VALLEY CLEAN ENERGY ALLIANCE

Staff Report – Item 17

TO: Valley Clean Energy Alliance Board of Directors

FROM: Mitch Sears, Interim General Manager
George Vaughn, Director of Finance & Internal Operations

SUBJECT: Update on Power Charge Indifference Adjustment (PCIA) and Energy Resource Recovery Account (ERRA)

DATE: March 12, 2020

RECOMMENDATIONS
Informational update, no Board decisions requested.

BACKGROUND
This purpose of this report is to update the Board on the most recent developments impacting the Power Charge Indifference Adjustment (PCIA), based on recent regulatory decisions and other updates.

Since December 2019, staff has provided several information updates on PCIA and PG&E to the Board and the Community Advisory Committee (CAC). This report is an update with the most recent developments.

Following are the primary activities and timeline regarding PCIA since December 2019:

- December 12: Staff Report and Presentation to Board on PCIA/ERRA
- January 24: CPUC issued Proposed Decision (PD) on PCIA/ERRA
- February 13: Presentation to Board on PCIA/ERRA
- February 20: VCE staff and regulatory counsel meet with four CPUC Commissioner's offices and staff from the CPUC Energy Division who oversee implementation of the PCIA by the CPUC
- February 27: Presentation to the CAC
- February 28: CPUC issued Final Decision on PCIA/ERRA

DECEMBER 2019 STAFF REPORT
The December 12, 2019 Board staff report provided background on the PCIA issue and laid out potential paths the exit fee rate could take, depending on final outcomes of regulatory decisions. The staff report also provided preliminary estimates of potential financial impacts to VCE.

Several PCIA projected 2020 rates were analyzed, with the worst case being approximately 4.25 cents per kWh. Also discussed in the SR was the PG&E generation rate estimate of -3% in 2020 and its impact on VCE revenue. These early estimates were based on the best forecast information available at the time.

Staff's estimate contained in the December staff report for a extreme-case scenario was a FY 2021 net loss of $3.0 million.

FEBRUARY 2020 BOARD PRESENTATION

Staff updated the Board in February 2020 with a presentation that captured the impacts of the CPUC Proposed Decision (PD) on the PG&E ERRA filing. This PD recommended a substantial PCIA increase in 2020, making it likely that PG&E will file a cap exception trigger later in 2020 due to their projected PCIA costs being significantly over the cap.

The outcome of the PD was that the PCIA would top our initial extreme-case scenario from the December staff report and that the PG&E generation rate would be moderately worse than the December projection.

The resulting analysis from the PD impacts showed VCE at a FY 2021 loss of $5.8 million, significantly worse than our prior estimate. This was due primarily to the PCIA increase and partially to the PG&E generation rate decrease.

MARCH 2020 UPDATE

On February 20th, VCE staff visited the CPUC offices in San Francisco along with regulatory counsel to directly convey the financial impacts the new PCIA would have on VCE. Staff clearly communicated the impact the volatility and sharp increase of the PCIA would have on VCE and other CCA's. As noted, the meetings included staff from four out of five commissioners and the senior leadership of the Energy Division. Staff believes the meeting was effective in presenting the CCA side of the PCIA concerns. Note: VCE was joined by senior staff from East Bay Community Energy who reinforced the impacts the PCIA decision would have.

On February 28th, the CPUC issued its Final Decision on PCIA & ERRA. This decision largely adopted the PD recommendations but did include approximately $93 million in overall PCIA reductions for PG&E (approximately 3% decrease). This $93 million reduction was one of the topics VCE and EBCE addressed in the meetings at the CPUC.

<u>Current status</u>

Based on current information, the PCIA expectation is:

- Current PCIA rate is approximately 2.7 cents per kWh
- PCIA will increase to the cap of approximately 3.2 cents on May 1, 2020
- PCIA will increase to approximately 4.6 cents (due to triggering the cap exception) later in 2020, likely to affect rates starting in Q4 2020
- The $93 million reduction earned in the overall PCIA will result in a slightly lower PCIA rate and slightly higher revenue; these impacts are being analyzed but aren't expected to be material to the forecast

Below is the FY 2021 projected financial update for VCE. Staff has opted to stay focused on FY 2021 because beyond that period the uncertainty is substantial since we have little insight into the PCIA rates for calendar year 2021 and beyond.

	FY 2021 w/ PCIA Cap Trigger
Assumptions	
PCIA - 2020	4.6 cents
PCIA - 2021	4.1 cents
2020 PG&E Generation Rate	-4%
2021 PG&E Generation Rate	+2%
Key Financial Measures	
Customer Payments - Gen Rates	$78,760
Less PCIA	($29,533)
Revenue to VCE	$49,227
Power Cost	$50,941
Operating Expense	$4,797
Net Margin	($6,433)
Cash (Unrestricted)	$6,609
Days Cash	25

POTENTIAL MITIGATION STRATEGIES

In order to mitigate the fiscal impacts listed above, staff is analyzing several policy levers for Board consideration at future meetings. Though none of the mitigation scenarios are desirable, staff believes it is important to begin a dialogue so the Board is aware of its options. The initial list of potential mitigation strategies includes:

- Increase VCE combined generation rate (generation, PCIA and Franchise Fee Surcharge) beyond PG&E's generation rates
- Temporarily lower VCE goals for renewable and/or carbon free portfolio resource mix, while still maintaining compliance with minimum State standards
- Accept the GHG-free large hydro and nuclear allocations from PG&E
- Adjust energy hedging strategies (i.e., increase potential risk to reduce costs)
- Consider merger with other CCA(s)
- Look for additional reductions in operating expense beyond those already captured

CONCLUSION

Staff has clarity about FY 2021, but due to PCIA volatility it is difficult to forecast beyond 2021.

Fiscal year 2021 will result in a negative impact on our net position and cash reserves. However, due to prudent financial planning and decisions by the Board, VCE has adequate reserves to navigate FY 2021 without using its line of credit and maintaining a positive cash balance.

If PCIA rates stabilize in calendar year 2021 and beyond, returning to closer to historical PCIA rates, then future years become more financially manageable if other major cost drivers remain relatively stable (i.e. market power costs). If, however, PCIA continues at the extremely high post-cap trigger rates, this will significantly impact VCE's business model.

Note: the March 12, 2020 Board agenda also includes the first review of the preliminary budget for FY 20/21, which is an item directly related to this PCIA update.

Attachment:
Item 14 from December 12, 2019 Board Meeting: Staff Report on Update on Power Charge Indifference Adjustment (PCIA) and Energy Resource Recovery Account (ERRA)

VALLEY CLEAN ENERGY ALLIANCE

Staff Report – Item 14

TO: Valley Clean Energy Alliance Board of Directors

FROM: George Vaughn, Finance and Operations Director, VCE
Mitch Sears, Interim General Manager, VCE

SUBJECT: Update on Power Charge Indifference Adjustment (PCIA) and Energy Resource Recovery Account (ERRA)

DATE: December 12, 2019

RECOMMENDATIONS
As this is an informational update, no Board decisions are required.

BACKGROUND
The purpose of this report is to provide background on the upcoming changes to the Power Charge Indifference Adjustment (PICA) for 2020. The information is based on the latest information available from the CPUC proceeding and analysis by CalCCA rate forecasting consultants. The CPUC is scheduled to take action on the 2020 PCIA and PG&E generation rates in mid-late January 2020. CalCCA is coordinating responses and dispute of PCIA charges that may reduce anticipated PCIA charges for 2020 – VCE is engaged with CalCCA on these efforts. Staff will provide an update to the Board at its January 2020 meeting. VCE staff presented a similar update to the VCE Community Advisory Committee at their meeting on December 5, 2019.

<u>Power Charge Indifference Adjustment (PCIA)</u>
Every customer that transitioned from PG&E to VCE is assessed an ongoing Power Charge Indifference Adjustment (PCIA) rate in their monthly bill. This is a portion of the overall generation rate that VCE charges. Assuming VCE continues to match PG&E generation rates, the higher the PCIA the lower VCE's margin.

PCIA is assessed by vintage year. The vast majority of VCE customers are 2017 vintage and always will be considered as such. There is also going to be a large swath of customers (incoming Net Energy Metering and Winters customers) who will be part of later PCIA vintages.

The current PCIA for VCE is approximately 2.70 cents per kWh. However, based on the most recent November 2017 Energy Resource Recovery Account (ERRA) update filing from PG&E, the PCIA rate for

PG&E CCA customers is very likely to increase starting in 2020, perhaps substantially, for all PCIA vintage years.

The reasons for this increase include both ongoing fluctuations in market energy prices, along with a substantial "one-time" PCIA under-collection driven by:

1. Lower "energy revenues" from sales into the CAISO, mainly due to lower prices
2. Lower customer revenue
    - Delays in implementing the 2019 PCIA
    - Used the older "system" billing determinants that under-collected for the past year
3. Less Renewable Energy Credit (REC) sales and true-up (PG&E)
4. Lower Resource Adequacy (RA) /True-up (PG&E)

The majority of VCE customers are 2017 PCIA vintage, and the weighted average PCIA rate, spread among all customer classes, is approximately 2.70 cents per kWh in calendar year 2019. With PG&E's filing, those rates could increase substantially. Some possible outcomes include:

- Increasing to the PCIA cap of approximately 3.17 cents per kWh
- Increasing to a substantially higher amount due to one-time charges, possibly as high as 4.49 cents per kWh

Additionally, 2020 PCIA vintage rates show a substantial increase for PG&E customers – to similar amounts as above – which would include the incoming Winters customers transitioning to VCE effective January 2021.

Assuming that VCE continues the practice of matching PG&E generation rates, these PCIA increases could have serious impacts on VCE's stability and growth potential. Impacts could be felt in cash flow, cash reserves, profitability, and debt covenants. These potential impacts are identified in the Analysis section of this report below.

<u>Anticipated PG&E Generation Rates - 2020</u>
Since VCE has so far matched PG&E generation rates, another factor that will have a potentially significant effect on VCE's financial outlook is the assumed increase or decrease in PG&E generation rates from the ERRA filing. The most recent outlook provided by CalCCA consultants is that PG&E's generation rates will drop approximately 3% in 2020, which also has a negative cash flow impact to VCE.

As noted above, the CPUC will take action on PG&E's 2020 rates in mid-late January 2020 in its ERRA proceeding, at which point the VCE financial model will be updated accordingly.

ANALYSIS
Currently, the PCIA and generation rates are not final. Therefore, any discussions and analysis presented in this report is not considered final and is based on best available data at this time. This will be updated as more information is gathered.

VCE staff analyzed the following three scenarios, along with several others to provide the Board with a range of potential financial outcomes for 2020 through 2022:

- Scenario 1: "As Is" base case scenario assuming no changes to VCE's current PCIA forecast that had the PCIA increasing significantly but less than the Cap in Scenario 2 below (Note: based on the data and information that became available in mid-November 2019 from PG&E and the CPUC, this scenario is presented for comparison purposes only as it is very unlikely to occur).
- Scenario 2: "PCIA to Cap" scenario assuming the PCIA rises to the CPUC cap in 2020 of 3.17 cents per kWh and remains there
- Scenario 3: "PCIA Exceeds Cap" scenario assuming the PCIA rises high enough to trigger a CPUC cap exception and goes to 4.25 cents per kWh for 2020 and down to 3.50 cents in 2021 and beyond (Note: the PCIA for 2021 and beyond decreases due to the assumption that a portion of the 2020 PCIA are "one-time" under-collections from 2019).

Following are the assumptions and impacts of each scenario:

		Fiscal Year Ended June 30, 2020		
		Scenario 1	**Scenario 2**	**Scenario 3**
		Base "As Is"	**"PCIA to Cap"**	**"PCIA Exceed Cap"**
Assumptions				
PCIA - 2019		2.7 cents	2.7 cents	2.7 cents
PCIA - 2020		2.7 cents	3.2 cents	4.25 cents
2020 PG&E Generation Rate		-3%	-3%	-3%
Key Financial Measures	**Debt Covenants**			
Change in Net Position	At least $1.00	$8,157	$7,406	$3,734
Debt Service Coverage Ratio	1.25 or greater	29	26	13
Net Position	At least $11.0 million	$15,510	$14,762	*$11,106*
Liabilities to Net Position	2.0 or less	0.51	0.54	0.71
Cash (Unrestricted)		$12,505	$12,009	$9,583
Days Cash		54	52	41
Revenue		$55,708	$54,957	$51,289
Gross Margin		$13,003	$12,252	$8,584

		Fiscal Year Ended June 30, 2021		
		Scenario 1	**Scenario 2**	**Scenario 3**
		Base "As Is"	**"PCIA to Cap"**	**"PCIA Exceed Cap"**
Assumptions				
PCIA - 2020		2.7 cents	3.2 cents	4.25 cents
PCIA - 2021		2.7 cents	3.2 cents	3.5 cents
2020 PG&E Generation Rate		-3%	-3%	-3%
2021 PG&E Generation Rate		+3%	+3%	+3%
Key Financial Measures	**Debt Covenants**			
Change in Net Position	At least $1.00	$5,368	$2,817	*($2,956)*
Debt Service Coverage Ratio	1.25 or greater	11	6	*-6*
Net Position	At least $11.0 million	$20,052	$16,769	*$7,359*
Liabilities to Net Position	2.0 or less	0.36	0.43	0.97
Cash (Unrestricted)		$14,564	$11,845	$2,947
Days Cash		59	48	12
Revenue		$57,727	$55,189	$49,480
Gross Margin		$10,156	$7,618	$1,909

		Fiscal Year Ended June 30, 2022		
		Scenario 1	**Scenario 2**	**Scenario 3**
		Base "As Is"	**"PCIA to Cap"**	**"PCIA Exceed Cap"**
Assumptions				
PCIA - 2021		2.7 cents	3.2 cents	3.5 cents
PCIA - 2022		2.7 cents	3.2 cents	3.5 cents
2021 PG&E Generation Rate		+3%	+3%	+3%
2022 PG&E Generation Rate		0%	0%	0%

Key Financial Measures	**Debt Covenants**			
Change in Net Position	At least $1.00	$8,297	$4,625	$1,661
Debt Service Coverage Ratio	1.25 or greater	18	10	4
Net Position	At least $11.0 million	$27,478	$20,551	*$8,190*
Liabilities to Net Position	2.0 or less	0.25	0.34	0.84
Cash (Unrestricted)		$21,057	$14,734	$2,917
Days Cash		83	58	12
Revenue		$62,391	$58,765	$55,904
Gross Margin		$13,180	$9,554	$6,693

**Note: All $ are in thousands of dollars.*

CONCLUSION

The impact of the potential PCIA rate increases can be substantial. Following are the key takeaways from staff's preliminary assessments:

- VCE is able to absorb the PCIA impacts of Scenario 2 without incurring additional debt or missing key covenants, although it will delay achievement of VCE's 90-day cash reserve policy and impact VCE's dividends and local project/program development.
- In Scenario 3, VCE would need to raise generation rates to maintain its financial standing. Without doing so, VCE would lose its cash reserves over time and never attain adequate levels of cash to maintain operations.
- In Scenario 3 or a comparable outcome, it is important to note that raising generation rates over those of PG&E for a limited or longer-term duration may be necessary to maintain financial reserves and stability. VCE's rates could still be kept "competitive" with PG&E even if not exactly PG&E's rates.
- CalCCA and the collective CCA efforts related to the 2020 PCIA rates are focused on correcting errors in the investor owned utilities (IOU) PCIA calculations that may moderate a small portion of the 2020 PCIA impact. In addition, the effort also includes the potential for large one time under-collection amounts (if they are valid under the CPUC PCIA formula), to be paid by CCA's over several years to spread out the payments to reduce volatility and avoid a spike in 2020.