





CITY OF HOUSTON

Finance Department

Interoffice

Correspondence

To: Budget and Fiscal Affairs Committee

From: Kelly Dowe, Director 
Finance Department
Scott Minnix 
General Services Department

CC: Mayor Annise Parker
Jim Moncur, Deputy Director Finance

Date: November 28, 2011

Subject: **Electricity Procurement**

The purpose of this memorandum is to brief the Budget and Fiscal Affairs Committee on an upcoming request for council action regarding procurement of electricity for the City of Houston.

The City is very large consumer of electricity, spending an average of \$132 million per year on this commodity (see chart below). Prices for electricity have come down significantly over the past year. A new contract for electricity will enable savings of up to 20% per year over the current contract. An ordinance is expected to be submitted to City Council that will authorize a new contract and a competitive bidding process with delegation to the Mayor to select the winning bidder within certain parameters. The bidding process and delegation will be similar to that employed routinely with bond transactions.

Current Contract

The City's current contract is with the Texas General Land Office who subcontracts with Reliant Energy Retail Services LLC. Under the current contract the following amounts have been expended by the City on electricity:

Fiscal Year	Mwh's Used	Amount Paid
2005	1,216,467	\$101,600,650
2006	1,270,635	\$133,191,195
2007	1,239,074	\$138,232,004
2008	1,254,562	\$141,462,475
2009	1,290,833	\$147,300,817
2010	1,288,747	\$136,226,645
2011	1,244,436	\$128,288,146

This contract has been in place since April, 2004 and expires on June 30, 2013.

Cost of Electricity

A major driver of the cost of electricity is the operating efficiency of electricity generating plants. There are concerns that costs for the Texas generation fleet will go up in coming years due to implementation of environmental regulations, inadequate generating capacity and increases in demand. Specifically, the implementation of EPA's cross state air pollution rules will likely require the shutdown of at least one large low-cost, high-polluting coal plant. Cleaner but more expensive natural gas plants will be expected to replace them. However there is no

significant new plant construction underway and the Texas transmission grid is already nearing capacity.

The term "Heat Rate" is used to quantify the operating efficiency of the Texas electricity generating fleet and is a defined, commercial term used to set costs in electricity contracts. A lower Heat Rate reflects the expectation of a more efficient, lower-cost electricity generating market. A higher heat rate reflects expectations of higher-cost markets. Heat Rates can be fixed or allowed to float with the market. Future expectations are for higher Heat Rates in Texas. Concern about a higher Heat Rate is a major motivating factor for fixing the Heat Rate now for future years in a competitive bidding process.

Basic Contract Terms

Term of the new contract will be for five years. Bidders will be required to bid on a fixed price for a Heat Rate and an Adder. The Adder is a fixed amount added to the price of electricity to cover the provider's ancillary charges, administrative costs and profit margin. Additional considerations will be the provider's ability to service one of the largest accounts in Texas and to provide adequate financial security for the account.

Recommendation

The Administration recommends that the City proceed with this authorization.