



CITY OF
**PALO
ALTO**

City Council Staff Report

From: City Manager
Report Type: ACTION ITEMS
Lead Department: Utilities

Meeting Date: March 27, 2023
Staff Report: 2303-1034

TITLE

Approval of and Direction on a Residential Natural Gas Rebate Program Funded by the City's General Fund at a Total Cost of up to \$1,771,586 to Mitigate Extraordinarily High January 2023 Natural Gas Costs, Approval of a Budget Amendment in the General Fund, and an Update on *Green v. City of Palo Alto*

RECOMMENDATION

Staff recommends City Council:

1. Approve a residential natural gas rebate program intended to mitigate extraordinarily high January 2023 natural gas costs, with a calculation option of either:
 - a. A consumption based rebate equivalent to 20% of the January 2023 gas bill
 - OR**
 - b. A flat rate of \$80.78 on an average January gas bill of \$403.90.
2. Amend the Fiscal Year 2023 Budget Appropriation (requires a 2/3 majority vote):
 - a. In the General Fund by:
 - i. Increasing the Transfer to the Gas Fund by \$1,771,586, and
 - ii. Decreasing the Budget Stabilization Reserve by \$1,771,586;
 - b. In the Gas Fund by:
 - i. Increasing the Transfer from the General Fund by \$1,771,586, and
 - ii. Decreasing Revenue from Residential Customers by \$1,771,586.

EXECUTIVE SUMMARY

In January 2023, natural gas commodity prices spiked to levels not seen since 2001, from an average of \$1 per therm to \$4 per therm. Since then, the March 2023 gas commodity price has decreased back to the average 2022 price of \$0.77 per therm.

As a result of the extraordinary high natural gas price spike, many residential customers in Palo Alto are suffering the economic burden of extreme and unexpectedly high gas bills. Given the General Fund surplus from FY 2022, City Council directed staff on February 13, 2023 to propose a rebate to gas residential customers of up to 20% based on the highest month of bills. In

response, staff analyzed January 2023 residential natural gas bills with service periods of January 1, 2023 through January 31, 2023.

This report outlines the total number of residential gas customers, average bill amounts, and different rebate options for Council's consideration. There are several ways to establish this type of a program. Two options for Council consideration are:

Option 1: A consumption-based rebate for all January 2023 residential natural gas customers equivalent to 20% of their January 2023 gas bill;

Option 2: A flat rebate of \$80.78 for all January 2023 residential natural gas customers based on an average January residential gas bill of \$403.90.

Both options would be funded by a General Fund transfer to the Gas Fund of up to \$1,771,586 which includes 600 customers who terminated service from the City since January 2023. As an alternative, Council could consider not including these customers, which would reduce the total rebate by approximately \$243,340 for option 1 or \$50,000 for option 2.

In addition, this report provides an update on the City's recent settlement agreement in *Green v. City of Palo Alto*, which will result in refunds to most City gas customers if the settlement is approved by the courts.

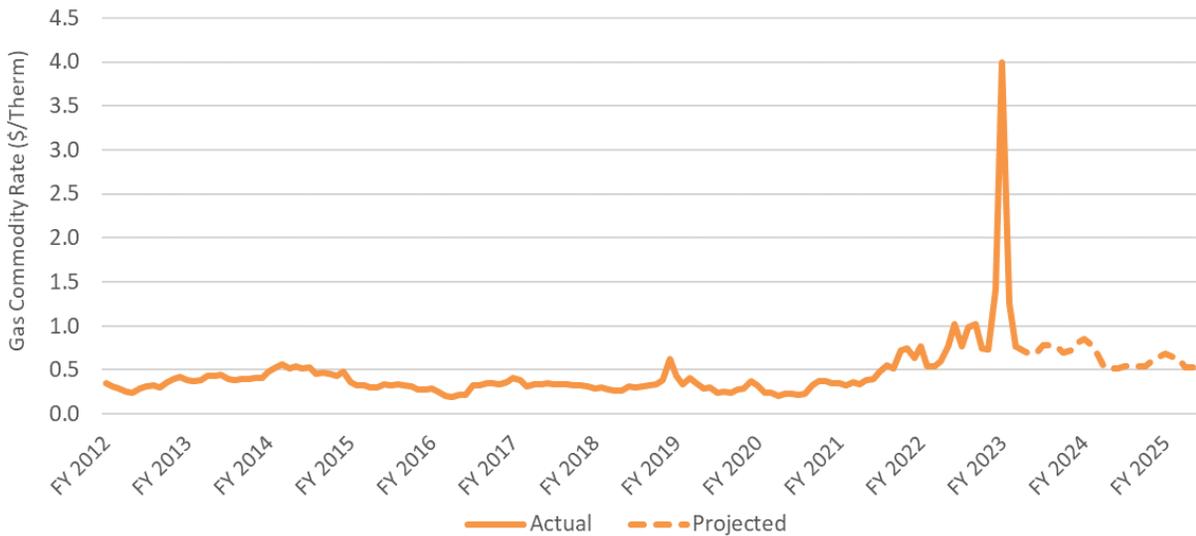
BACKGROUND

In 2000-01 the California energy crisis occurred, causing major disruptions to gas supply costs. Wholesale gas prices rose over 500% between January 2000 and January 2001. The Council approved drawing down reserves to provide ratepayer relief and, for two years following the crisis, City of Palo Alto Utilities (CPAU) rates were above PG&E's as reserves were replenished.

In April 2001 the Council approved a hedging practice of buying fixed price gas one to three years into the future. After reaching a low point in October 2001, prices continued to rise, and the CPAU hedging strategy frequently resulted in a wholesale supply cost advantage compared to PG&E, until prices began to decline steeply in mid-2008. At that point the City's gas wholesale supply costs became higher than market gas prices due to fixed price contracts entered into prior to 2008. As a result, the City's gas wholesale supply costs were higher than PG&E's for several years.

In 2012 Council approved a plan to discontinue the hedging strategy and purchase all gas on the short-term ("spot") markets. Since July 1, 2012, the commodity portion of the gas rates changes every month based on the spot market gas price. As shown below, from 2012 until late 2022, gas commodity rates were very stable.

Historical and Projected Natural Gas Market Prices



Natural gas market prices were extremely high in January 2023; much higher than last year’s winter prices, and the highest since the 2001 energy crisis. Gas commodity prices for January 2023 were five times higher than January 2022 gas prices, tripling some customers’ gas bills. The February and March 2023 gas commodity rates are \$1.26 and \$0.77 per therm; significantly lower than January 2023 rate of \$4.00 per therm. CPAU’s monthly gas commodity and volumetric rates are available on the Utility’s residential rates page.¹

Gas customers across California are experiencing similar impacts. Gas market prices can fluctuate greatly from month to month due to trade issues, weather, and supply or production challenges. The unusually high prices this winter have been attributed to historically cold weather, high gas demand, low regional gas storage levels, constraints on gas supplies flowing into California, and an increased reliance on natural gas in the electric power sector as a result of the ongoing drought’s impact on hydroelectric supplies. CPAU purchases natural gas for its customers at market prices, and does not control those market prices, nor mark-up the cost of the gas purchased on behalf of its customers.

Even with the City using reserves (\$2.5 million) to mitigate the price increases and not passing the full cost of January gas through to customers, residents are greatly impacted by these cost increases. The City is providing free access to the Home Efficiency Genie program, sharing energy saving tips, enrolling eligible customers to the rate assistance program, and offering special payment plan arrangements for those who need extra time paying their winter gas bills for six to eight months. The stability of current and future gas rates is important to CPAU customers. As

¹ Utility’s Residential Rates <https://www.cityofpaloalto.org/files/assets/public/utilities/rates-schedules-for-utilities/monthly-gas-commodity-rates.pdf>

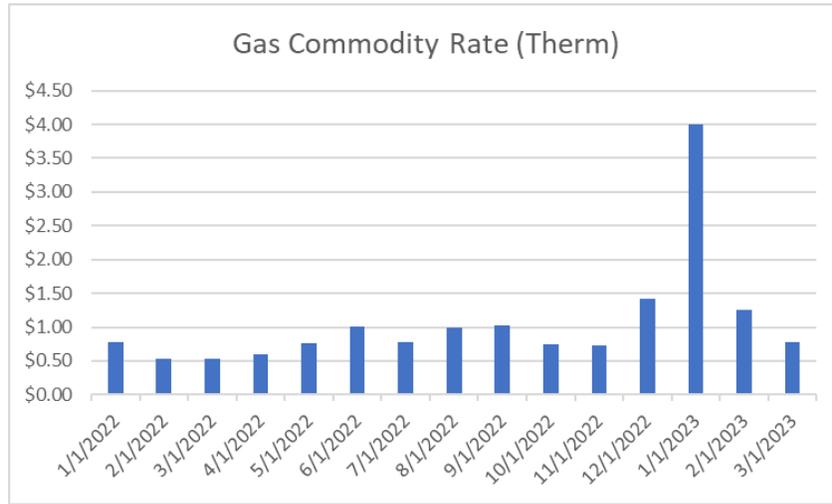
such, staff plans to propose seasonal hedging alternatives to Council that could mitigate future gas commodity market price spikes.

ANALYSIS

Late last year, staff anticipated that the January 2023 gas commodity price would exceed the utility's commodity rate cap of \$2/therm, based on monthly forward price data suggesting it would settle around \$3.50/therm. To that end, in December, Council approved staff's recommendation to double the commodity rate cap to \$4/therm (Staff Report #15047)² effective January 1, 2023. The settled commodity price at Citygate index for January 2023 reached \$5/therm. As a result, the gas utility covered commodity costs that exceeded the \$4/therm cap by drawing down approximately \$2.5 million in Gas reserves.

² Staff Report 15047 <https://www.cityofpaloalto.org/files/assets/public/agendas-minutes-reports/agendas-minutes/city-council-agendas-minutes/2022/20221219/20221219pccsm-amendedtime.pdf>

**2022 – 2023 YTD Actual Gas Market Commodity Costs
Incurred by Gas Utility Customers**



Staff analyzed January 2023 residential natural gas bills for the service period from January 1, 2023 through January 31, 2023. CPAU had a total of 21,931 residential gas customers in January 2023. The total January 2023 residential gas retail commodity charges were \$8.9M, compared to \$4.8M in December 2022 when the commodity cost was \$1.42 per therm. Gas residential bills for January 2023 were as follows:

| Jan. 2023 Gas Residential Bill Range | % of Total Residential Gas Customers | # of Residential Gas Customers |
|---|---|---------------------------------------|
| Greater than \$1,000 | 4.4% | 973 |
| \$500 to \$1,000 | 27.5% | 6,034 |
| \$150 to \$500 | 43.7% | 9,582 |
| Less than \$150 | 24.4% | 5,342 |

On February 13, 2023, as part of the City Council adoption of the mid-year budget actions, the Council directed staff to develop a residential gas rebate program. This report offers additional information for Council to consider adopting such a program.

Two options for consideration include:

Option 1: Consumption-based rebate for all January 2023 residential natural gas customers equivalent to 20% of their January 2023 gas bill.

The average rebate under Option 1 will range from \$2.39 for customers with January 2023 gas bills less than \$20, to \$609.50 for customers with January 2023 gas bills greater than \$2,000.

Option 2: Flat rebate of \$80.78 for all January 2023 residential natural gas customers, based on an average January residential gas bill of \$403.90.

The average residential gas customer used 76.1 therms in January 2023 and was billed \$403.90. \$80.78 represents 20% of the average residential January 2023 gas bill.

The table below shows rebate amounts under both options. The total cost to the General Fund of the rebates under either option will be up to \$1,771,586. It is important to note that 600 customers during this period have terminated service from the City since January 2023. The Council can consider not including these customers in the rebate program which would reduce program costs by \$243,340 for option 1 or \$50,000 for option 2.

Jan. 2023 Residential Gas Rebate Amounts and Costs

| Jan. 2023 Gas Bill Range | Number of Accounts | % of Total Accounts | Total Gas Retail Bill Charges; Jan. 2023 | Average Jan. 2023 Gas Bill | Cost of Option 1; 20% Rebate Amount | Cost of Option 2; Flat \$80.78 Rebate | Option 1; Average Customer Rebate at 20% Level | Option 2; Flat Rebate |
|--------------------------|--------------------|---------------------|--|----------------------------|-------------------------------------|---------------------------------------|--|-----------------------|
| < \$20 | 996 | 4.5% | \$ 11,885 | \$ 11.93 | \$ 2,377 | \$ 80,457 | \$ 2.39 | \$ 80.78 |
| \$20 - \$49.99 | 1,019 | 4.6% | \$ 36,822 | \$ 36.14 | \$ 7,365 | \$ 82,315 | \$ 7.23 | \$ 80.78 |
| \$50 - \$99.99 | 1,849 | 8.4% | \$ 138,420 | \$ 74.86 | \$ 27,684 | \$ 149,362 | \$ 14.97 | \$ 80.78 |
| \$100 - \$149.99 | 1,478 | 6.7% | \$ 184,444 | \$ 124.79 | \$ 36,889 | \$ 119,393 | \$ 24.96 | \$ 80.78 |
| \$150 - \$199.99 | 1,440 | 6.6% | \$ 250,927 | \$ 174.25 | \$ 50,185 | \$ 116,323 | \$ 34.85 | \$ 80.78 |
| \$200 - \$299.99 | 2,850 | 13.0% | \$ 715,232 | \$ 250.96 | \$ 143,046 | \$ 230,223 | \$ 50.19 | \$ 80.78 |
| \$300 - \$399.99 | 2,735 | 12.5% | \$ 954,365 | \$ 348.95 | \$ 190,873 | \$ 220,933 | \$ 69.79 | \$ 80.78 |
| \$400 - \$499.99 | 2,557 | 11.7% | \$ 1,146,966 | \$ 448.56 | \$ 229,393 | \$ 206,554 | \$ 89.71 | \$ 80.78 |
| \$500 - \$599.99 | 2,184 | 10.0% | \$ 1,196,926 | \$ 548.04 | \$ 239,385 | \$ 176,424 | \$ 109.61 | \$ 80.78 |
| \$600 - \$699.99 | 1,623 | 7.4% | \$ 1,049,637 | \$ 646.73 | \$ 209,928 | \$ 131,106 | \$ 129.35 | \$ 80.78 |
| \$700 - \$799.99 | 1,050 | 4.8% | \$ 784,075 | \$ 746.74 | \$ 156,815 | \$ 84,819 | \$ 149.35 | \$ 80.78 |
| \$800 - \$899.99 | 704 | 3.2% | \$ 596,422 | \$ 847.19 | \$ 119,284 | \$ 56,869 | \$ 169.44 | \$ 80.78 |
| \$900 - \$999.99 | 473 | 2.2% | \$ 447,375 | \$ 945.82 | \$ 89,475 | \$ 38,209 | \$ 189.16 | \$ 80.78 |
| \$1,000 - \$1,499.99 | 786 | 3.6% | \$ 924,556 | \$ 1,176.28 | \$ 184,911 | \$ 63,493 | \$ 235.26 | \$ 80.78 |
| \$1,500 - \$1,999.99 | 110 | 0.5% | \$ 185,125 | \$ 1,682.95 | \$ 37,025 | \$ 8,886 | \$ 336.59 | \$ 80.78 |
| > \$2,000 | 77 | 0.4% | \$ 234,657 | \$ 3,047.50 | \$ 46,931 | \$ 6,220 | \$ 609.50 | \$ 80.78 |
| Grand Total | 21,931 | | \$8,857,834 | \$ 403.90 | \$ 1,771,567 | \$ 1,771,586 | | |

The City of Palo Alto also provides several financial assistance programs. As of March 2023, approximately 700 customers are on the utilities rate assistance program³, which provides a 25%

³ Rate Assistance Programs <https://www.cityofpaloalto.org/Departments/Utilities/Residential/Utilities-Assistance>

discount based medical and financial need. The City has received 185 new rate assistance enrollments since January 1, 2023.

Due to the unprecedented natural gas price spike, other gas utilities are also in the process of establishing financial relief programs.

- The City of Long Beach⁴ will develop a program with approximately \$1.5 million intended to reach those most in need. The program will focus on providing financial relief to Long Beach residential customers, particularly those who are low income, disabled and seniors on fixed income. Long Beach will divert any unplanned 5% utility user tax revenues to fund the assistance program.
- San Diego Gas & Electric (SDG&E)⁵ announced a pair of programs to help customers who have seen high utility bill increases due to wholesale natural gas price spikes. SDG&E will set aside \$6 million to provide one-time financial assistance of up to \$600 for customers who may not qualify for low-income rate assistance but are at risk of service disconnection due to arrearage. Another \$10 million will be budgeted for vulnerable and low-income residents. A total of \$16 million to fund the programs will come from shareholders, not ratepayers.

Green v. City of Palo Alto Update

The pending resolution of *Green v. City of Palo Alto* (Case No. 16CV300760), the 2016 class action lawsuit which challenged the City's gas and electric rates, will also provide refunds to most City gas customers. In June 2021, the Santa Clara Superior court judge held that the City's gas rates were taxes requiring voter approval under California's Proposition 26, because they were set at a level sufficient to fund the annual transfer to the City's general fund.⁶ The City has since negotiated a settlement with plaintiff's counsel which will allow the City to provide refunds to ratepayers more quickly than if the parties continued through the appeals process.⁷

While the precise timing is unknown, the City set aside funding sufficient to pay all refunds due under the settlement as soon as the trial court approves.

As part of the settlement, both sides jointly requested that the Court of Appeal approve a stipulated (agreed-upon) reversal of the trial court judgment, and direct the trial court to enter

⁴ The City of Long Beach

<https://www.publicnow.com/view/1651AC037FF028C6906782E18F784A7A7417A6CB?1675360833>

⁵ San Diego Gas and Electric <https://www.sdge.com/residential/pay-bill/get-payment-bill-assistance/bill-payment-options-temporary-financial-help/one-time-assistance-bill-assistance#:~:text=If%20you're%20experiencing%20temporary,visit%2021%20San%20Diego%20online>

⁶ The trial court found the City's electric rates did not violate Proposition 26.

⁷ In November 2022, City voters also approved Measure L, affirming a general fund transfer of up to 18% of gas utility revenues, effective immediately.

a new judgment consistent with the terms of the parties' settlement agreement. Those terms are as follows:

1. The City will pay \$17,337,111 in refunds to gas customers to settle 8 years of gas rate claims (September 23, 2015 – June 30, 2022), allocating funds based on the terms of gas customers consumed during the relevant periods.⁸
2. Current customers will receive refunds via on-bill credits over 2 years: one-third credited 90 days after the trial court signs the final settlement order, one-third 12 months later, and the final third 24 months after the order.
3. Former gas customers will be mailed a check for their total overpayment within 150 days after the final settlement order is signed, and current customers in ill-health or over age 65 may request refunds by check instead of on-bill credits.

Implementation of the settlement agreement and refund payments will require approval and action by both the District Court of Appeal and the trial court, with the Court of Appeal expected to rule on the parties' motion for stipulated reversal by mid-April. After that, the trial court must take several procedural steps, including consolidating the customer groups into a single class, directing the parties to give notice to the class, and entering an order approving the settlement.

If the trial court approves the settlement agreement, individual refund amounts will vary because they will be based on the amount of gas consumed during the time period covered by the lawsuit. For example, a residential customer who used the median amount of gas consumed from September 23, 2015 through June 30, 2022 would receive approximately \$156. The City hopes to receive approval to issue refunds as soon as possible, which is especially timely in light of recent gas price spikes. If the courts do not approve the parties' settlement, both sides anticipate relitigating their appeals.

FISCAL/RESOURCE IMPACT

Gas Residential Rebate Program

The City's General Fund will provide full funding of the gas residential rebate program through a transfer to the Gas Fund. The General Fund receives a five percent utility users tax (UUT) on monthly electric, gas, and water bills, under Chapter 2.35 of the Palo Alto Municipal Code. The City received \$444,438 in UUT for January 2023 gas residential bills compared to \$242,521 in December 2022. The unplanned increase in UUT revenue will be recorded in the General Fund Budget Stabilization Reserve, which will be used to fund the transfer to the Gas Fund for the rebate program.

⁸ Refunds will be allocated accordingly: 26% to customers active from September 2015-June 2016; 21% to customers active during FY 2017 and 2018, 13% to customers active during FY 2019; 23% to customers active during FY 2020; and 17% to customers active during FY 2022. No refunds are due for gas rates collected in FY 2021 and after June 30, 2022 because the gas utility operated at a loss for those years, even excluding the general fund transfer. Customers who opted to be excluded from the settlement, as well as the judge assigned to the case, will not receive refunds.

Green v. City of Palo Alto

The resolution of *Green v. City of Palo Alto* will also have fiscal impacts for the City's gas ratepayers and the general fund. If the trial court approves the settlement agreement, individual refund amounts will be based on the amount of gas consumed during the time period covered by the lawsuit. For example, a residential customer who used the median amount of gas consumed from September 23, 2015 through June 30, 2022 will receive approximately \$156. The City has set aside funding in the General Fund sufficient for a claims administrator to pay all refunds (approximately \$17.4M) due under the settlement as soon as the trial court approves, via on-bill credits and refund checks, as applicable.

TIMELINE

Gas Residential Rebate Program

Depending on whether any configuration is required in the SAP billing system, staff can post a gas rebate credit on a customer's bill in two to four weeks. Under the two weeks scenario, the rebate will appear on the customer's bill as "Miscellaneous Credit." If Council prefers to modify the rebate description on the utility bill to "Gas Rebate" or another label, it may require an additional two weeks for system configuration change, testing, and validation. After the rebates are posted, customers will begin receiving their gas rebates in mid or late April depending on their billing cycle. For those 600 customers who have terminated services, a bill credit would not be feasible; staff would explore alternatives including issuing individual checks to known forwarding information if available.

Green v. City of Palo Alto

The City expects a mid-April decision from the Court of Appeal on whether it has approved the parties' joint motion for stipulated reversal and directed the trial court to approve the parties' settlement. The trial court's timeline for notice to the class and a decision on the final settlement order is unknown, but could take several months. In the meantime, the City has set aside funding sufficient for a claims administrator to pay all refunds due under the settlement as soon as the trial court approves, via on-bill credits and refund checks, as applicable.

STAKEHOLDER ENGAGEMENT

When the City learned of the higher gas prices in late November and early December, City staff informed customers in advance through utility bill messaging, social media, Nextdoor, email newsletters, website, and other community forums, to take action and save energy to try to avoid surprisingly high utility bills.

As noted above, the City's Utilities Director shared a message on the City's community message portal at medium.com about the high gas utility costs with information on ways the City can assist residents through this challenging time. The message also answers community questions about the unprecedented high gas costs. For this communication go here⁹: <https://medium.com/paloaltoconnect/in-the-public-interest-28a7d9ecb0df>

⁹ City Community Message Portal <https://medium.com/paloaltoconnect/in-the-public-interest-28a7d9ecb0df>

The City is offering resources to help customers with higher than anticipated utility bill costs this winter, with access to free home efficiency assessments through the Home Efficiency Genie, payment arrangements, tips for no-cost and low-cost energy efficiency at cityofpaloalto.org/efficiencytips¹⁰, and more. Customers are encouraged to contact Utilities Customer Service at [\(650\) 329-2161](tel:6503292161) or UtilitiesCustomerService@cityofpaloalto.org if they have questions about their utility bill or need assistance.

ENVIRONMENTAL REVIEW

Council's approval of the rebate programs described in this report does not meet the definition of a project for the purposes of the California Environmental Quality Act under Public Resources Code 21065. Environmental review is not required.

APPROVED BY:

Dean Batchelor, Director Utilities

Staff: Jonathan Abendschein, Assistant Director Utilities

¹⁰ City Energy Efficiency Tips <https://www.cityofpaloalto.org/Departments/Utilities/Residential/Home-Efficiency-Genie/Efficiency-Tips>