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REPORT TO HONORABLE MAYOR AND COUNCILMEMBERS

ANALYSIS OF PROPOSED ELECTRIC AND GAS FRANCHISES

INTRODUCTION

This Report explains differences between the ordinances to award gas and electric franchises that were advertised in the City's Invitations to Bid on March 19, 2021, and the ordinances that the Mayor now recommends to the Council under San Diego Charter section 103.[1]

The ITB advised that "the franchise may be awarded by introduction and adoption of an ordinance substantially in the form specified in as either Exhibit A or Exhibit B attached hereto." It further provided that "[a]ny recommendation for a franchise award shall be based on the highest responsible bid that is determined by the City to be in its best interest. The City reserves the right to negotiate changes to the bid terms, or to negotiate with the current franchise holder to renew, extend, or amend and replace the current franchise."

In addition, the ITB required bidders to "include a detailed narrative proposal for a Cooperation Agreement" addressing climate harm mitigation, local energy, and social issues that would be adjunct to the franchises, and provided that "[t]he proposals for the Cooperation Agreement shall be subject to acceptance, rejection, or requests for modifications by the Mayor." The ITB also said "[t]he Mayor may recommend that the franchise be awarded to the highest bidder who submits the highest value Cooperation Agreement proposal determined to be acceptable and meets the other terms in this Notice."

Bids were opened on April 16, 2021. San Diego Gas & Electric Company (SDG&E) was the only bidder. Its bids included a detailed proposal for a Cooperation Agreement, since renamed an "Energy Cooperation Agreement," and responded in a categorical topical manner to the ITB requirements. Instead of expressly taking exception to any provision of the advertised franchises, SDG&E's bids stated "[w]e look forward to a discussion with you so that we may jointly discuss these details [of the advertised franchise requirements] to support introduction and adoption of the authorizing ordinance."

[1] The two Invitations to Bid were virtually identical except for their Bid Amounts and Undergrounding and are hereafter referred to by the singular ITB.

Following the bid opening, the City and SDG&E engaged in negotiations regarding the terms of the franchises and the Energy Cooperation Agreement, resulting in the documents that will be introduced at the City Council meeting on May 25, 2021.

This Report highlights negotiated changes to the ITB and, where warranted, explains the legal and practical implication of those changes. The sections referenced are from the Electricity Franchise, unless otherwise indicated.

ANALYSIS

I. CHANGES TO SECTION 1

A. **Section 1(a)**. San Diego Gas & Electric Company has been added as Grantee throughout the Franchises assuming that the Council approves the Mayor's recommendation by a two-thirds vote.

B. **Section 1(c) and (t).** Definitions were added for "Administrative MOU" and "Undergrounding MOU," which are terms that are referenced repeatedly in the Franchises. Note that due to the addition of these definitions, the numbering in the original ITB has changed. Both MOUs will be negotiated after the Franchises are approved.

C. **Section 1(d).** Applicable Law now also includes the San Diego Charter, the San Diego Municipal Code, and the Federal Power Act.

D. **Section 1(e).** The Bid Amount is $70 million dollars plus interest if paid in installments.

Comment: The ITB required a minimum Bid Amount of $70 million dollars.

E. **Section 1(f).** The ITB definition of "Books and Records" was changed to delete "any and all" (records) and the language that allowed City to determine which records are relevant was limited to those "which are both for the purpose of, and reasonably necessary to, verify Grantee's compliance with the terms in this Franchise." The City may review "information to verify the applicable prevailing wage was paid" instead of "contract worker payroll."

Comment: The changed definition gives Grantee more control over which records the City may review based on Grantee's determination of which records are and are not "reasonably necessary" for the City to review to confirm compliance with the Franchise and Energy Cooperation Agreement.

F. **Section 1(h).** The ITB definition of "Commencement Date" was changed to delete the reference to bidders who do not already possess a Certificate of Public Convenience and Necessity (CPCN) from the California Public Utilities Commission CPUC."

Comment: The deleted language does not apply to bidders like SDG&E who have a CPCN. As such, the language was deleted as superfluous.

G. **Section 1(p)**. Following the reference to Account No. 451 is the language "or its superseding account."

II. CHANGES TO SECTION 2

A. **Section 2(a).** In the Purpose section, the ITB requirement to cooperate with the City's Climate Action Plan (CAP) "to the fullest extent practical" is changed. As negotiated, the requirement applies to only the December 2015 CAP, and the word "fullest" is removed. A subpart (7) was added to the effect that Grantee agrees to meet in good faith about CAP updates.

III. CHANGES TO SECTION 3

A. **Section 3(b).** As originally advertised, the primary term of 10 years would automatically extend an additional 10 years unless the Mayor "recommends against an extension and reasonably proves to the City Council by a preponderance of the evidence that Grantee has not complied with any term" of the Franchise or Cooperation Agreement. The Mayor's case would be based, in part, on information from the Compliance Review Committee. If two-thirds of the City Council agreed by public vote that the Grantee is not in compliance with the Franchise or Cooperation Agreement, renamed "Energy Cooperation Agreement," then the second 10-year term would be void and the Franchise would terminate. The ITB language also included timelines for such actions.

As negotiated, the second 10-year term is automatically granted unless one of the conditions described in Section 15 occurs: breach; the automatic renewal for a second term is voided; or municipalization. The exercise of these termination options would require the City to refund a portion of the Bid Amount as described in Section 4, Compensation.

Comment: This change reflects a reorganization and modification of the ITB. Discussions of termination and breach are moved to Section 15, new pro rata refund provisions associated with termination appear in Section 4, and provisions that survive the termination of the Franchise are moved to Section 16.

B. **Section 3(c).** This section discussed which terms would survive the expiration or termination of the Franchise, including completion and discharge of obligations and payments, and bond and insurance requirements.

Comment: These provisions have been moved to Section 16, which addresses survivability, Section 13, which addresses insurance, and Section 22, which addresses performance bonds.

IV. CHANGES TO SECTION 4

A. **Section 4(a).** This Section has been amended to add that Grantee will be assessed the same fees as any other applicant.

B. **Section 4(d):** A notice requirement was changed from 10 days to 30 days. This means that if Grantee agrees to pay another City a greater fee than it pays the City, it must notify the City of such agreement within 30 days. SDG&E sought this change saying it needed the additional time to notify regulators and update billing cycles.

C. **Section 4(e).** With regard to Electricity, this Section has been rewritten to provide payment of the $70 million Bid Amount over a 10-year term as described in a newly added Table 1, instead of nine successive payments as originally contemplated. Payment of the $70 million Bid Amount shall be paid in $10 million increments "in lawful money" by August 1 of 2021, 2022, 2023, 2024, 2025, 2030, and 2031. Promissory note installments would mature on August 1 of the year each payment is due, and each promissory note shall provide for the payment of the principal amount plus interest, calculated on an actual/actual basis at the annual rate of 3.38%.

If the Franchise is terminated before expiration under Section 15, then any promissory notes not yet due will be void and the City must refund portions of the Bid Amount. It is important to review Table 2 to understand the refund provisions.

In addition to the Bid Amount, Grantee will contribute $5 million per year, for a total of $20 million, to the City's General Fund, in 2037, 2038, 2039 and 2040, for City to use to further its Climate Action and Climate Equity goals. Grantee may make such contributions to the City's General Fund earlier, but not later, than the years indicated. The contributions will not be made if the Franchise is not in effect during the contribution years.

With regard to Gas, Grantee shall pay the $10 million Bid Amount over the 20-year term as follows: $500,000 to the City Treasurer by August 1 beginning in 2021 until the $10 million is paid in full or the Franchise is terminated. The promissory notes shall bear interest as provided in Section 4(d)(3). The notes shall not be due and payable to the City until the maturity date of each installment on the note. If the Gas Franchise is terminated early, then the City is not required to refund any portion of the Bid Amount.

Comment. The new provision potentially increases the total bid for the Electricity Franchise by $20 million to a total of $90 million if the City does not exercise its right to terminate the franchise under Section 15. Unlike language in the ITB, however, the new language requires the City to refund portions of the Bid Amount even if Grantee breaches the Franchise or Energy Cooperation Agreement.

The Bid Amount of $10 million for the Gas Franchise is paid over a twenty-year term in $500,000 increments and does not have a refund provision.

D. **Section 4(e)(3).** The proposed change to this section eliminates the reference to equal payments over nine years.

Comment: The ITB's Bid Amount of $70 million during the initial term of the Electric Franchise is met, but the refund language is new. The ITB's Bid Amount of $10 million for the Gas Franchise is also met.

E. **Section 4(e)(4):** The ITB's requirement that the Grantee provide a letter of credit to secure payment of the promissory notes is eliminated. It is replaced with a provision that Grantee will provide a letter of credit for the notes on City demand if **its** creditworthiness declines during the Term. Cost for letter of credit is born by Grantee.

Comment: A letter of credit provides the City with recourse to payment if Grantee is unable or refuses to pay portions of the Bid Amount when due. The ITB required security for payment of the Bid Amount obligations and the proposed revisions delete that requirement and replace it with a requirement to furnish security later if Grantee's creditworthiness is called into question.

F. **Section 4(e)(6):** This subsection was deleted in its entirety and replaced with language describing a pro rata refund of the Bid Amount due to Grantee if City terminates the Electricity Franchise under section 15 before the Franchise expires. There is no pro rata refund requirement in the Gas Franchise.

Comment: Please review the Electricity Franchise to understand the refund provisions.

G. **Section 4(e)(7**). This provision of the ITB provided that promissory notes for Bid Amount payments in future years would be payable to the City if Grantee forfeited the Franchise by breach and is now deleted. With regard to the Electricity Franchise, there is now a provision that requires Grantee to pay to the City, in addition to and separate from the Bid Amount, $5 million per year in 2037, 2038, 2039, and 2040, for a total of $20 million, to the City's General Fund to further its Climate Action and Climate Equity goals. The City would not be eligible for these funds if the Franchise is not in effect for any reason in 2037, 2038, 2039, or 2040.

Comment. This change means that if Grantee breaches the Franchise, and the Franchise is terminated, the portions of the Bid Amount that would be due in future years will not be paid to the City.

In addition, Grantee will contribute $5 million to the City's General Fund in years 2037, 2038, 2039, and 2040 if the Franchise is extended beyond its initial 10 years.

V. CHANGES TO SECTION 5

A. **Section 5(b).** A sentence was added that payment of the Bid Amount is controlled by Section 4, Compensation.

B. **Section 5(g):** The provision for Grantee to provide City with its CPUC annual reports is deleted and replaced with language that addresses disputes concerning the City's access to Grantee's records. Specifically, disagreements concerning City's access to Grantee's Books and Records will be elevated to each party's designee for resolution.

Comment: The physical delivery of CPUC annual reports is not necessary given the Internet. This provision is a vestige from the 1970 franchise and is now obsolete. The new language inserts a dispute resolution process.

VI. CHANGES TO SECTION 6

A. **Section 6(b):** This provision was changed to provide that the Compliance Review Committee will provide recommendations to the Council regarding the automatic renewal of the secondary 10-year term. Language was also added giving Grantee the right to deliver a contemporaneous response to the City Council regarding the Compliance Review Committee reports.

Comment: This change gives the Compliance Review Committee a voice on the question of whether the Council should end the Franchise at the end of the first 10 years and provides the Grantee with an opportunity to respond.

B. **Section 6(c):** The provision relating to access by City officials to Grantee records is changed: City officials will have access to records that "are reasonably necessary" to confirm compliance with the Franchise, instead of to records City officials believe to be "germane" to verification. The time allowed for production of records changed from 5 days to 10 days. If Grantee is unable to produce records within that timeframe, an exception will be permitted so long as the Grantee provides a good faith explanation and an estimate of when it will produce.

Comment: A standard of "reasonably necessary to confirm compliance" is objectively higher than "germane to verification." Grantee represented in negotiations that it would have trouble meeting a 5-day timeline.

C. **Section 6(d):** Like Section 6(c), this provision was changed to limit the discretion the independent auditor of the Compliance Review Committee would have in determining which records should be produced for audit. The new language allows the auditor access to records that are "relevant to confirming Grantee's compliance with the Franchise."

Comment: This language may lead to disputes concerning which records are relevant for City review.

D. **Section 6(e).** Language was added to ensure the right of the City Attorney as a Charter officer to confirm compliance with the Franchise.

VII. CHANGES TO SECTION 8

A. **Section 8(a):** This provision reserved the City's right to require Grantee to relocate to make way for City improvements of any type or description. It has been revised to require the City to provide to Grantee substantially complete plans for the portions of the projects ready for relocation before Grantee is required to relocate facilities that conflict with the City's uses of its streets. In addition, the subsection now states that the Administrative MOU will include detailed procedures for relocations, and that the Administrative MOU will not control over the Franchise.

Comment: This requirement would prevent the City from directing relocations before it has substantially complete designs and may have cost and scheduling implications for the City.

B. **Section 8(b)-(d)**: These subsections were deleted and replaced with language that references existing litigation between the City and Grantee concerning the relocation of Grantee's facilities that conflict with City's water projects. Specifically, the new language states: "Notwithstanding the language in Section 8(a) of this Franchise, with regard to such costs, the City and Grantee agree that they will abide by the final determination of the California courts or settlement thereof and Section 8(a) shall not supersede any such determination or settlement. Any agreements presently in effect or subsequently executed between the City and Grantee regarding the cost of such relocations shall remain in effect unless and until such final determination by the courts or settlement by the City and Grantee."

Comment: Sections 8(b)-(d) were intended to close loophole arguments concerning Grantee's obligations. These subsections are replaced by a new subsection 8(b), which means that the City is agreeing that a Superior Court judge or appellate court, not the City, will determine the contract terms for cost responsibility of all relocations of Grantee facilities necessitated by all City water projects from now until 2041, not just the two projects (Pure Water Program and Montezuma Road pipeline projects) now before the courts. This may have cost and scheduling implications for the City.

C. **Section 8(c):** This subsection was deleted in whole. It provided that if Grantee ever disputes its duty to honor relocation directives then it must nonetheless bear all the costs and perform the relocations while the dispute is pending.

Comment: In two noteworthy situations, the redevelopment of the East Village/Petco Park and the Pure Water Program pipelines, Grantee insisted that the City bear half or all the cost before it would perform necessary relocation work, resulting in project delays and increased costs and liabilities. The City paid for relocation associated with Pure Water and reserved its rights to seek remedies from the Grantee. City and Grantee are in litigation to resolve this dispute.

D. **Section 8(d):** This section was deleted in whole. It allowed Grantee to ask for a relocation schedule extension if it could not meet the timeline provided in Section 8(a).

VIII. CHANGES TO SECTION 9

A. **Section 9(a):** Language was added that the Administrative MOU does not curtail or limit Grantee's rights under the franchise. In addition, Grantee would now have 60 days, instead of 30 days, to apply for an Administrative MOU following the Effective Date.

B. **Section 9(b):** The words "comply with the general terms attached" were deleted and the words "include the matters described in" were substituted. The words "agreed upon" were added in reference to the established terms of the Administrative MOU and the word "Grantee" was conjoined with City in reference to establishment of the Administrative MOU terms.

Comment: These changes transform the Administrative MOU into a bilaterally negotiated instrument.

C. **Section (9)(b)(1):** The ITB gave the City Engineer or designee "sole discretion" to determine the information needed for City requirements. As amended, the City's designee must use "reasonable" discretion, be specific, and follow "Good Utility Practice" as that term is defined in the Franchise. In addition, the City's requests for specific City projects or concerns must be "in a form and type deemed appropriate by Grantee in its reasonable discretion." Further, the City and Grantee may agree in the Administrative MOU on more detailed procedures for the provision of GIS data, including, if feasible, the Grantee providing the City with secure electronic access to certain GIS information of Grantee either directly or through an approved contractor. Finally, Grantee disclaims any representation or warranty for the accuracy of its GIS locational data, and commits to provide staff at the scene of an emergency promptly on City request.

Comment: Access to timely and accurate information about the location of Grantee facilities in the City's own streets is important to City planners, engineers, and contractors, who plan and perform excavation in the City's streets. Safety is often an issue. These changes defer details to the Administrative MOU, which is a guiding document that lacks the force of an ordinance, but the language provides the Grantee with discretion on what records it will provide. Although the City typically gives reasons for its data requests, it must now identify specific projects or concerns. Although Grantee is justified in having security concerns, the City keeps location records confidential and such records are generally exempt from disclosure under the California Public Records Act (CPRA). The language disclaiming Grantee's representations about the accuracy of its locational data may relieve it from liability for the reasonable accuracy of the data. The City and its contractors must use dig alert notifications and other due diligence to confirm information.

D. **Section 9(b)(1)(A).** The City's standard CPRA language, used in all City contracts, prevents the City from being liable for protecting or using the information provided to it by third parties. By that language, the City assumes no liability associated with a third party's records unless it is solely negligent or engages in willful misconduct. The amended language broadens the City's liability to include "active negligence," and if the City is sued for withholding from disclosure Grantee's records at Grantee's direction, the Grantee will defend and indemnify the City "to the extent" the City is sued for withholding that information from disclosure. "To the extent" replaces "if."

Comment: The City's liability for withholding Grantee's records at Grantee's direction expands under the amended language to include active negligence. Active negligence in California may occur if a City employee fails to perform a precise duty, participates in an affirmative act of negligence, or is connected with negligent acts or omissions by knowledge or acquiescence. In addition, "to the extent" may be used by Grantee to limit its liability.

E. **Section 9(b)(1)(B)(3).** This provision in the ITB was changed so that Grantee is provided 10 days' notice instead of 5 days' notice to arrange for standby safety observers. In addition, Grantee will pay for safety observers when the facilities to be protected are transmission level, and the City will pay for safety observers if the facilities are distribution level. The ITB required the Grantee to pay for both. Last, if the Grantee provides better terms to any other city, it will inform City of such terms and make adjustments to match.

Comment: According to an expert with whom we consulted, the need for safety engineers is encountered far more often for distribution facilities than transmission facilities, meaning the City's costs will be far greater than those of Grantee. Grantee represented in negotiations that every other City pays for standby engineers.

F. **Section 9(b)(1)(4).** These words have been added: "and Grantee shall cooperate unless reliability, safety, and compliance obligations make such adjustments impractical" to the condition that City may modify company's Two-Year Plan under the administrative requirements.

Comment: This language reflects the jurisdiction of the California Public Utilities Commission over regulation of Grantee's system and its safety, reliability, and compliance.

G. **Section 9(b)(1)(5):** In this section regarding the Joint Utilities Coordinating Committee (JUCC), the City Manager replaces the City Engineer. Also, Grantee is no longer required to "encourage" other utilities to participate on the JUCC, and instead must commit to helping the City "efficiently communicate and schedule" with other utilities.

Comment: The City cannot require other utilities to participate. This is likely not an issue as other utilities typically participate.

IX. CHANGES TO SECTION 10

A. **Section 10(a):** Note that undergrounding only applies to the Electricity Franchise. This section does not appear in the Gas Franchise.

In the undergrounding section, the words "expected to continue" were deleted as they relate to CPUC Rule 20 undergrounding funding. Words were added at the end of this subsection requiring the City and Grantee to provide dedicated liaisons for undergrounding project coordination.

Comment: There is an ongoing Rulemaking at the CPUC (R.17-05-010) that casts uncertainty on the future configuration or continuation of the rate-based Rule 20 undergrounding program. If the Rule 20 program is reduced or eliminated, undergrounding revenue received by City would not yield 4.5% of Grantee's Gross Receipts as anticipated in the ITB, as 1.15% of that amount is Rule 20 revenue. Accordingly, changes in Rule 20 may mean that only 3.35 % of Grantee's gross receipts are guaranteed as undergrounding revenue, as the 1.15% assumed Rule 20 funding would not be assured going forward.

B. **Section 10(b):** This subsection was conditioned by the added words "[a]s long as Rule 20 or its successor tariff remains in effect…."

Comment: See comment on Section 10(a).

C. **Section 10(d):** Words were added again regarding possible changes to Rule 20 program.

Comment: See comment on Section 10(a).

Section 10 (f): The changes in this subsection relate to the City's ability to perform design and construction of undergrounding projects using its own engineers and contractors. It has been amended to provide that Grantee's duty to cooperate is "upon receipt of substantially complete plans from City." Also, it now states that the City's right to perform the projects with its own hired engineers and contractors is to be addressed in the Undergrounding MOU, and is subject to the Grantee's agreement on a project basis, which may not be unreasonably withheld.

Comment: In undergrounding districts where the City elects to self-perform undergrounding projects, the system belongs to the Grantee and jurisdiction remains with the CPUC. Accordingly, Grantee's cooperation is essential with regard to design process, plan review, safety, CPUC General Order compliance review, and the placement of wire in conduit, "cutover" from overhead, and energization. The new language says that Grantee will cooperate only after the City submits "substantially complete" plans. The Undergrounding MOU will describe the working relationship in more detail.

D. **Section 10(h):** The ITB provided that the City could perform its own undergrounding "where City determines it is more appropriate for it to contract for work." This language has been amended to state that City can perform its own undergrounding work in circumstances "where City and Grantee agree" it is more appropriate for the City to contract for work.

Comment: The City is giving up its right to unilaterally make decisions that impact its ability to manage its own undergrounding projects. Under the prior Undergrounding MOU, the City did not allow Grantee discretion to decide whether the City could self-manage a project.

E. **Section 10(i):** The ITB allowed reimbursement by the City to the Grantee for expenses directly and exclusively related to undergrounding electric infrastructure and specified that Municipal Undergrounding Surcharge funds could not be used for employee or executive incentives and bonuses, or for any indirect costs that are not directly related to the program. That language has been changed to allow payment from the Municipal Undergrounding Surcharge of indirect costs "reasonably related" to the program and employee incentives and bonuses. Last, language is added that says the Undergrounding MOU will describe the accounting information and documentation Grantee must include with all invoices for the undergrounding work submitted for reimbursement from the Municipal Undergrounding Surcharge funds.

Comment: Accountability measures will be shifted from the Franchise to the Undergrounding MOU. The Franchise will have been granted before the Undergrounding MOU is negotiated, so the City may lose leverage in insisting on specific accounting information in post-Franchise negotiations. The new language does not define "indirect costs not reasonably related to the program," or provide information as to how the City will determine whether Grantee made money, lost money, or broke even on any undergrounding project. Payment of employee and executive incentives and bonuses from the Municipal Undergrounding Surcharge has been a point of contention for many years. Although executive incentives and bonuses will no longer be paid from Municipal Undergrounding Surcharge funds, employee incentives and bonuses will be. Grantee represented that many of its employees who work on undergrounding projects have "at-risk" compensation and goals tied to the success of this program, and that their compensation as utility employees is subject of commission review, reporting analysis, funding, and a biannual audit. Employee bonuses may have basis if Grantee is obliged to pay them under its employment terms.

F. **Section 10(j):** Regarding undergrounding projects, language has been amended to require Grantee to "verify," instead of "justify," invoices to be paid from public funds. Furthermore, Grantee "shall submit to the City on an annual basis Grantee's average undergrounding costs per mile under the Municipal Undergrounding Surcharge program, calculated using the 'miles installed' methodology further described in the Undergrounding MOU." The words "…in any way relating to [to Grantee's undergrounding charges]" were deleted and the words "reasonably necessary to verify [same]" were inserted. Finally, instead of 5 business days to provide requested Books and Records to the City, Grantee will have 10 business days.

Comment: The ITB reserved for the City the right to access "all Books and Records that it deems necessary to verify expenditure(s)" and the right to "all requested Books and Records in any way relating to charges to or expenditure of Municipal Undergrounding Surcharge funds." As amended, the City's access must be "reasonable" and "reasonably necessary to verify" charges, which means that Grantee may challenge the City's right to review books and records to verify expenditures.

G. **Section 10(k):** Words were added to provide that the City will emphasize undergrounding projects in communities of concern and high fire threat areas, set project priorities in coordination with the Grantee, and provide Grantee with its project priorities when Grantee prepares its Two Year Plans. Language stating that "[a]ny dispute regarding reimbursement of costs shall not alter the obligation of Grantee to adhere to timelines" was removed.

Comment: Disputes regarding reimbursement of costs may impact performance timelines.

X. CHANGES TO SECTION 12

A. **Section 12(a):** Words were deleted to remove required compliance with updates to the City's 2015 Climate Action Plan. This sentence was deleted: "Subject to Applicable Law, Grantee shall permit distributed energy resources to deliver all practical excess amounts of electric energy and capacity not used at the sites of distributed energy resources located within the City to be made available to other customers of Grantee and/or to any operating CCA program established by the City…" This sentence was added: "Grantee accepts that the City will support expansion of net energy metering, feed-in tariffs, and other economic mechanisms to foster development of local renewable fueled electric distributed resources, electric storage, microgrids, electric transportation, and other technologies to be increasingly integrated with the design and operation of Grantee's electric distribution system."

Comment: As explained in comments to Section 2(a), this means that Grantee will not commit to supporting updates to the City's CAP without knowing what those changes will be. Subjects addressed in this Section are controlled by legislation and the CPUC, and are deferred to the Cooperation Agreement.

B. **Section 12(b):** The requirement that Grantee use best efforts to "minimize service costs to City residents and businesses" was deleted.

Comment: Though written as a "best efforts" condition, it is true that Grantee cannot treat customers in the City of San Diego any differently than customers in its other cities for purposes of its general rates. The Grantee's general rate cases are periodically filed at the CPUC to present the Grantee's costs for ratemaking purposes, and these cost presentations are typically litigated by numerous parties including the CPUC's own public advocates and any other party wishing to participate, including the City.

C. **Section 12(c):** Words were removed that made the Energy Cooperation Agreement a binding document for purposes of the second 10-year term.

Comment: New Section 15 permits the City to terminate the Franchise for breach of the Energy Cooperation Agreement at any time following dispute resolution, as described in Section 17, a court determination that breach has occurred, a recommendation by the Mayor, and a two-thirds vote by the City Council.

D. **Section 12(d):** This section has been amended to provide that the City Council must allow the Grantee to amend the Energy Cooperation Agreement to adapt to evolving circumstances if the request is reasonable.

E. **Section 12(e):** Changes were made to make clear that shareholders will pay for the Climate Equity Fund.

XI. CHANGES TO SECTION 13

A. **Section 13(a):** Changes were made to the indemnification provision involving all claims, including those arising from losses, damages, or injuries sustained by certain classes of persons. The words "employee" and "…anyone employed by them (company's subcontractors) or anyone they control" were replaced by "employee of a" subcontractor "of any tier." The words "anyone directly or indirectly employed by them, or anyone that they control" were deleted and "employee," agent, or subcontractor "of any tier" were inserted. In addition, language was added stating that Grantee's duty to defend, indemnify, and hold harmless the City will not include claims or liabilities arising from the active negligence, sole negligence, or willful misconduct, or claims or liabilities regarding the award, amendment, renewal or extension of the Franchise to Grantee.

Comment: The replaced language should provide substantially same coverage of obligation. However, contrary to the City's standard language, Grantee would not defend and indemnify the City for "active negligence," or claims and liabilities associated with the awarding of this Franchise.

B. **Section 13(e):** Language was added to provide that insurance coverage amounts may not increase at the "reasonable discretion" of the City's Risk Manager by "more than forty percent (40%) every five (5) years."

Comment: Use of the term "reasonable" permits Grantee to challenge the City Manager's discretion.

XII. CHANGES TO SECTION 14

A. **Section 14:** The ITB required the Grantee to repair damage to City streets caused by its operations. The language has been amended to provide that the Grantee "shall not be responsible for repairing the Streets to a condition better than existed prior to Grantee's work being performed, except as required by Applicable Law. For the avoidance of doubt, if Grantee's operations cause the need for a repair to a street, sidewalk, curb or gutter, which, because of a change in Applicable Law must be built to new standards, Grantee shall repair or build the street, sidewalk, curb or gutter to such new standards."

Comment: The changes require repairs to be performed to comply with Applicable Laws as they exist at the time the damage is done (e.g., current Americans with Disabilities Act requirements and City codes). This is an acceptable legal minimum.

XIII. CHANGES TO SECTION 15

A. **Section 15:** The section title has been changed from “Forfeiture and Other Remedies” to “Forfeiture, Termination, and Other Remedies.” It has been substantially restructured and rewritten. Termination, which the ITB addressed in Section 3(b), is now addressed in Section 15, as is breach.

Under the ITB, the Grantee would be entitled to a secondary 10-year term if it “faithfully performed all conditions agreed to in the Franchise and Section 12 [Cooperation with City Climate Action, Local Energy, Energy Justice, and Purchasing of Local Materials] herein.” Grantee’s compliance would be assumed unless the Mayor recommended against an extension and “reasonably proves to the City Council by a preponderance of the evidence that Grantee has not complied with any term.” In gathering such evidence, the Mayor would need to consult with the Compliance Review Committee and then persuade at least two-thirds of the City Council that Grantee failed to comply with the Franchise or Cooperation Agreement.

Further, the ITB provided that should Grantee “fail, neglect, or refuse to comply with any of the conditions of the Franchise, and if such failure, neglect, or refusal shall continue for more than thirty (30) calendar days after written demand by the City Manager for compliance,” the City Council could invoke “all rights and remedies allowed under law, including but not limited to breach of contract, declaratory relief, specific performance, and mandatory injunction.” The City Council could “terminate the right, privilege and franchise granted in and by the Franchise,” in which case, “all the rights, privileges and the Franchise of Grantee shall be at an end” and Grantee “shall surrender all rights and privileges in and to the Franchise.”

As negotiated, Section 15 now addresses breach where termination is not contemplated, termination for breach, municipalization, and liquidated damages. It is also amended to provide for pro rata refunds of the Bid Amount to Grantee if the City terminates the Franchises.

Comment: The 1970 Franchises adopted language similar to that which exists in California Public Utilities Code Sections 6291 and 6292. These statutes empower municipalities to include in their franchises provisions that allow forfeiture of a franchise if the grantee fails, neglects, or refuses to perform any franchise obligation after having been given a 10-day notice to cure. Section 12 of the 1970 Franchises varied from the 10-day notice by allowing 30 days’ notice. In addition, the 1970 Franchises specified that a majority, and not a super-majority, of the City Council could forfeit the Franchises.

B. **Section 15(a):** This subsection is now titled “Interpretation.” The first three sentences concerning the importance and materiality of each term of the Franchise remains intact.

As negotiated, if dispute resolution as described in Section 17 does not resolve the "issue," "then the remedies in this Section 15(a) [written demand, opportunity to cure], (b) [breach where termination is not sought], (c) [breach where termination is sought], (f) [liquidated damages], and (g) [liquidated damages for breach of specified conditions] shall apply. If Grantee fails, neglects, or refuses to comply with any of the conditions of the Franchise, and if such failure, neglect or refusal shall continue for more than thirty (30) calendar days after written demand by the City Manager for compliance, then the City may exercise the remedies provided in Section 15."

Comment: Before a breach can be declared, the parties must participate in dispute resolution, as described in Section 17. As a general matter, dispute resolution is preferred over litigation, but this is problematic if even the most minor of disputes must be resolved by mediation and then, if unsuccessful, through litigation. The parties should endeavor to create a less cumbersome dispute resolution process through the Administrative MOU and the Undergrounding MOU.

C. **Sections 15(b)**: Under the ITB, Sections 15(b) through (e) addressed liquidated damages associated with Grantee's conduct resulting in postponement of City services or projects and other delay expenses that may not warrant forfeiture of the Franchise. Liquidated damages "represent a reasonable endeavor by the parties to estimate a fair compensation for any loss that may be sustained by the City as a result of that breach of the specified condition for that period." Under the ITB, the City could recover liquidated damages and actual damages.

Liquidated damages are now addressed in Sections 15 (f) and (g). As negotiated, "the City may either collect liquidated damages under Section 15(g) *or* pursue alternative remedies for breach under Sections 15(b) and (c), but may not pursue both." Sections 15(f) and (g) also cap the time period for which the City may pursue its claims against Grantee. Also, "[d]uring the pendency of any disputed liquidated damage assessment period, the parties shall engage in dispute resolution as provided in Section 17, and any resulting decision by a court of competent jurisdiction shall control regarding the payment of the liquidated damages set forth in this Section 15(f)."

Liquidated damages are reduced to one-tenth of the amounts in the ITB as follows:

- Damages are reduced from $6,000 to $600 per calendar day for delay and disruption pertaining to Grantee's failure to deliver facility location records and electricity facility drawings and other engineering record information;

- Damages are reduced from $15,000 to $1,500 per calendar day for Grantee's failure to timely coordinate, bear costs, and physically relocate facilities at the City Manager's direction;

- Damages are reduced from $15,000 to $1,500 per calendar day for Grantee's failure to provide and pay for standby engineers for protection of Grantee facilities.

Comment: The liquidated damages provisions, intended to encourage timely compliance with the Franchise, would not incentivize Grantee's performance and are unlikely to be used. Liquidated damages can only be triggered after dispute resolution fails and a court intervenes. Further, if the City invokes liquidated damages, it will lose the ability to seek alternative remedies for breach.

D. **New Section 15(b):** The Franchise adds a new Section 15(b) titled "Breach of the Franchise: Remedies Aside from Termination." It provides that if the Grantee breaches the Franchise by failing, neglecting, or refusing to comply with any of the conditions of the Franchise, and this breach continues for more than 30 calendar days after written notice demanding compliance from the City Manager, then the City "may" invoke the dispute resolution procedures of Section 17, "and upon obtaining a final and non-appealable judgment that the Franchise has been breached from a court of competent jurisdiction," may obtain all rights and remedies allowed by law with the exception of termination, including money damages, declaratory relief, specific performance, and mandatory injunction. The City would not lose its right to terminate, which is now described in a new Section 15(c).

Comment: If dispute resolution does not lead to a satisfactory result, the City must litigate.

E. **Section 15(c):** The Franchise adds a new Section 15(c), titled "Breach of the Franchise: The Remedy of Termination." In addition to the rights and remedies described in Section 15(b), "if the City Manager in consultation with the City Attorney recommends that the City terminate the Franchise, by proposing a resolution to the City Council to terminate the Franchise, the City may then, after obtaining a two-thirds vote of the members of the City Council, terminate the Franchise and all the rights, privileges and the Franchise shall be at an end." In such case, Grantee must "immediately" surrender all rights and privileges in and to the Franchise and refund portions of the Bid Amount to Grantee as described in Section 4, titled "Compensation."

Comment: This subsection replaces the provisions of Section 3(b) of the ITB, which provided that the second 10-year term could be voided if the Mayor recommended, and two-thirds of the Council agreed by public vote, that Grantee did not fulfill the requirements of the Cooperation Agreement.

As negotiated, the Mayor, in consultation with the City Attorney, may recommend that the City Council terminate the Franchise at any time for breach upon a two-thirds vote. The parties must first exhaust the dispute resolution requirements of Section 15(b), which could involve litigation if the parties are not satisfied. The City would be responsible for a pro rata refund of the Bid Amount as described in Section 4, Compensation. Although the termination process is not fleshed out, the materials presented to the City Council for a final determination would likely include information that evidences a breach has occurred.

F. **Section 15(d):** The Franchise adds a new Section 15(d) titled "The City's Right to Void the Automatic Renewal for Secondary Term." This provision affirms that the City may void the automatic renewal for the secondary term by a two-thirds vote of the City Council that would occur no later than 30 calendar days prior to the 10th anniversary of the Effective Date, and no earlier than the ninth anniversary of the Effective Date. Voiding the automatic renewal does not require a finding of any breach by Grantee. If the automatic renewal is voided, the City must refund portions of the Bid Amount to Grantee as described in Section 4, titled "Compensation." The parties would not need to participate in dispute resolution, as described in Section 17, before exercising this option.

G. **Section 15(e):** The Franchise adds a new Section 15(e) titled "Termination due to Municipalization Ordinance." This section describes the City's right to terminate the Franchise if the City Council, or the electors of the City, adopt an ordinance to municipalize the City's electric services pursuant to San Diego Charter Section 104 or other Applicable Law. If such termination were to occur, the City must refund portions of the Bid Amount to Grantee as described in Section 4, titled "Compensation." The parties would not need to participate in dispute resolution, as described in Section 17, before exercising this option.

Comment: The City's right to terminate the franchise to provide electric services to City residents and businesses as a municipality is a right reserved to municipalities and their electors in Article XI of the California Constitution and Section 1 of the City Charter. This language recognizes this reserved right, but adds a provision requiring the City to refund a portion of the Bid Amount if municipalization occurs during the franchise term.

XIV. CHANGES TO SECTION 16

A. **Section 16:** The Franchise adds a new Section 16 titled "Survivability," which provides that certain sections of the Franchise will survive beyond termination of the Franchise. Those sections include Section 1 (Definitions), Section 4(e)(6) (Compensation), Section 15(b), (c), (d) and (e) (Forfeiture, Termination, and Other Remedies), Section 16 (Severability), Section 17 (Dispute Resolution), Section 18 (Publication Expense), Section 19 (Authority for Grant), Section 20 (No Transfer Without Consent), Section 21, (Right of City Electors), Section 22 (Performance Bond), Section 23 (Bankruptcy), Section 24 (Acquisition and Valuation), Section 25 (Severability), and Section 26 (Effective Date). In addition, the insurance required of Grantee in Section 13 must be maintained until it fulfills its obligations to the City.

Comment: The list of subsections that survive termination does not include the completion of undergrounding construction projects begun under Section 10, which could create practical and legal problems if the franchise is terminated in the middle of ongoing undergrounding projects. This is a policy issue that may be addressed in the Undergrounding MOU.

XV. CHANGES TO SECTION 22

A. **Section 22:** The ITB required Grantee to provide a performance bond in the amount of $30 million. In the Franchise, the bond amount is reduced to $5 million. In addition, the City will be required to prove that Grantee caused actual damage to the City.

Comment: Performance bonds guarantee the performance of contracted work. If Grantee fails to perform, the City may tap the performance bond to complete the work that Grantee failed to perform. As revised, the City must prove that Grantee caused damages to the City, which in and of itself can lead to disputes. Ultimately, the amount of a performance bond is a policy decision and does not preclude the City from seeking relief through other available legal remedies.

CONCLUSION

This Report is intended to assist the Council in its review of critical legal agreements and background information that will impact the City's General Fund and its provision of gas and electric services for up to 20 years. We encourage a throrough review of the Franchises and affiliated documents, as well as consultant reports prepared by NewGen Strategies & Solutions and JVJ Pacific Consulting, LLC. We are available should you have any questions.

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By /s/ Mara W. Elliott

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