

Economic Impact Report:

**“Adopting Community Choice
Aggregation Draft Implementation
Plan and Adopting Further
Implementation Measures”**

and

**“Adopting Community Choice
Statement of Intent”**





City and County of San Francisco

Office of the Controller - Office of Economic Analysis

Community Choice Aggregation: Economic Impact Report

May 22, 2007

Main Conclusions

San Francisco's proposed Community Choice Aggregation (CCA) process has not yet advanced to the point where a definitive economic impact statement can be made. While on the one hand, CCA could result in greater competition in San Francisco's electricity market, leading to lower prices and environmental benefits, the currently-proposed CCA plan could also create a situation where consumers pay higher energy prices than they would with PG&E. As presently drafted, the primary adverse economic impact of the proposed ordinances, and the draft implementation plan, is that they do not sufficiently insure consumers against the latter possibility.

Highlights

- The proposed ordinance and implementation plan call for a CCA supplier to "meet or beat" PG&E rate for electricity generation. However, this meet-or-beat requirement only applies during the first 60 days. The CCA supplier is also required to propose a long-term, structured rate plan for the period after 60 days, and this plan must *intend* to meet or beat PG&E's rates over the long term. CCA suppliers may either propose a generation rate that is indexed to PG&E's or one that increases at a specified, fixed annual increment over the life of the project.
- Business and residential consumers are afforded an opportunity to opt out of CCA during the first 60 days of the program. However, if the selected CCA supplier has proposed a fixed rate plan, consumers would have to estimate the future difference in rates between PG&E and the selected CCA supplier, something very difficult for the general public to do. Given the inevitable uncertainty surrounding PG&E's future rates, consumers might not have adequate information to make an informed decision on this matter. Requiring consumers to accept this uncertainty would constitute an adverse economic impact.
- In addition, the "opt out" character of the decision means that customers who are not informed about their rights, may not understand the issues, or simply take no action, will become part of CCA, whether it is in their economic interest to do so, or not.
- It is unlikely that private market participants would elect to participate in a bidding process that would require them to match PG&E's rates while relying on a significantly higher share of more costly renewable energy than PG&E.

Risk Mitigation

The risk of an adverse economic impact on consumers can be mitigated by revising the rate requirements on prospective CCA suppliers in the implementation plan:

- The plan could direct CCA suppliers to offer two tiers of service: a default service whose generation rate can never exceed PG&E's, and an optional service whose rate increases at a fixed percentage each year. This would reduce the risk, to consumers, of their rates unexpectedly rising above PG&E's rates.
- The plan could also mitigate the economic impact by allowing a free opt-out opportunity every two years, as Ohio's CCA does.

INTRODUCTION

Scope of This Report

This OEA report was written in response to the introduction of two ordinances concerning Community Choice Aggregation (CCA) in San Francisco.

San Francisco's CCA process has not yet advanced to the stage where any definitive economic impact statement can be made. A detailed economic impact assessment will not be possible until the RFP process is complete, a structured long-term rate plan has been submitted, and an opt-out penalty has been set.

The proposed implementation of CCA could lead to greater competition in the City's electricity markets, lower rates for consumers, and a greater reliance on local sources of renewable energy and conservation. Such an outcome would benefit the San Francisco economy and the global environment.

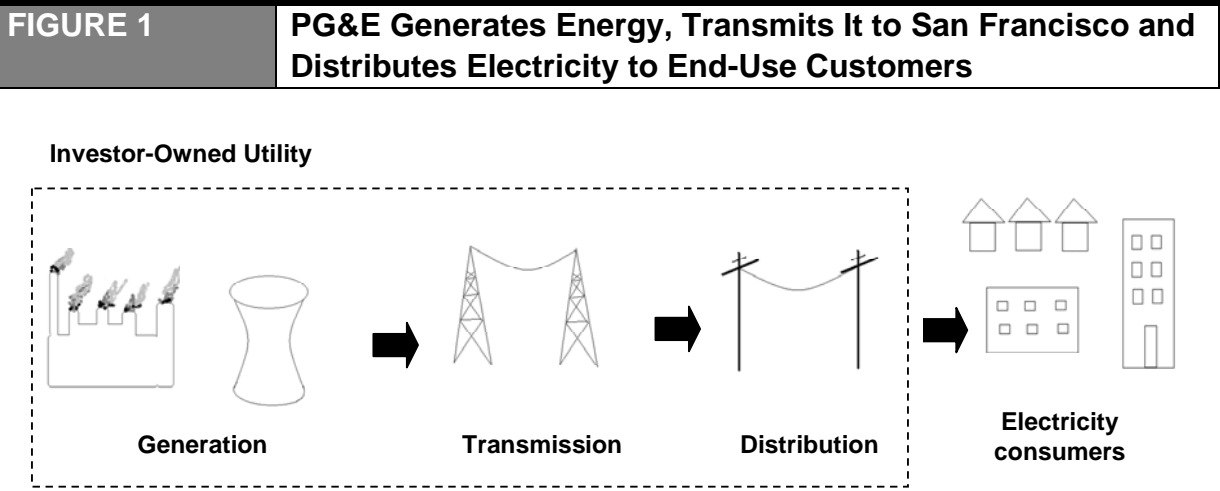
Alternatively, it could create a situation in which some consumers are unable to properly estimate future market trends, make an uninformed decision about CCA (or make no decision at all), and shift into a higher rate regime enforced by a high exit penalty. Such an outcome would have a powerful negative impact on the San Francisco economy.

At this stage, there is only a risk of an adverse economic impact. In this report, the OEA highlights some areas for concern and potential mitigation to inform the policy debate.

BACKGROUND

San Francisco's Current Electricity Service System

San Francisco residential, commercial and industrial customers currently get electricity from PG&E, an investor-owned utility that serves the Northern California market. PG&E generates energy or procures it from other suppliers, transmits that energy through infrastructure it owns and distributes it, as electricity, directly to end-users. Currently, the City and County of San Francisco (the City) primarily provides power to municipal facilities and businesses on City-owned property, using power from Hetch-Hetchy hydropower facilities.



Assembly Bill 117

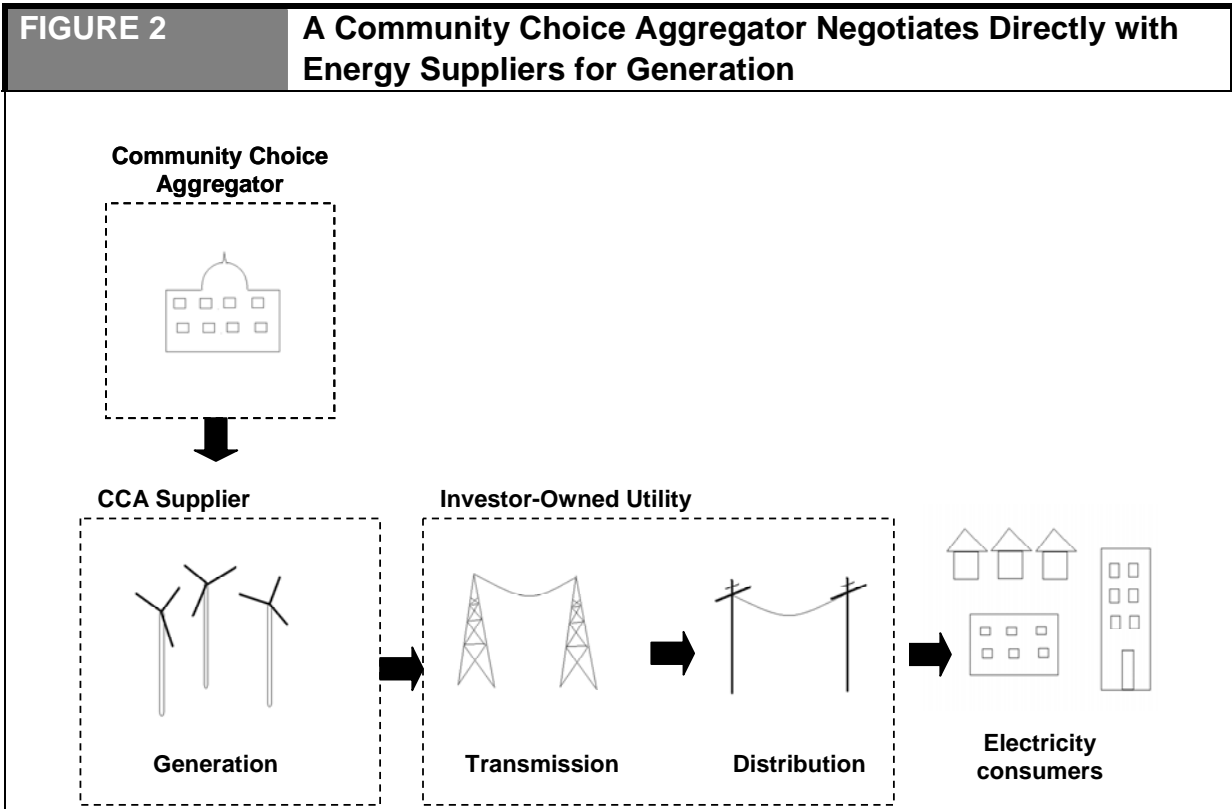
Under State Assembly Bill 117 (AB 117), passed in 2002, California cities may pursue an alternative model for electricity service, known as Community Choice Aggregation. Under a community choice program, a city would aggregate the total electricity demand load within jurisdictional boundaries and directly negotiate power contracts with energy suppliers on behalf of all end-users. Jurisdictions can also work together by aggregating their demand to secure a better deal.

AB 117 created an opt-out process for selecting a new energy supplier.

Prior to AB 117, individual customers were free to select an alternative electricity provider, but had to *opt in*, or consciously make such a decision. Under a Community Choice Aggregation program, a municipality could declare itself the default provider for all residents and businesses within its boundaries.

Customers would be able to *opt out* of Community Choice Aggregation and return to investor-owned utility service on an individual basis. As the aggregator, the city, rather than the utility, would determine the generation sources for those consumers who did not opt out.

Senator Carole Migden, then an Assemblywoman, wrote AB 117 in response to an unsuccessful electricity market restructuring effort in California. In the late 1990s the State implemented a deregulation plan to encourage competition in the electricity market, with the intent of increased consumer choice and lower retail electricity prices. Instead, supply shortages and electricity price shocks occurred, and few customers exercised their option to switch from default utilities to alternate suppliers. AB 117 was intended to protect consumers and return low, stable electricity rates to California by allowing communities to aggregate demand, thereby giving municipal aggregators greater market leverage to negotiate low-price, long-term energy contracts.



**California Community
Choice Aggregation
Plans**

*San Joaquin Valley
Power Authority*

In January 2007, the San Joaquin Valley Power Authority (SJVPA) approved a Community Choice Aggregation Implementation Plan for 13 cities. The plan, the first in the state to be submitted to the California Public Utilities Commission, outlines the SJVPA's program management plan. If the Commission certifies the plan, San Joaquin could begin implementing Community Choice Aggregation as early as November 2007. SJVPA will implement aggregation in four phases over a two-year period, first serving municipal energy sources, then adding large commercial and industrial customers, then medium commercial accounts and ultimately including residents and small businesses.¹

*Berkeley, Oakland,
Emeryville and Marin
County*

Other Bay Area governments, including Berkeley, Oakland, Emeryville and Marin County are considering forming Community Choice Aggregation programs. Berkeley, Oakland and Emeryville commissioned feasibility studies to explore the formation of a Joint Powers Authority to manage one aggregation program for the three cities. The Authority is in the process of developing an implementation plan for the proposed policy, and the city councils of each city will review the plan this year.

¹ Local Government Commission. "San Joaquin Valley Power Authority Files Implementation Plan with CPUC." Currents Newsletter 54 (March/April 2007): 2. Available at: <http://www.lgc.org/freepub/energy/newsletter/index.html>.

POLICY DEBATE

Benefits

Aggregating demand can increase the bargaining power of consumers and cities with CCA suppliers, as a larger share of the market speaks with one voice.

Some profits may be returned to customers...but CCA suppliers are motivated by self-interest, and an aggregator must negotiate to get a better deal for customers.

By establishing local control, CCA can give greater power to municipalities to effect environmental policy.

This section briefly summarizes some of the perceived benefits and risks in the debate concerning Community Choice Aggregation.

Cities using or exploring the Community Choice Aggregation model are usually motivated by the possibility of offering low, stable retail electricity rates to local end-users in deregulated markets in which energy prices can be volatile.

Aggregation programs shift all customers, who do not opt out of the process, to the aggregation program. A local aggregator therefore represents a large market in negotiations with energy suppliers, potentially giving it greater leverage to secure lower retail rates.

It has also been argued that municipal aggregators, who unlike investor-owned utilities are not beholden to shareholders, can potentially return some profit to customers, in the form of lower retail rates.

However, while a municipal aggregator could act in the public interest in this matter, the CCA supplier—whether it be a for-profit or a non-profit organization—would not. Thus, any consumer advantages that an aggregator could secure by acting in the public interest will be limited by its ability to drive a hard bargain with self-interested energy providers.

Taking a broader view of the advantages of local control, some programs use the Community Choice Aggregation to promote local goals, such as renewable energy procurement targets that exceed those of the incumbent utility. Renewable energy sources are often claimed to feature more stable generation costs than fossil fuels, particularly imported fossil fuels.

In California, the formation of a Climate Action Team in 2005, and the passage of the Global Warming Solutions Act (AB 32) in 2006 have initiated a process to reduce the state's greenhouse gas emissions to 1990 levels by 2020. The State enacted a Renewable

Portfolio Standards (RPS) (SB 1078) in 2002, which mandated investor-owned utilities purchase 20% of their electricity from renewable sources by 2017. This has since been accelerated to 20% by 2010, and 33% by 2020. If San Francisco wished, as a policy decision, to achieve a higher RPS, Community Choice Aggregation could be a means to do so. In fact, the draft implementation plan commits to a 51% RPS.

Risks

As a new policy, CCA has risks and uncertainties, particularly relating to customer service.

Some risks associated with CCA are that the aggregation model is a relatively new, untested policy; and for cities that have little experience managing energy procurement, the risks can be high. For example, the Cape Light Compact in Massachusetts, discussed in more detail in the next section, had difficulty collecting accurate demand data from a local electricity provider. It was forced to expend additional resources to ensure that they could meet customer demand.

Confusion over billing services also led to customer dissatisfaction. Customer satisfaction is particularly important because in all existing aggregation models customers can opt out of the service and return to the incumbent utility, generally for free in the first few months, then for a fee thereafter. Therefore, if an aggregator fails to offer services comparable to those of the incumbent utility, customer retention rates could fall, and the aggregator would lose the contract negotiation leverage associated with a large demand load.

ECONOMIC IMPACT FACTORS

The general policy debate reviewed in the previous section involves many important issues, but an economic impact assessment is primarily concerned with a policy's impact on prices. In this context, the economic impact factors concerning CCA can be summarized in two questions.

1. Is it feasible for a CCA service provider to meet or beat PG&E's rates over the long term?
2. If not, will CCA cause consumers to pay more for electricity than they otherwise would without CCA?

We analyze these questions in this section.

Feasibility of “Meeting or Beating” PG&E's rates

In some areas where it has been adopted, Community Choice Aggregation has created a positive economic impact, by reducing the energy rates, and increasing the use of renewable energy sources.

For example, the Cape Light Compact, a Massachusetts aggregator representing 200,000 customers in 21 towns and two counties, formed in response to state restructuring legislation. The Compact negotiates on behalf of its members for lower electricity prices and runs an energy efficiency program. The Compact tries to acquire the best market rate for electricity, protect consumer interests, improve quality of service, and encourage environmental protection, renewable energy development and demand-side management.

CCA has produced savings for customers in Massachusetts and Ohio

The Compact ran a pilot project from 2002 to 2004, serving about 50,000 customers. Mirant, the alternative energy provider, offered electricity at savings of 0.05% to 24%, relative to the default provider, depending upon the time period and customer class. On average, the Compact's rates were about 12% below the default provider's rates over the 20-month pilot period. In a letter to the Federal Energy Regulatory Commission, the Compact's Administrator reported that the program successfully enrolled and served large groups of

customers and that customers were generally satisfied with the program. In November 2004 the Cape Light Compact transitioned from the pilot program to full implementation, expanding its customer base to about 180,000. Three of the seven eligible suppliers that the Compact approached could meet the contract conditions, and the lowest bidder, ConEd Solutions, currently offers rates about 4% below those of the default supplier.² However, the Massachusetts consumers did not have to pay a Cost Responsibility Surcharge (CRS) to the investor-owned utility. The California Public Utility Commission (CPUC) requires this surcharge of California CCA consumers, to compensate a utility for past generation investments it made to support the customer base that switched to CCA.

NOPEC in Northeast Ohio gives consumers the option of paying more for green power.

The Northeast Ohio Public Energy Council (NOPEC), serving 118 towns and cities, formed in 2000 to create price competition and stability in a restructured electricity market. NOPEC established a service contract ensuring that rates would always be lower than those that the local utility charges. The program includes a green tariff component, a voluntary surcharge that individual customers can pay for clean energy, and secured a generation mix that is cleaner than other power in Ohio.³

In its most recent Annual Report, NOPEC reported that it saved customers \$46 million over the five years since the organization's establishment, equating to about \$33 per customer annually. In 2005, NOPEC switched to a new energy service provider after Green Mountain Energy, the generator that had served the program since 2001, terminated its contract. NOPEC also delayed the launch of a natural gas aggregation program after market prices unexpectedly increased.⁴

There are significant differences between San

² Downey, Margaret T., Administrator, Cape Light Compact. *Letter to Magalie R. Salas, Secretary, Federal Energy Regulatory Commission, Re: Electric Energy Market Competition Task Force (Docket No. AD05-17-000)*. The Cape Light Compact. Barnstable, Massachusetts: December 2, 2005.

³ Navigant Consulting, Inc. *Community Choice Aggregation: Base Case Feasibility Evaluation*. Berkeley, California: April 2005.

⁴ Northeast Ohio Public Energy Council. *2005 Year-End Report*. Ohio: 2005.

San Francisco's CCA plan calls for more renewable energy than the State has mandated for investor-owned utilities...

Francisco's CCA plan and those pursued in Massachusetts and Ohio. These differences reflect the capacity of the CCA framework to accommodate a variety of local goals. In NOPEC's case, for example, the value proposition was clearly and explicitly to offer the lowest possible rates for electricity and gas, by aggregating demand across 118 jurisdictions. Cape Light Compact is similarly focused on reducing the cost of electricity for consumers, although it does meet Massachusetts's Renewable Portfolio Standard (RPS).

San Francisco's conservation and clean energy emphasis, reflected in a commitment to support 360 MW of conservation and renewable energy, is aimed at ensuring that Community Choice Aggregation would result in greater greenhouse gas reductions than the state's RPS. The energy service provider must commit to developing a certain threshold of clean energy under its contract, specifically 107 MW of conservation, 150 MW of new wind power, 31 MW of local solar generation, and 72 MW of new distributed generation capacity, on-site generation from sources currently unspecified. Furthermore, the Plan commits the City to a Renewable Portfolio Standard of 51% by 2017.

Renewable Energy Bonds—municipal bonds authorized by San Francisco voters through Proposition H in 2001—could finance this clean energy component, and providers must include bond repayment schedules in their bids.

The Plan also emphasizes in-city generation in order to promote reliable service. This generation would primarily include solar energy, which would not contribute to local air pollution. Local generation can help mitigate service disruption caused by transmission line disruption. Service contracts would also commit the energy provider to meeting the California Public Utilities' Resource Adequacy Requirements, which obligate utilities to maintain a set reserve margin of energy above the expected demand

⁵ California Public Utilities Commission.

⁶ Rebecca Smith, "The New Cost of Alternative Energy". Wall Street Journal, February 23, 2007.

load.⁵

...But a high RPS target may conflict with the goal of meeting or beating PG&E's generation rates

These goals will make it difficult to also comply with the plan's other goal that a CCA supplier meet or beat PG&E's rates. For example, wind will remain more expensive than natural gas for several years, despite impressive recent price reductions, according to a review of renewable energy prices in the Wall Street Journal⁶:

"A plant entering service in 2015, the administration said in a 2006 report, could make electricity from wind for 5.58 cents a kilowatt hour -- versus 5.25 cents for natural gas, 5.31 cents for coal and 5.93 cents for nuclear."

Solar power is similarly more expensive than natural gas. Even in sunny areas, according to the Wall Street Journal, costs of generating electricity with solar panels range between 26 and 35 cents per kilowatt hour. New technologies such as concentrating solar power (CSP) are more promising, but:

"It costs 9 cents to 12 cents to generate one kilowatt hour of electricity by CSP -- not counting any subsidies -- compared with about 3 cents to 5 cents to generate the same amount of electricity by burning coal."

In the next 5-10 years, achieving 51% RPS and meeting or beating PG&E's rates is unlikely.

It would be hazardous to draw any hasty conclusions regarding the feasibility of meeting or beating PG&E's generation rates while aiming for a high RPS, over the course of many years. Many regulatory issues will affect the relative prices of different forms of energy in the near future, including tax incentives and other subsidies for investing in renewable generation and using energy efficient equipment, to how carbon should be priced to reduce greenhouse gas emissions. This latter issue will affect how competitive renewables are compared with fossil fuels, which will rise in price as carbon is priced. However, given the pace of technological change, it appears that at least near-term, in the next 5-10 years, achieving 51% RPS and meeting or beating PG&E's rates is unlikely

Notwithstanding the higher prices for renewables generation, which may also, to some extent, be offset

CCA customers in San Francisco would also have to pay a Cost Responsibility Surcharge to PG&E

by tax-exempt financing available through the Proposition H bonds, any San Francisco customer switching to CCA would owe PG&E a charge, called a Cost Responsibility Surcharge (CRS), to compensate it for investments it has already made in generation capacity to serve the departing customer.

Although CCA customers would only be responsible for paying the CRS for a fixed period set by the CPUC, perhaps five years, it could have a significant effect on consumer prices during that time.

Table 1 provides an illustration of what the impacts of higher renewable prices and the CRS could be on a typical residential bill. The example assumes a typical household consumption of 300 kilowatt-hours per month, a CRS of \$0.02/kWh, and a CCA generation rate that is 51% wind (the lowest price form of renewable), and 49% PG&E's current rate. The generation rate for wind is the estimated 2015 rate quoted above, \$0.0558/kWh.

It indicates that the final customer bill would be 24% higher under CCA, largely because of the impact of the CRS.

Bill Component	Status Quo		CCA (assuming 51% wind, 49% status quo price)		
	Rate/kWh	Monthly Cost	Rate/kWh	Monthly Cost	
Generation	\$ 0.043	\$ 12.90	\$ 0.050	\$ 14.86	
Transmission	\$ 0.009	\$ 2.70	\$ 0.009	\$ 2.70	
Distribution	\$ 0.040	\$ 12.00	\$ 0.040	\$ 12.00	
Taxes/Fees		\$ 6.90		\$ 7.39	
CRS	\$ -	-	\$ 0.020	\$ 6.00	
Total		\$ 34.50		\$ 42.95	24% Difference

This example does make some simplifying assumptions: the implementation plan doesn't attain 51% RPS until 2017, the CRS has not been set yet, and the 49% component of the rate includes PG&E's current 12% renewable share. On the other hand, the implementation plan is planning to rely on solar as well as wind, which would raise the rate above what is

shown here.

Even a competitive bidding process might not result in lower rates for San Francisco consumers, given the ambitious RPS target and CRS requirement.

A recent OEA study, in cooperation with UC Berkeley graduate student Alexandra MacKie, estimated that a conservative CRS charge of \$0.02 / kWh, imposed on a typical residential customer in San Francisco for five years, would require a CCA supplier to beat PG&E's generation rate by 11-18% during that time period, in order for a residential customer's total bill to remain the same in both situations. The CRS is again largely responsible for the difference.

Given the current generation cost profiles associated with all forms of renewable energy, **the risk of a CCA provider not being able to meet or beat PG&E's rates is significant.** Thus, given the renewable requirements detailed in the implementation plan, even a competitive bidding process might not result in lower rates for San Francisco consumers. This raises the potential of an adverse economic impact.

“Meet or Beat” is not a Requirement over the Long Term

Because there is some reason to doubt whether the planned renewable mix of the implementation plan is compatible with meeting or beating PG&E's rates over the long term, the draft implementation plan's requirements on this score are critical in any assessment of the economic impact of the proposed ordinances.

Ordinance file number 070501 outlines the implementation plan's policy with respect to rates. There are two different goals: one applies during the 60 day opt-out period, and the other applies subsequently. Initially:

“The CCA supplier must bid electric generation rates that ‘meet or beat’ current PG&E rates for each rate class...Bids must also include the ultimate CCA electric bill rates which will also include the Cost Responsibility Surcharge that will be imposed by the CPUC.”

During the opt-out period, in other words, the customer will see rates that “meet or beat” PG&E's rates. After that period, however:

“Thereafter the CCA supplier shall commit to a

structured long-term rate intended to meet or beat PG&E's electric rates."

In the draft implementation plan, prospective CCA suppliers have two options for proposing structured long-term rates: an indexed method and a fixed method. The indexed method means the supplier's rates will be indexed to PG&E's rates in some way, such as 1% below PG&E's generation rate. The fixed method means the rates will change at a known, constant percentage every year, regardless of how PG&E's rates change.

The actual economic impact, of course, will depend on what the actual rate structure of the selected ESP is. That being said, any rate plan that leads to higher costs for consumers would reduce disposable income for discretionary spending. The City, in its capacity as community choice aggregator, would presumably pick the vendor offering the best deal to consumers. If that vendor proposes an indexed rate plan, assessing the economic impact is reasonably straightforward.

Under a fixed rate plan, even though consumers have the right to opt out, it will be difficult for them to judge if CCA is offering them a good deal.

If that vendor proposes a fixed rate plan, however, the situation becomes more complicated. The opt-out provision in AB 117 offers a degree of consumer protection. The problem for consumers is that, even though they have the right to opt out, they will have essentially no way to accurately evaluate the economic costs and benefits, because the average consumer has no way of knowing PG&E's rates ten or fifteen years in the future. While rate stability may be perceived as a good-in-itself, if a stable rate is consistently higher than an unstable rate, this will cost consumers.

RISK FACTORS AND MITIGATION

Requiring CCA suppliers to offer a default service that never exceeded PG&E's generation rate would mitigate the risk of an adverse economic impact, especially for lower-income households.

The potential economic impact described in the previous section can be minimized by further specifying the types of bids that prospective CCA suppliers are allowed to propose in response to the RFP. As the draft implementation plan is currently written, these suppliers have the option of proposing an *indexed* long-term rate structure (indexed to PG&E's rate), or a *fixed* rate structure, which means rates will increase a fixed amount every year.

However, if prospective suppliers were mandated to offer consumers *the option of* an indexed or a fixed rate, with the default being an indexed rate that could never exceed PG&E's generation rate (including the CRS), then the risk of an adverse economic impact would be mitigated.

In this alternative proposal, the customer would be placed in CCA unless he or she opted out, as AB 117 provided. However, if the customer did not opt out, the default service would be the indexed rate. Alternatively, the consumer could choose the fixed rate, but would have to consciously choose that decision.

Nothing in this alternative approach would mandate that the fixed-price approach needed to offer a higher renewables mix. It is likely, given the higher cost of renewable generation, that the renewable component would be concentrated in the fixed service. This, however, could and should be left entirely to the prospective CCA suppliers, with no adverse impact on consumers.

Despite the fact that, under this alternative scenario, some consumers would pay more for electricity than they would keeping PG&E, there would be no adverse economic impact. This is because those consumers who chose the premium option made a conscious choice for more stable energy prices and a more conscientious environmental attitude, in the same way that many consumers knowingly decide to spend more up front for a hybrid car, for both environmental and

economic reasons.

Why is this approach different than the opt-out approach called for by the state legislation and outlined in the implementation plan? After all, isn't choosing not to opt-out of CCA a "conscious choice"? In a perfect world, there would be no difference. In reality, however, there are always wide gaps in participation between opt-in and opt-out models.

Ironically, the very "meet or beat" provision that applies only during the opt-out period, may discourage customers from carefully understanding what their future electricity expenditures would be under CCA, if they did not opt out. Requiring the two options might encourage the CCA supplier to actively market the advantages of the fixed price product, whereas the opt-out approach simply creates incentives for the CCA supplier—and the City, as aggregator—to minimize opt-out, regardless of the consequences for consumers.

It is likely that less well-educated, or less well-informed, consumers would be less likely to opt out of CCA, even if it were in their economic interests to do so. Low educational attainment, limited English proficiency, and lack of media access are all strongly associated with low income. These consumers would therefore experience a double impact. They would be less likely to opt out of CCA, even if it was in their economic interest to do so, and the penalty they could pay as a result of *not* opting out would be a higher percentage of their income, than of a wealthier, more informed resident.

Less-educated and lower-income residents may be less likely to opt out of a higher cost CCA plan, but proportionately more of their income would be at risk from higher prices.

The primary potential downside of the approach is that it might reduce the size of the aggregated market that will finance the new conservation and renewable generation. However, the implementation plan already provides for a scalable investment in H bond-financed generation, depending on the initial opt-out rate.

In addition, the overall opt-out rate from this alternative approach would likely be lower, since consumers would have an ironclad guarantee that, if they so wished, their generation rates would never exceed PG&E's. The CCA supplier would therefore probably

Minimizing the opt-out penalty, or offering a free opt-out period every two years, would also help to reduce the adverse economic impact a consumer could experience

benefit from a larger base of consumers than under the pure opt-out scenario, even if they did have to operate under more stringent price conditions than the implementation plan currently requires.

If a restructuring of the RFP requirements detailed by the implementation plan is not pursued, another way to mitigate the risks of an adverse impact on consumers is by minimizing the opt-out penalty. The IP currently plans to set the opt-out fee on the basis of what is needed to secure the H bonds. From an economic point of view, however, this is not the only interest at issue. The opt-out penalty is also the maximum possible adverse impact a consumer could ever be subjected to, regardless of what CCA and PG&E rates do in the future. One way to cap the potential adverse economic impact is to minimize this fee, or devise programs or subsidies to enable low-income residents to pay it when it makes economic sense to do so. The Cape Light Compact offers a free opt-out opportunity every two years: this would be an alternative way of capping the potential adverse impact to consumers, short of lowering the opt-out penalty itself.

In any event, there is reason to suspect that if the RFP requirements are restructured in the ways recommended above, the opt out fee would not need to be as high to secure the anticipated H bond issue because, again, the consumer would be protected by default from any rate rises and would be unlikely to ever opt out.

On a related note, to the degree that the opt-out rates are higher than expected, additional financial risks could arise, regarding the repayment of the H bonds. This could create additional costs that would burden the remaining customers. In this type of utility industry, building a critical mass of demand is vital to creating a sustainable enterprise.

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