

**SAN JOSE CLEAN ENERGY**  
(An Enterprise Fund of the City of San José)

Independent Accountant's Report on  
Applying Agreed-Upon Procedures

For the Year Ended June 30, 2020



Certified  
Public  
Accountants

**SAN JOSE CLEAN ENERGY**  
(An Enterprise Fund of the City of San José)  
For the Year Ended June 30, 2020

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## Independent Accountant's Report

Honorable City Council and  
Risk Oversight Committee  
San José, California

We have performed the procedures enumerated below on the City of San Jose's (City) compliance with the Clean Energy Risk Management Regulations effective October 3, 2019 for the year ended June 30, 2020. The City's management is responsible for the City's compliance with those requirements.

The City's Finance Department, Community Energy Department (CED), City Attorney's Office, and the Office of the City Auditor have agreed to and acknowledged that the procedures performed are appropriate to meet the intended purpose of assisting specified parties in evaluating whether the City complied with the Clean Energy Risk Management Regulations effective October 3, 2019 for the year ended June 30, 2020. This report may not be suitable for any other purpose. The procedures performed may not address all items of interest to a user of this report and may not meet the needs of all users of this report and, as such, users are responsible for determining whether the procedures performed are appropriate for their purposes.

The procedures and the associated findings are as follows:

1. We obtained the Northern California Power Agency (NCPA) and Weekly Management Reports for the last full week of each quarter for the year ended June 30, 2020 and reviewed the reports for regular update of load and resources forecasts as evidence of monitoring and measuring the supply portfolio against estimated demand.

Finding: No deviations were found as a result of applying the procedure.

2. We obtained the Risk Management Regulations (RMR) Concentration Report as of December 31<sup>st</sup> and June 30<sup>th</sup> and reviewed energy confirmation for counterparties that have a 10% or higher concentration rate to ensure that the City has complied with the concentration limits identified in Section 15.2 of the RMR.

Finding: No deviations were found as a result of applying the procedure. We reviewed the Risk Management Regulations (RMR) Concentration Report as of December 11, 2019 and June 24, 2020, as these reports were the closest dates available for the December 31<sup>st</sup> and June 30<sup>th</sup> dates requested in the procedure, respectively. There were no reports available for the quarter ending December 31, 2019 and June 30, 2020.

3. We obtained the Approved Counterparty logs for counterparties SJCE has entered into agreements with for the year ended June 30, 2020 and reviewed supporting documents to show that the City has managed counterparty liquidity risk by:
  - a) Regular, up-to-date credit evaluations
  - b) Requiring collateral in accordance with the RMR.

Finding: No deviations were found as a result of applying the procedure.

4. We obtained the Banking Services Agreement with Wells Fargo Bank and the bank statement balance as of June 30, 2020 and determined that the City has managed custodial credit risk by keeping deposits at FDIC insured institutions below insurance thresholds, or maintaining minimum 100% collateral, and actively monitoring the creditworthiness of the custodian.

Finding: No deviations were found as a result of applying the procedure.

5. We obtained the Approved Counterparty Log and the Finance Counterparty Credit Analysis Procedures (Procedures) as of June 30, 2020 and reviewed to determine if counterparty credit assessment and monitoring were performed by reviewing evidence of counterparty diversification, credit risk premium, covenants, posting collateral.

Finding: No deviations were found as a result of applying the procedure.

6. We judgmentally selected ten individual Transmittal Sheets from each quarter of the year ended June 30, 2020 and determined whether the executed transactions are within transaction term limits and transaction volume limits authorized in Appendix 4 of the RMR.

Finding: No deviations were found as a result of applying the procedure. However, there was no complete population of transmittal sheets with date of executed transactions, thus, we selected from Awarded Contract List with term start dates. Based on the term start date listed on the Awarded Contract list, only two transmittal sheets were selected for the quarter ended September 30, 2019 and none for the quarter ended December 31, 2019, as only two transmittal sheets had term start dates that began within the quarter ended September 30, 2019 and none had start dates within the quarter ended December 31, 2019. Therefore, we selected a total of 22 items for this procedure.

7. We obtained the Revolving Credit Agreement with Barclays Bank and the City's bank statements for the year ended June 30, 2020 and determined whether the City funded an operating reserve, and ensured the department has a credit facility to support cash flow needs.

Finding: No deviations were found as a result of applying the procedure.

8. We obtained and reviewed agreements with and invoices for power purchase and sale agreements for the months of December 2019 and June 2020 ensuring (a) counterparty representatives are authorized by the counterparty and (b) long-term power purchase and sale agreements are approved as to form by the City Attorney and reviewed by appropriate legal and market experts.

Finding: We are unable to verify for seven out of eight short-term power purchase agreements whether the City Attorney's Office reviewed and approved the power purchase agreements, as there is no documentation indicating reviews or approvals kept on file. There are no agreements related to sale transactions. There are no long-term power purchase and sale agreements entered into for the months of December 2019 and June 2020. No other deviations were found as a result of applying the procedure.

9. We obtained a copy of the Load Resource Balance for the months of December 2019 and June 2020 and recalculated the coverage ratios reported by the City for the purposes of complying with the Recommended Coverage per Appendix 9 (see attached Schedule A) of the RMR.

Finding: We noted during our review of the Load Resource Balance for the Months of December 2019 and June 2020 that there are no reported Year 3 and Year 4 coverage ratios.

In addition, the City did not meet the minimum coverage per Appendix 9 of the RMR for the following:

<b>December 2019</b>	<b>Period</b>	<b>Actual Coverage</b>	<b>Minimum Coverage</b>	<b>Maximum Coverage</b>	
Prompt Quarter	January 2020	82%	90%	115%	
	February 2020	87%			
Next Quarter	June 2020	72%	85%	115%	
Prompt Year	July 2020	72%	80%	110%	
	August 2020	74%			
	November 2020	78%			
	December 2020	76%			
	January 2021	49%			
	February 2021	48%			
	March 2021	54%			
	April 2021	49%			
	May 2021	48%			
	June 2021	40%			
	Year 2	July 2021	39%	50%	90%
		August 2021	40%		
September 2021		43%			
October 2021		46%			
November 2021		44%			
December 2021		43%			
	January – June 2022	Not Reported			
Year 3	July 1, 2022 – June	Not Reported	30%	75%	
Year 4	July 2023 – June 30,	Not Reported	0%	50%	

<b>June 2020</b>	<b>Period</b>	<b>Actual Coverage</b>	<b>Minimum Coverage</b>	<b>Maximum Coverage</b>
Prompt Year	January – December 2021	63% - 78%	80%	110%
Year 2	January – December 2022, except for May 2022	39% - 47%	50%	90%
Year 3	July 1, 2022 – June 30,	Not Reported	30%	75%
Year 4	July 2023 – June 30, 2024	Not Reported	0%	50%

10. We compared the description of the types of Energy products listed in the Expected Power Cost Workbook for the months of December 2019 and June 2020 with the list of Energy products that are listed as authorized and consistent with the Appendix 6 of the RMR.

Finding: No deviations were found as a result of applying the procedure.

11. We obtained Expected Power Cost Workbook, Power Contract Tracking Report, and Approved Counterparty Log Master Workbook for the months of December 2019 and June 2020;

judgmentally selected 10 transactions; and obtained additional documentation to determine whether the City meets the permitted transactions and approved product requirements of the RMR, as follows:

- a) Transactions are duly authorized and within risk limits, and shall not cause individual counterparty credit limits to be exceeded.
- b) Transactions shall utilize contract terms intended to minimize the risk of loss if a counterparty fails to deliver, take delivery or pay for transactions provided.
- c) Transactions are executed and documented following standardized procedures.
- d) Transactions are approved as to form by the City Attorney's Office.

Finding: We are unable to verify for 13 out of 20 transactions whether the City Attorney's Office approved the transactions, as there is no documentation indicating approvals kept on file. No other deviations were found as a result of applying the procedure.

- 12. Based on the sample of transactions selected in procedure 11 above, if unauthorized transactions were observed, we reviewed the appropriate deviations report as required in Section 5.4 of the RMR as amended from time to time.

Finding: No deviations were found as a result of applying the procedure.

- 13. We reviewed the Management Reports listed in Appendix 7 (See attached Schedule B) of the RMR, such as Standing RMR Reports, Bilateral RA Transaction Reports, and Procurement and Regulatory Update Reports for the last month of each quarter, to determine whether SJCE complied with the reporting requirements, report frequency, primary responsibility, approval and deadlines.

Finding: We noted during our review of the Management Reports listed in Appendix 7 of the RMR, there were a total of 10 separate reports to be completed. The following reports were not completed and approved for the periods selected below:

<b>Report</b>	<b>Frequency</b>	<b>Period not completed</b>
Portfolio Performance Report	Weekly	Weekly report for the month of September 2019
		Weekly report for the month of December 2019
		First week report for the month of June 2020
Portfolio Risk Exposure (Open Position/ Scenario Planning)	Quarterly	No report was submitted during the fiscal year ending June 30, 2020

<b>Report</b>	<b>Frequency</b>	<b>Period not completed</b>
Credit Limit Status by Counterparty and Master Agreement Report	Weekly	1 <sup>st</sup> – 3 <sup>rd</sup> weeks of September 2019
		2 <sup>nd</sup> – 4 <sup>th</sup> weeks of December 2019
		1 <sup>st</sup> and 3 <sup>rd</sup> weeks of March 2020
		All weeks for the month of June 2020
Credit Exposure to LOC Issuers	Quarterly	Quarter ending September 2019

For the following reports listed, we are unable to verify whether it was reviewed and approved by the City, as there is no documentation indicating reviews or approvals kept on file:

<b>Report</b>	<b>Frequency</b>	<b>Period not approved</b>
Load and Resource and Concentration Balance	Quarterly	All quarters for the fiscal year June 30, 2020
Coverage Ratio – Procurement Report	Monthly	All last month of each quarter for the fiscal year June 30, 2020
Credit Exposure to LOC Issuers	Quarterly	All quarters for the fiscal year June 30, 2020

14. We reviewed an individual transaction from each quarter of the year ended June 30, 2020 and determined whether the transaction includes formal and official documentation by the City as follows:

- a) Competitive bidding or ROC approved variance authorizing bilateral negotiations.
  - i. SJCE front office manages a Request for Offers (RFO) inbox for the purposes of capturing bid solicitations.
- b) Written commitment to the transaction
  - i. SCJE front office manages an RFO inbox for the purposes of capturing bid solicitations.
- c) Confirmation the transaction with the counterparty with a written and executed confirmation
  - i. All transactions with the counterparty are memorialized with a written and executed confirmation.

- d) Authorization/Approval
  - i. Each confirmation includes a cover sheet to ensure appropriate authorization/approvals are in place.
- e) Actual product delivery
  - i. Both the Northern California Power Agency (NCPA) and the Middle Office review expected power costs and confirm the quantities match information included on confirmation. NCPA confirms the actual delivery of energy products prior to SJCE submitting invoices for payment.
- f) Billing and settlement
  - i. Both NCPA and the Middle Office review expected power costs and confirm the quantities match information included on confirmation. NCPA confirms the actual delivery of energy products prior to SJCE submitting invoices for payment.

Finding: We are unable to observe whether competitive bidding was approved for two out of four selections, as the two deviations did not have documentation indicating competitive bidding approvals kept on file. No other deviations were found as a result of applying the procedure.

- 15. We obtained listing of employees who are engaged in approved product transactions and consultants performing services for SJCE as of June 30, 2020 and reviewed completed Form 700 – Community Energy Classifications annual conflict of interest filings.

Finding: No deviations were found as a result of applying the procedure.

We were engaged by the City to perform this agreed-upon procedures engagement and conducted our engagement in accordance with attestation standards established by the American Institute of Certified Public Accountants. We were not engaged to and did not conduct an examination or review, the objective of which would be the expression of an opinion or conclusion, respectively, on the City's compliance with the Clean Energy Risk Management Regulations effective October 3, 2019 for the year ended June 30, 2020. Accordingly, we do not express such an opinion or conclusion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

We are required to be independent of the City and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements related to our agreed-upon procedures engagement.

The City's response to the deviations identified as a result of our procedures is described in the management response starting page 10. The City's response was not subjected to the procedures applied in this agreed-upon procedures engagement and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the City Council, Risk Oversight Committee, the City Auditor, and Finance Department and is not intended to be and should not be used by anyone other than these specified parties.



Walnut Creek, California  
November 17, 2021



**SAN JOSE CLEAN ENERGY**  
**(An Enterprise Fund of the City of San José)**  
**Schedule A**  
**For the Year Ended June 30, 2020**

**ENERGY RISK MANAGEMENT REGULATION APPENDIX 9**  
**RECOMMENDED COVERAGE**

SJCE will manage risks associated with its Load Obligation through procurement of energy up to four years ahead consistent with Table 1 below, and through medium and long term contracts up to 25 years in length that are consistent with SJCE’s Integrated Resource Plan (IRP). To access the market at different times, SJCE will hedge its load obligation by soliciting energy supply offers at regular intervals during favorable buying periods during the year (focusing on Spring and Fall). The Director of Community Energy, or designee, will review each solicitation; solicitation reviews shall cover pre-solicitation portfolio positions, expected coverage, procurement limits and market analysis. Supply offers will be selected with respect to the risks outlined in this document (i.e. price risk, counter party credit worthiness, concentration risk, etc.).

SJCE will seek to achieve coverage ratios consistent with Table 1 Coverage Thresholds. SJCE will apply coverage ratios within the ranges set forth in Table 1 taking into account market and system conditions during particular time periods, such as higher risks of price spikes during the Summer and early Fall, and opportunities to take advantage of low prices from favorable hydro conditions during the Spring, and schedules for natural gas storage reports.

**Table 1 Coverage Thresholds**

	Minimum Coverage	Maximum Coverage
Prompt Quarter	90%	115%
Next Quarter	85%	115%
Prompt Year	80%	110%
Year 2	50%	90%
Year 3	30%	75%
Year 4	0%	50%

From time to time, the Front Office staff may recommend procurement strategies outside of these Coverage Thresholds for ROC review and approval.

The Front Office shall prepare an Integrated Resource Plan (IRP) every two years in accordance with State law requirements and City policy. The IRP shall be presented to City Council for approval and filed with the California Public Utilities Commission. The Front Office shall propose long term transactions for approval by City Council and the ROC as appropriate and consistent with the requirements of the approved IRP.

**SAN JOSE CLEAN ENERGY**  
**(An Enterprise Fund of the City of San José)**  
**Schedule B**  
**For the Year Ended June 30, 2020**

**APPENDIX 7**  
**MANAGEMENT REPORTS**

**1. Management Reports**

The following energy risk management reports shall be developed and presented as further described in the following table:

		Primary Responsibility			Report Frequency						Approval
		Front	Middle	Back	Weekly	Monthly	Quarterly	Annual	Bi- Annual	As Needed	
a.	Load and Resource & Concentration Balance	X					X				CED Deputy Director of Power Resources
b.	Portfolio Performance (MTM)		X		X						CED Division Manager of Risk Management, Contracts and Administration
c.	Portfolio Risk Exposure (Open Position)/Scenario Planning		X				X				CED Division Manager of Risk Management, Contracts and Administration
d.	Exceptions Report		X							X	CED Division Manager of Risk Management, Contracts and Administration
e.	Master Agreements	X						X			CED Deputy Director of Power Resources
f.	Annual Regulations Update		X					X			CED Division Manager of Risk Management, Contracts and Administration
g.	Credit Limit Status by Counterparty and Master Agreements	X			X						CED Division Manager of Risk Management, Contracts and Administration
h.	Coverage Ratio – Procurement Report	X				X					CED Deputy Director of Power Resources
i.	Integrated Resource Portfolio	X							X		CED Deputy Director of Power Resources
j.	Credit Exposure to LOC Issuers		X				X				CED Division Manager of Risk Management, Contracts and Administration

**SAN JOSE CLEAN ENERGY**  
**(An Enterprise Fund of the City of San José)**  
**Schedule B**  
**For the Year Ended June 30, 2020**

**1.1. Description of Management Reports**

- a. Load and Resource Concentration Balance: The Front Office produces the Load and Resource Balance report detailing total resources by source as compared to total actual load. This report shows supply surpluses and shortages. The Load Resource and Balance report is updated weekly and presented to the ROC quarterly.
- b. Portfolio Performance (MTM): A Middle Office report comparing the cost of the portfolio of contracts, to the current market value of the portfolio (tracking what SJCE paid for the contract to what it is worth now). This is also known as MTM. The Portfolio Performance report is updated weekly and presented to the ROC quarterly. The Middle Office staff will also share this report with SJCE management on a weekly basis to monitor collateral needs.
- c. Exceptions Report: A Middle Office report summarizing current exception and violation reports. The Exception Report is developed and presented to the ROC quarterly.
- d. Annual Policies Update: A Middle Office report providing an annual review of risk management policies and procedures and recommendations for needed updates. The Annual Policies Update report is presented to the ROC annually.
- e. Credit Limit Status by Counterparty and Master Agreements: A Middle Office report showing counterparty credit limits, credit used, credit remaining, as well as current set of approved master agreements. Special flagging of counterparties nearing their credit limits should also be included. The Credit Limit Status by Counterparty report is presented to the Front Office and Back Office staff, as well as to SJCE's management on a weekly basis.
- f. Coverage Ratio – Procurement Report: A Front Office report detailing the coverage ratio and trading strategies for the next 3 years. The Procurement report is presented to the ROC monthly.
- g. Integrated Resource Plan: This is a plan prepared every 2 years by the Front Office that shows long-term supply and resources plan.
- h. Credit Exposure to LOC Issuers: This report is prepared and presented to the ROC on a quarterly basis by the Middle Office in order to track Credit Exposure to LOC issuers at the portfolio level.

**TO:** MACIAS GINI & O'CONNELL, LLP

**FROM:** Lori Mitchell

**SUBJECT:** SEE BELOW

**DATE:** November 17, 2021

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Approved

Date

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**SUBJECT: RESPONSE TO INDEPENDENT ACCOUNTANT'S REPORT ON THE CITY OF SAN JOSE'S COMPLIANCE WITH CLEAN ENERGY RISK MANAGEMENT REGULATIONS FOR THE YEAR ENDED JUNE 30, 2020**

## **BACKGROUND**

The Administration has reviewed the Independent Accountant's report on the City of San José's compliance with Clean Energy Risk Management Regulations (*Effective: October 3, 2019*) for the year ended June 30, 2020. This memorandum details the Administration's response to the findings related to several procedures detailed in the report, along with a discussion of the process improvements currently underway. The Administration greatly appreciates the work of the City Auditor and the team at Macias Gini & O'Connell, LLP (MGO) for this report.

## **PROCEDURES AND PROCESS IMPROVEMENTS**

**Procedure 2:** The Administration provided MGO with Concentration Reports as of December 11, 2019 and June 24, 2020 which had been presented in the Risk Oversight Committee (ROC) meetings as these were the closest dates available for the December 31, 2019 and June 30, 2020 dates requested in the procedure, respectively. Beginning in fiscal year 2021-2022, the Administration will ensure Concentration Reports as of December 31<sup>st</sup> and June 30<sup>th</sup> will be made available as part of procedure reviews for future fiscal years.

**Procedure 6:** For this procedure, the Administration provided MGO with an Award of Contract List with term start dates for the year ended June 30, 2020. Beginning with the procedure review for fiscal year 2020-2021, the Administration began providing a complete population of transmittal sheets with date of executed transactions and will continue to do so as part of procedure reviews for future fiscal years.

**Procedure 8:** For the short-term power purchase agreements noted in the finding for this procedure, the Administration did not provide documentation of City Attorney's Office review and approval for many of these agreements as obtaining City Attorney's Office signature approval on short-term power purchase agreements was not included as part of the contract execution process until December 2020. Since that time, the Administration is now requiring City Attorney's Office signature approval on all short-term power purchase agreements as part of the power purchase agreement execution process. It is important to note that the master enabling agreements that contain the majority of the required terms and conditions pertaining to the City's short-term transactions with energy suppliers are always reviewed and approved by the City Attorney's Office. While it has also been standard practice for the City Attorney's Office to review each short-term confirmation agreement containing the specific business terms (e.g., product type, price, quantity, etc.) of each transaction, the City Attorney's Office did not begin formally approving/signing these confirmation agreements until December 2020.

**Procedure 9:** The Administration has observed that the review requirements for this procedure do not align with the Recommended Coverage thresholds outlined in Appendix 9 of the Risk Management Regulations (RMR). The procedure requires the Load Resource Balance for the months of December 2019 and June 2020 be used to re-calculate the coverage ratios reported by the City for purposes of complying with the Recommended Coverage per Appendix 9.

As noted in the MGO finding for Procedure 9, the Load Resource Balance does not provide coverage ratios for Year 3 and Year 4. To fully support the accurate re-calculation of coverage ratios for this procedure, the Administration will amend Procedure 9 to note the use of the Power Contract Tracker (PCT) rather than the Load Resource Balance for this procedure. The PCT tracks all executed power purchase agreements and provides data for Year 3 and Year 4, thereby allowing for the accurate re-calculation of coverage ratios for all the years, as outlined in Appendix 9 of the RMR.

It is important to note that the re-calculation of coverage ratios should be performed based on the periods outlined in Appendix 9 (e.g., by quarter or by year) rather than by month as shown in the report. In addition, while the City strives to achieve the recommended coverage ratios outlined in Appendix 9, actual coverage ratios may vary from the recommended coverage ratios due to a variety of factors, including weather variations, changes in economic conditions, variations in energy price forecasts and changes in customer energy demands. For example, beginning in Spring 2020, the City adjusted its energy procurement strategy to account for the potential impact on energy demand due to the COVID-19 pandemic. This was done in order to avoid potential over-procurement in the face of the global pandemic and this change resulted in actual coverage ratios below the minimum coverage for a few periods as reported in June 2020. The potential impact of the pandemic on the expected load/energy demand of the City was presented to the ROC in Summer 2020. Also, as reported in the December 2019 ROC meeting, the actual coverage ratio was below the minimum coverage as recommended by the RMR for prompt quarter and Year 2 due to the market conditions at that time. Year 3 and Year 4 coverage ratios were not calculated since the energy demand forecasts for 2022 and 2023 were under development.

**Procedure 11:** As noted above for Procedure 8, the Administration did not provide documentation of City Attorney's Office review and approval for many short-term power purchase agreements for the year ended June 30, 2020 due to the fact that the City Attorney's Office signature approval was not included in the short-term power purchase agreement execution process until beginning December 2020. The Administration is now including City Attorney's Office signature approval on all short-term power purchase agreements as part of the execution process.

**Procedure 13:** The Community Energy Department is working to improve the process and procedures for developing and approving the energy risk management reports outlined in Appendix 7 of the RMR. As part of the annual process to amend the RMR for the fiscal year ending June 30, 2022, which is currently underway, a review of the management reports listed in Appendix 7 will be performed to ensure they align with operational needs and develop standard procedures to ensure the reports are provided to the appropriate audience and produced according to the frequency outlined in Appendix 7. An internal report approval process will also be developed to ensure reports are reviewed and approved per the requirements of Appendix 7.

**Procedure 14:** The Administration did not provide sufficient documentation indicating competitive bidding occurred on two out of four transactions selected for review. Although all four transactions did result from competitive bidding, the Community Energy Department will work to improve internal operating procedures for documenting the process for evaluating and selecting bids to ensure sufficient documentation will be available as part of procedure reviews for future fiscal years.

## **CONCLUSION**

The Administration thanks the City Auditor's Office and the team at MGO for the comprehensive review of the City's compliance with Clean Energy Risk Management Regulations. We appreciate the hard work and professionalism in conducting this review. Serving as the administrator of San José Clean Energy, the Community Energy Department began operations in 2018 and continues to explore opportunities to build and strengthen its operating procedures. The findings contained in this report will help inform many of the process improvements the City will seek to implement in the coming months.

/s/

LORI MITCHELL

Director, Community Energy Department

For questions, please contact Zachary Struyk, Assistant Director of Community Energy, at (408) 535-4868.