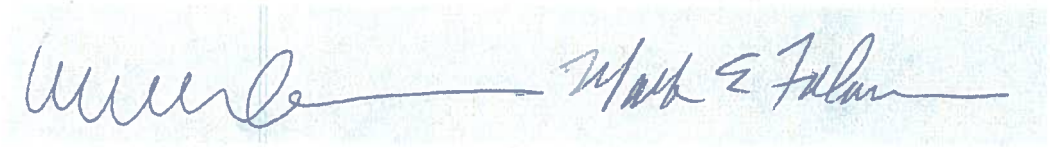
[22] This is exacerbated by the fact that the exit fees charged to CCA customers by PG&E vary depending upon when the customer begins CCA service. If MEA decides to have similar rates for both Phase I and Phase II customers, then the rates for Phase I customers might increase or decrease relative to the rates those customers saw during Phase I.
[23] MEA Presentation, October 2009, p. 36.

Conclusions

Based on our review, MRW does not find any fatal flaws with the Agreements. However, as noted above, there are certain issues that would place financial risk on MEA or its customers that should be addressed by MEA.[24]

Please give us a call at (510) 834-1999 if you have questions about this material.

Best regards,



William A. Monsen and Mark E. Fulmer
Principals

attachment

[24] By financial risk we mean the risk that customers would pay more for power than they would have otherwise had they remained with PG&E. We note that there is, of course, upside risk—that MEA consistently provides power at a cost less than PG&E.

ATTACHMENT 1

ADDITIONAL ISSUES IN CONFIRMATION

1. **Open issues in the Confirmation.** In the final draft of the Confirmation dated November 5, 2009, there are three issues that remain open (i.e., they are denoted with [square brackets]). These are (1) definition of CAISO Charges, (2) Definition of "Weighted Average Price", and the final sentence in Section 6 (regarding the party that is responsible for paying transportation charges for unit-specific purchases). The open issues all represent potential costs that will be borne by MEA customers rather than the supplier. The magnitudes of the potential costs are unknown but are likely not so great that they would endanger MEA's viability.

   Recommendation: MEA should finalize these three open issues in the following manner:

   - Definition of CAISO Charges: The open issue is whether "Imbalance charges" are included in the definition of CAISO Charges. MRW believes that the supplier should bear these imbalance charges (as is indicated in Appendix 1, section 1(c).) MEA has indicated that the final draft of the Confirmation will not include Imbalance Charges within the definition of CAISO Charges (i.e., the supplier will bear them, not MEA).
   - Definition of Weighted Average Price: The Weighted Average Price is used to determine the price that MEA would pay/receive if it uses more/less energy than allowed under the Agreement. MRW recommends that MEA clearly define how this important factor is calculated. MEA agrees, and has held this issue open awaiting the MEA load profile data necessary to better understand the weighted average price.
   - Responsibility for delivery of energy from unit-specific resources: Section 2.4 states "[For unit-specific Energy delivered hereunder pursuant to Section 2.4, **Buyer shall be liable for all costs associated with delivering Energy from the generation point (the load aggregation point) to the Delivery Point** and Seller shall assist Buyer (at Buyer's cost) with obtaining all Congestion Revenue Rights ("CRRs") required relating to the congestion from such generation point to the Delivery Point.]" (emphasis added). MEA indicates that it intends to bear the costs associated with transmitting power from any unit-specific generator approved by MEA to the Delivery Point. Per the discussion in Issue 1, above, MRW believes MEA should request pricing whereby (1) the supplier bear the costs of delivery from the unit-specific resource(s) to the Delivery Point, and (2) the supplier bears the cost of delivery from the unit-specific resource(s) to NP15 EZ Gen Hub, just as it does for all system power being supplied under the Agreements.

2. **Requirement to Supply "Baseline hourly volumes" (Section 5.2):** The Confirmation now includes a new exhibit: Baseline hourly volumes. To date, all volumes have been either monthly or annual volumes. MRW does not understand the need for providing these data, since MRW understands that all purchase obligations are on a monthly or annual basis. MEA indicates that this will be deleted.

Recommendation: MRW concurs with MEA that since no other sections of the Agreements reference baseline hourly volumes, this should be deleted.

3. **Commercially Reasonable Efforts (Sections 7.1 and 7.2):** The Confirmation now does not include a provision that the supplier will use "Commercially Reasonable Efforts" to minimize/maximize the costs/revenue associated with under-/over-use of non-renewable energy. The Confirmation states that the supplier will use Commercially Reasonable Efforts if it has to buy/sell additional renewable energy and other services (see Sections 7.3, 7.4, 8.1, and 8.2).

   Recommendation: MEA should insist that the supplier use Commercially Reasonable Efforts in the case where it must buy or sell non-renewable energy to meet MEA's loads. MEA concurs and intends to include such language in the final version.