

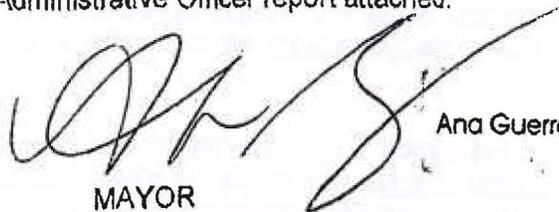
0150-10526-0000

TRANSMITTAL

TO Marcie L. Edwards, General Manager Department of Water and Power	DATE NOV 18 2015	COUNCIL FILE NO.
FROM The Mayor	COUNCIL DISTRICT	

AGREEMENTS WITH ULTRAMAR INC., A SUBSIDIARY OF VALERO ENERGY CORPORATION, RELATING TO AN ELECTRIC SERVICE AGREEMENT, CUSTOMER GENERATION INTERCONNECTION AGREEMENT, AND AGREEMENT FOR REIMBURSEMENT OF COSTS RELATING TO ADVANCED TREATED RECYCLED WATER SERVICE

Approved and transmitted for further processing including Council consideration.
See the City Administrative Officer report attached.


MAYOR

Ana Guerrero

OFFICE OF THE CITY ADMINISTRATIVE OFFICER

Date: November 13, 2015

CAO File No. 0150-10528-0000
Council File No.
Council District: 15

To: The Mayor

From: Miguel A. Santana, City Administrative Officer *MAS*

Reference: Communication from the Department of Water and Power dated June 18, 2015; referred by the Mayor for report on July 10, 2015

Subject: **AGREEMENTS WITH ULTRAMAR INC., A SUBSIDIARY OF VALERO ENERGY CORPORATION, RELATING TO AN ELECTRIC SERVICE AGREEMENT, CUSTOMER GENERATION INTERCONNECTION AGREEMENT, AND AGREEMENT FOR REIMBURSEMENT OF COSTS RELATING TO ADVANCED TREATED RECYCLED WATER SERVICE**

SUMMARY

The Department of Water and Power (DWP; Department) requests approval of a proposed resolution that authorizes a package of agreements with Ultramar Inc. (Ultramar), a subsidiary of Valero Energy Corporation (Valero). Valero is a San Antonio, Texas, based company that operates two refineries in California with one facility located within the community of Wilmington.

Approval of the proposed resolution specifically authorizes the DWP Board of Commissioners (Board) to execute the following agreements:

- i. Electric Service Agreement (ESA) RCS140003 provides Valero with a contract rate for electric service in accordance with the Electric Rate Ordinance, as modified by Supplemental Capacity Charge (SCC) discounts if Valero maintains a steady electrical load and consistent energy consumption. Additionally, it allows Valero to purchase DWP excess energy at a rate of \$0.045 per kilowatt hour (kWh) with a term of five years.
- ii. Customer Generation Interconnection Agreement PD3463 (CGIA) to clarify DWP and Valero responsibilities, procedures, and conditions relating to Valero self-generation facilities connected to the DWP Power System with a term of five years.
- iii. Reimbursement Agreement WR-15-1060 for DWP to finance up to \$1.0 million of Valero costs for the Front End Engineering Design (FEED) and estimate of costs for on-site improvements necessary to receive advanced treated recycled water service. The DWP Board is authorized by Charter Section 675(e)(2) to finance the use of systems and materials to conserve water or electric energy without further approval by the Mayor or City Council.

The ESA establishes a five year experimental contract rate to encourage Valero to maintain a steady electrical load and consistent energy consumption. If Valero achieves certain operating usage levels, the contract rate offers an escalating discount to the SCC. The SCC is intended to

recover costs from customers that require a high energy load and consumption on an intermittent basis. Additionally, Valero agrees to purchase any available excess DWP energy as a replacement for Valero's self-generated energy. DWP states that it can provide Valero a steady energy load at a lower cost than for intermittent loads which often require additional operating costs for rapid starting and stopping of generating facilities. A steady load enables a more efficient utilization of the overall Power System capacity. It is forecasted by DWP that the ESA will reduce Valero's current energy costs by \$1.4 million annually or \$7.0 million over the five year term of the contract. If Valero achieves higher load factors, it will result in further cost savings for Valero and benefit the DWP with additional gross revenue up to \$12 million annually depending upon how much energy Valero actually uses.

The CGIA clarifies DWP and Valero responsibilities when Valero's self-generation facilities are connected to the DWP Power System. It specifically establishes detailed conditions under which DWP and Valero personnel may safely operate and maintain the interconnected facilities.

In conjunction with the ESA and CGIA, DWP and Valero have agreed to enter an Agreement for Reimbursement that allows DWP to finance up to \$1.0 million of Valero initial costs for the design of on-site retrofits required for the potential use of recycled water. The design will include a cost estimate for construction which DWP will use to determine the economic feasibility of converting the Ultramar/Valero facility from potable to recycled water. If the conversion is deemed feasible, DWP will finance the full cost for on-site retrofits estimated to be \$5.0 million. Valero would pay DWP a potable water rate, rather than a lower recycled water rate, in order to repay the DWP the financing expense. It is anticipated that the payback period would be completed in no more than 10 years of recycled water sales at the potable water rate. The DWP Board of Commissioners is authorized by Charter Section 675(e)(2) to finance the use of systems and materials to conserve water or electric energy without further approval by the Mayor or City Council.

Approval of the proposed resolution is pursuant to City Charter Sections 373 for contracts longer than three years. The City Attorney has reviewed and approved the proposed resolution as to form and legality. Additional information relating to this request is provided in the Appendix.

RECOMMENDATIONS

That the Mayor:

1. Approve the proposed resolution authorizing two agreements between the Department of Water and Power (DWP) and Valero Energy Corporation (Valero) including (i) Electric Service Agreement RCS140003 with a term of five years, and (ii) Customer Generation Interconnection Agreement PD3463 with a term of five years; and,
2. Return the proposed resolution to the Department for further processing, including Council consideration.

FISCAL IMPACT STATEMENT

Approval of the proposed Electric Service Agreement and Customer Generation Interconnection Agreement will affect the Power Revenue Fund with a reduction in revenue of \$1.4 million annually or \$7 million over the five year term of the contract offset by a potential increase in revenue up to \$12 million if Valero achieves higher load factors. There is no impact to the City General Fund. The proposed agreements comply with the Department's adopted Financial Policies.

MAS:RR:06160010

APPENDIX

ELECTRIC SERVICE AGREEMENT AND CUSTOMER GENERATION INTERCONNECTION AGREEMENT

Valero currently pays rates in accordance with the approved electric rate ordinance, as provided in the Customer Generation Interconnection Agreement (CGIA). DWP proposes to replace the existing CGIA with a new Energy Service Agreement (ESA) and CGIA. Approval of the new energy agreements will establish a five year experimental contract rate designed to encourage and incentivize consistent operations at Valero that benefits the Department.

Electric Service Agreement – The proposed ESA provides Valero with Supplemental Capacity Charge (SCC) discounts ranging from 40 to 100 percent for maintaining a steady energy load with consistent consumption. The SCC is intended to recover the DWP costs of owning generating capacity and providing large amounts of energy for customers with intermittent usage. However, according to DWP, Valero regularly achieves a load factor of 90 to 100 percent and is not an intermittent high load customer. As a result, the DWP is satisfactorily recovering the costs of its generating assets from Valero through the applicable rate charges set in existing Rate Schedules CG-3 and CG-3(j). DWP analysis supports providing a discount to the SCC for continuing Valero's steady energy usage while satisfactorily recovering DWP's cost of service.

Valero currently generates approximately half of its energy demand with its own facilities and fuel. The remaining energy demand is provided by the DWP. In order for DWP to more effectively utilize its Power System, this proposed contract is also designed to encourage Valero to decrease its own energy generation and increase its usage of DWP. To achieve this goal, the proposed ESA enables the DWP to deliver excess energy to Valero. During periods of excess generation availability (as determined by the DWP), Valero may purchase the excess energy at a new Excess Generation rate of \$0.045 per kWh. DWP states that the rate is based on the current market price for gas generation including costs for operations and maintenance. An alternative to selling excess energy to Valero is for DWP to sell the energy in a wholesale energy market. However, it is a concern that other utilities could also have excess energy during the same periods which will affect the market prices. A second alternative is to shut down solar and/or wind power generating facilities. Existing power purchase agreements for wind and solar energy require the DWP to continue paying for energy regardless of the DWP demand so this option would not likely achieve any cost savings. DWP did not provide data regarding its historical excess energy generation and future excess energy will be determined based on numerous factors including, but not limited to, weather conditions, system-wide customer demand, and generating facility performance.

This agreement will be evaluated during the five year term to determine the benefits for both the Department and the customer, as well as to determine if other similar agreements should be implemented.

INTERCONNECTION AGREEMENT

Customer Generation Interconnection Agreement – The proposed Interconnection Agreement updates an existing agreement related to Valero's self-generation facilities. It also clarifies responsibilities for both parties and identifies conditions under which Valero and DWP personnel may safely operate and maintain the self-generation facilities. The term of the Interconnection Agreement is five years.

REIMBURSEMENT AGREEMENT FOR IMPROVEMENTS RELATED TO RECYCLED WATER

As part of an initial effort to expand the City's Advanced Water Purification Facility (AWPF) at the Terminal Island Water Reclamation Plant, DWP was tasked with identifying customers to use the additional recycled water. DWP evaluated four industrial customers in the Harbor area and determined that Valero could be served first from the expanded AWPF. Converting Valero's refinery operations to recycled water is expected to benefit the City by reducing the City's demand for potable drinking water and conserve 1,000 acre feet per year (AFY) or 325,900,000 gallons annually. Subsequent conversion of the other industrial customers is anticipated to be offered based on various factors including proximity to recycled water pipelines.

DWP proposes Reimbursement Agreement WR-15-1060 for financing both the initial engineering plans up to \$1.0 million and the on-site capital costs of converting the Valero refinery to utilize recycled water. Based on the results of the initial engineering plans and an estimate of costs, DWP will determine the economic feasibility of converting the Ultramar/Valero refinery to recycled water. If DWP determines that the conversion to recycled water is feasible, a recycled water service agreement will be submitted for City Council consideration.

Recovering the costs of the reimbursement agreement and the associated on-site improvements will be through the sale of lower cost recycled water to Valero at a higher potable rate with a component of the rate dedicated to the financing charges. DWP estimates that on-site improvement costs will total \$5.0 million. The payback period is estimated to be 10 years.

DWP states that a similar reimbursement agreement for recycled water infrastructure costs was executed with Playa Vista Company, LLC. The amount financed for Playa Vista Company was approximately \$4.2 million which is being repaid to DWP through a similar methodology of charging a higher potable water rate for recycled water.

If it is determined by DWP that recycled water service for Valero is infeasible, this reimbursement expenditure would not be repaid by Valero. Costs associated with any off-site infrastructure including the construction of recycled water pipelines to Valero will be funded through the DWP Water Revenue Fund.

The DWP Board of Commissioners (Board) is authorized by City Charter Section 675(e)(2) to execute this Reimbursement Agreement without further approval by the Mayor or City Council.