Special Committee on the Future of JEA

Final Report

July 25, 2018

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1. The Special Committee

The entity that eventually became the Special Committee on the Future of JEA was created in response to activities by JEA Board Members that generated interest and concern in the community about the future of the utility. At his last meeting before leaving the board in November 2017, outgoing Board Member and former Chairman Tom Petway suggested that the time was right for the JEA to consider whether the services and financial benefits derived from a privatization of JEA would better serve its customers and the citizens of Jacksonville. New Board Chairman Alan Howard subsequently requested that JEA management engage a qualified firm to appraise the value of JEA's constituent utilities – electric, water/wastewater, and district energy. Public Financial Management (PFM - already a financial advisor to JEA) was engaged by JEA to prepare such a report, which delivered a draft copy to JEA Board members, City Council members and the Mayor's administration on February 2nd. The final report was delivered by PFM on February 14, 2018 at a Special Council Meeting with some members of the JEA Board also in attendance.

On February 20th, City Council President Anna Lopez Brosche created the Special Committee on the Potential Sale of JEA with five members (Council Members John Crescimbeni (Chair), Danny Becton, Anna Lopez Brosche, Garrett Dennis and Joyce Morgan). The committee was charged with four tasks:

- Understand all aspects and implications (who, what, when, where, and why) of a potential sale of JEA, and the roles that various parties to such a potential sale will play in the process.
- Conduct necessary meetings and hearings to gather the relevant facts the entire City Council should consider in its decision(s) related to a potential sale of JEA.
- Offer monthly (or more frequent, as necessary) updates as to the progress of this work to the City Council at its regular meetings.
- Make recommendations to ensure a transparent and open process for the citizens of Jacksonville as to the consideration of a potential sale of JEA.

The Special Committee did not have a final reporting deadline, but was requested to make a status report at the June 26, 2018 City Council meeting, the last meeting before the end of Council Member Brosche's term as Council President.

In one of its first actions, the Special Committee considered an offer by the Jessie Ball duPont Fund to assist the Council in its study of JEA-related issues by funding the services of a consultant to the Special Committee. A subcommittee of the Special Committee met with the duPont Fund's President and developed a scope of services document and list of preferred consultant qualifications. The duPont Fund eventually determined that it would contract with the consultant directly and commission their work on behalf of the City rather than provide funding to the City to hire the consultant through its procurement process.

The Special Committee on the Potential Sale of JEA met seven times during March and April of 2018. At the March 27th City Council meeting (revised committee charge memo issued April 19th) the Council President changed the name of the committee to the Special Committee on the Future of JEA and expanded its membership to include all City Council members – Greg Anderson, Danny Becton, Anna Lopez Brosche, Katrina Brown, Reggie Brown, Aaron Bowman, Lori Boyer, Doyle Carter, John Crescimbeni, Garrett Dennis, Al Ferraro, Reggie Gaffney, Bill Gulliford, Tommy Hazouri, Jim Love, Joyce Morgan, Sam Newby, Matt Schellenberg, Scott Wilson - with Council Member Crescimbeni continuing as Chairman. The charge of the committee was changed to two items:

- Understand JEA's role in the consolidated government, contributions to the City of Jacksonville, governance practices, and future in the context of both changing technology and regulatory environment.

- Conduct necessary meetings and hearings to gather the relevant facts the entire City Council should consider in its responsibility to represent the citizens and taxpayers of the City of Jacksonville.

The revamped Special Committee (which included a change of membership on July 12, 2018 when City Council members Ju'Coby Pittman and Terrance Freeman replaced Katrina Brown and Reggie Brown) met an additional seven times from April through late July and issued its final report on July 25th. A full record of the committee's meetings (including minutes and verbatim transcripts) and links to all of the presentations, handouts, studies, and other documentation provided to the committee is available on the City Council's website at http://www.coj.net/city-council/standing-committees/special-committee-on-the-future-of-jea.

2. About JEA

The entity now known as JEA had its origins in 1893 when the citizens of Jacksonville approved a referendum to issue bonds to fund the construction of a city electric generating plant. The City of Jacksonville operated an Electric Department for 70 years. During this time the electric operation was managed briefly by a Board of Bond Trustees and then by the City Commission. A substantial portion of the utility's net revenues were transferred to the City's general operating fund, constituting a major funding source for the city budget. When city/county consolidation was approved by the voters in 1967 the new City Charter provided for the creation of an independent Jacksonville Electric Authority (JEA) governed by a seven-member board appointed by the Mayor and confirmed by City Council. In 1997 the City transferred its water and sewer utility operations to JEA to achieve better operational efficiency and to take advantage of economies of scale. JEA has since expanded into an additional business line by constructing three "district energy" plants in downtown Jacksonville in the early 2000s to provide chilled water to serve the air conditioning needs of nearby buildings. One plant downtown serves City Hall, the county courthouse, the main library and its parking garage, City Hall Annex, State Attorney's Office and the JEA headquarters. A second plant in the Sports Complex serves the Veterans Memorial Arena and Baseball Grounds. The third plant in Springfield serves the UF Health Jacksonville hospital complex, the UF Proton Therapy Institute and UF College of Medicine.

JEA is currently the eighth largest municipal utility in the country, serving 458,000 electric customers, 344,000 water customers, 267,000 sewer customers and 10,000 reclaimed water customers (JEA 2017 Report to Customers). The electric operation covers 900 square miles of territory through 745 miles of transmission lines and 6,800 miles of distribution lines, and sold 13.9 million megawatt hours of power in 2017. The water operation covers 655 square miles of territory with water drawn from 137 wells, treated at 37 water plants, distributed through 4,700 miles of distribution pipes, and delivered over 43 billion gallons to customers in 2017. The sewer operation covers 680 square miles of territory with 4,000 miles of collection mains transporting wastewater to 11 treatment plants, and treated over 30 billion gallons of wastewater in 2017. JEA's operating revenues and expenses for the fiscal years 2012-13 through 2016-17 are attached. [**See Exhibit 1**]

JEA's owned electric generating capacity is 3,090 megawatts spread over seven plants. 67% of its generating capacity is fueled by natural gas (Kennedy Generating Station, Northside Unit 3, Brandy Branch, Greenland Energy Center), 25% is solid fueled (Northside Units 1 and 2, Plant Scherer), and 8% other (Northside oil, solar farms, landfill methane gas). The utility has 12 purchase power agreements in force (nine operational for 258.6 megawatts and three under construction for 212 megawatts) and has agreements pending for five additional privately owned solar generating plants (totaling 250 megawatts). JEA's next generating capacity expansion will take the form of the five private solar plants, the eventual addition of gas-fired capacity at the Greenland Energy Center on the Southside and an additional capacity expansion at the Brandy Branch Generating Station. [**See Exhibits 2, 3 and 4**] JEA and Florida Power and Light recently made a joint decision to decommission and demolish the solid-fueled (coal/petroleum coke) St. Johns River Power Park (SJRPP) on Jacksonville's Northside (see Section 5 below).

While the JEA's number of customers has steadily increased over the years, the utility's volume of sales on both the electric and water sides has leveled off or decreased in recent years. JEA has experienced actual declines in both electric and water sales from their peaks in 2006 and

2007 (respectively) to 2016 – a 10% decline from peak in electric sales and a 14% decrease in water sales. Electric sales peaked in 2006, declined through 2013, and increased slightly through 2017. The decline and subsequent leveling off of sales is largely attributable to the increased use of energy-efficient appliances and better energy efficiency in building construction, along with the effects of the economic recession in 2008-09. Water sales peaked in 2007, declined steadily through 2014, and have resumed a slight growth trend. The decline in water usage is largely attributable to increased emphasis in recent years on water conservation practices to preserve the potable water supply and on more water-efficient appliances. [**See Exhibits 5 and 6**]

JEA contributes, in several forms, a substantial portion of the City of Jacksonville's General Fund budget each year. The largest portion comes from the JEA's annual contribution to the City, the amount of which is negotiated between the City and JEA on a typically 5-year basis. For many years the contribution has been set at the *greater of* either a figure arrived at by multiplying a millage rate by JEA's actual electric and water sales amounts, or a contractually agreed upon minimum increase over the previous year's contribution. The electric-based contribution to the City has increased from $25.7 million in fiscal year 1978-79 to $92.3 million in FY2016-17; the water-based contribution has increased from $9.5 million in FY97-98 (the first year after the transfer of water and sewer operations to JEA) to $23.6 million in FY2016-17. [**See Exhibit 7]** The JEA annual contribution increased each year from FY2004-05 through FY2015-16 as a result of the minimum guaranteed increase. As a result of a newly negotiated agreement between the City and JEA that reduced the guaranteed minimum annual increase from $2.5 million to a 1% increase over specific base year amounts set for each of the five years of the contract, the contribution increases in FY16-17 and FY17-18 were once again set by the sales calculation. [**See Exhibits 8 and 9**]

The City levies a franchise fee on JEA of 3% on electric revenues (up to a maximum of $2.4 million in sales or $72,000 in franchise fee per customer per fiscal year) and on all water and sewer revenues. The franchise fee is charged on customer accounts in Duval County only with the exception of customers in Urban Service Districts 2-5 (the Beaches cities and Baldwin), the City of Jacksonville accounts, and JEA accounts. The City also levies a utility service tax of 10% on all purchases of electricity and water (in addition to metered or bottled natural, LP or manufactured gas not related to JEA). Between 2009 and 2017 the franchise fee ranged from a low of $37.5 million to a high of $41.7 million annually, while the utility service tax ranged from $70.7 million to $87.3 million. Both of these fees would be levied on or collected by a private investor-owned utility should JEA be privatized. [**See Exhibit 10**]

3. Value of JEA

The Special Committee learned that there is a distinction between a "valuation" study and an "evaluation" study of a utility. A valuation study examines the monetary value of a utility's assets and attempts to determine what a buyer might be willing to pay for those assets. An evaluation study considers broader strategic issues and community concerns, opportunities and challenges, etc. in addition to simple asset value. The Council Auditor's Office has previously produced two reports on JEA, at the request of council members. A 2007 report (#637) found that JEA had a net asset value of $1.5 billion and estimated the value of its cash flow to the City (negotiated annual contribution, franchise fee, utility service tax) over 30 years at $2 billion. The value of the utility's cash flow to a private utility purchaser over 30 years was estimated at $3.15 billion. A 2012 report (#722) found that JEA had a net asset value of $1.8 billion and estimated the value of its cash flow to the City over 30 years at between $2.04 and $2.49 billion (depending on the methodology). The net present value of the cash flow over 30 years to a private utility purchaser was estimated at $1.04 to $1.22 billion.

As mentioned earlier, in February 2018, PFM released its evaluation study to the City Council and the JEA Board in a joint meeting. Michael Mace, Managing Director of Public Finance Management Inc., presented four different value ranges calculated using four different methodologies:

- $7.9 - $10.1 billion using the discounted cash flow model
- $8.5 - $10.2 billion using the price-to-earnings ratio model
- $7.5 – $10.3 billion using the cash flow multiple model
- $8.1 - $11 billion based on the rate base multiple model

Mr. Mace said that the evaluations were done on a fairly conservative basis using moderate assumptions and represent gross transaction value *before* retirement of debt (currently $5.3 billion) and settlement of other outstanding long-term contracts and obligations (i.e. the JEA's contractual obligation on a purchase power agreement for a portion of the output of nuclear plant Vogtle under construction in Georgia). PFM suggested a reasonable expectation for net proceeds from sale of JEA under current market conditions would be $2.9 - $6.4 billion.

The Council Auditor's Office was requested to produce a new study of JEA's value, which was released as Special Report #807 – The Potential Sale of JEA: Things to Consider. The evaluation portion of the report started from the PFM report's estimated gross value of $7.5 to $11 billion, subtracted out a variety of financial obligations that would have to be paid off using the proceeds of a sale and arrived at a potential net proceeds value of $1.7 to $5.2 billion. JEA's outstanding obligations include: 1) long term debt - $3.9 billion; 2) Plant Vogtle obligation -

$1.2 billion; 3) accrued pension liabilities - $541,025,000; 4) interest rate swap termination costs - $100 million; 5) accrued “other post-employment benefits (OPEB) - $34,526,000; and 6) environmental liabilities - $21,654,000. The Auditor’s report also included a list of other “things to consider” in determining the value of the JEA as a City-owned asset, including: the value of the JEA’s annual contribution to the City as a reliable source of revenue; JEA’s various cooperative projects with the City over the years (assistance in funding septic tank phase-out initiatives, providing the City with water quality credits to meet the City’s obligations, purchasing land for conservation purposes, development of a shared citywide radio system, etc.); the value of the utility as a large company headquartered in downtown Jacksonville; the value of JEA’s corporate sponsorship of local events and activities; the value of JEA’s sole focus on Jacksonville rather than a larger utility’s responsibilities for a much larger service area; and the value of JEA as a local employer and purchaser of goods and services, particularly in its commitment to using the City’s Jacksonville Small and Emerging Business (JSEB) program.

The committee learned that a portion of the value of JEA’s assets is located in adjacent counties which have the first right of refusal to purchase them in the event of privatization of JEA. The purchase price of JEA’s water and sewer assets in Nassau County is $44.66 million and in St. Johns County it is $217.97 million per the terms of the respective Interlocal Agreements as of 2018. The Nassau County assets are a stand-alone system operated by JEA. The St. Johns County assets are interconnected with Jacksonville’s system and the cost and process to bifurcate those two systems in the event of a sale of JEA is unknown.

The Council Auditor’s Office contacted the Property Appraiser’s Office to learn how that office places a value on JEA’s real and personal property assets as a non-taxable entity. Keith Hicks, Chief Appraiser at the Property Appraiser’s Office, reported that JEA’s property is inspected at least once every five years as required by state law using a combination of physical inspections and aerial photography, but acknowledged that the JEA does not undergo the same degree of detailed inspection as a taxable entity would. He said that given the very complex appraisal needed to estimate a value for JEA, the Property Appraiser’s Office recommended that an outside agency that specializes in the utilities industry be consulted to develop an accurate estimated market value. The Property Appraiser’s 2018 in-progress appraised value for JEA is $432,416,183 for real property and $6,324,505,586 for tangible personal property, for a total appraised just value of $6,756,921,769. [**See Exhibit 11**]

JEA has several different kinds of value to the City, of which the annual financial contribution to the City is only one. The Special Committee learned that JEA employees contribute thousands of hours annually as both volunteers (using up to eight hours of paid leave to participate in the activities of approved non-profit organizations and events) and as ambassadors (engaging with JEA customers through speaking engagements, participation in community events and educational programs). The value of employee volunteer hours totaled $344,379 over the last three fiscal years. The JEA also procures goods and services for its operations in the Northeast Florida economy, spending between $110 million and $169 million per year in the five-county Northeast Florida area over the past seven years. A substantial portion of that procurement spending is directed to small businesses through the JEA's participation in the City's JSEB (Jacksonville Small and Emerging Business) program. JEA's spending with JSEB, minority- and female-owned businesses over the past ten years has ranged from a low of $9.6 million in FY13-14 to a high of $30.6 million in FY05-06.

In 2013, the Northeast Florida Regional Council released an Economic Impact Analysis for JEA. The study estimated the economic impact and value of JEA to Duval County in 2012. The annual impact of JEA on Gross County Product (GCP) indicated

- JEA contributed between $860 - $910 million to GCP
- JEA contribution was 1.4% - 1.5% of Duval County GCP
- JEA directly and indirectly impacted 4,500 - 4,700 jobs
- JEA impacted Earnings/Personal Income $206 - $310 million

Only the tangible impacts were quantified in the analysis.

JEA is an economic development partner with the City in several ways. The utility has two "program riders" or incentive programs for large corporate users of electric power - an economic development rider and an economic stimulus rider. Currently, Sysco International Food Group Inc., Dresser Equipment Group Inc., and Hans Mill Corporation are utilizing those riders. Pursuant to an Ordinance Code provision, the City appropriates a portion of the JEA annual contribution (equal to one-quarter mill multiplied by the gross kilowatt-hours delivered by the JEA during the preceding 12 months) to the Jacksonville Port Authority for the purpose of land acquisition and development of any marine terminal capital construction or improvement project, including payment of debt service on bonds issued for capital projects. From FY 1996-97 to FY 2016-17, $63,584,846 of revenue from JEA was pledged to JPA for debt service. For FY 2017-18, the amount pledged from the JEA assessment is $3,062,125. In the 1990s JEA also spent approximately $53,000,000 on electric, water and sewer infrastructure at Cecil Field to assist the City in creating Cecil Commerce Center.

JEA is also a member, sponsor, or partner of dozens of organizations and events throughout its service area. JEA is a dues-paying member of organizations ranging from the chambers of commerce of Jacksonville, Clay County, St. Johns County and Amelia Island/Fernandina Beach to economic development organizations (JAX USA Partnership, Nassau County Economic

Development Board, Clay County Economic Development) to industry associations (First Coast Manufacturers Association, Associated Industries of Florida) to minority business organizations (Asian-American Chamber of Jacksonville, First Coast Hispanic Chamber of Commerce, Jacksonville Black Chamber of Commerce, Indo-US Chamber of Commerce), among others. JEA's paid memberships in these organizations has ranged from a total of $257,000 to $563,000 over the past five years. The utility participates financially and through employee participation in scores of community events, ranging from the World of Nations festival to the Martin Luther King, Jr. Breakfast, the United Negro College Fund to Leadership Jacksonville, and the WJCT TEACH event to Earth Day celebrations.

Another aspect of JEA's value is the fact that as a municipal utility, JEA qualifies for reimbursement from the Federal Emergency Management Agency (FEMA) for damages it sustains from significant natural disasters. Private investor-owned utilities are not eligible for FEMA reimbursement for their damages, so they apply to the Florida Public Service Commission for authorization to place storm recovery charges on customer bills to recoup the cost of uninsured damages. JEA suffered reimbursement-eligible damages in the amount of $14.6 million from Hurricane Matthew in 2016 and $17.4 million from Hurricane Irma in 2017, of which FEMA and the State of Florida will eventually reimburse 87.5% ($28 million total for the two storms).

Another aspect of JEA's value is its partnership with the City in various types of community improvement projects. In 1998, JEA started the "Groundworks Program" to dedicate resources to the water and sewer system just transferred to it by the City, which improved water quality so much that the EPA lifted an administrative order previously imposed on the City to clean up its effluent into the river. Over $3,618,940,436 has been invested by JEA in capital improvements to the water and sewer system to date. JEA performed the project management function for the $75 million septic tank remediation project that was part of the Better Jacksonville Plan and has spent approximately $20,000,000 to purchase over 5,000 acres of preservation land to complement the City's Preservation Project. Rather than the City and JEA each constructing their own radio systems, JEA coordinated the design and construction of a radio system that the City and JEA could both use. JEA is also performing and financing the City's LED (Light Emitting Diode) streetlight conversion project at an estimated cost of $10 million. Pursuant to a 2016 interagency agreement between the City and JEA, JEA contributed $15,000,000 to be used in conjunction with a $15,000,000 match from the City for water and sewer infrastructure. It also agreed to transfer 30.34 metric tons of its excess Total Nitrogen Water Quality Credits to the City at no cost (valued at $2.1 million per year) each year through December 2023 to help the City meet its water quality improvement obligations to the Florida Department of Environmental Protection.

A question was raised during the course of the special committee's hearings about the potential impact of the privatization of JEA on the Duval County Public Schools. Unlike a privately owned utility, JEA does not pay any property taxes to the city, school district or other taxing entities. The City receives the annual contribution pursuant to its contract with JEA but the School Board does not receive any financial contribution. The Council Auditor was asked to investigate the potential for increased revenue to the School Board from a privatized utility paying the school millage levy. The Council Auditor's Office reported that the Duval County School Board (DCSB) would receive additional ad valorem taxes, although the amount DCSB would receive is limited. The Auditor estimated that DCSB would receive approximately $8 million per year for capital purposes, pursuant to the Local Capital Improvement Millage for school districts, but explained that the DCSB would probably not receive additional operating revenue from the sale of JEA. Based on the way the Florida Education Finance Program (FEFP) formula works, increases in revenue from the Required Local Effort or the Discretionary Local Effort millage levies would likely be offset by a corresponding decrease in State funds. The Local Capital Improvement Millage however, is not part of the FEFP calculation. This information was confirmed with the Florida Department of Education.

4. <u>Plant Vogtle</u>

One factor that has a substantial, but somewhat unknown, impact on establishing JEA's value is its purchase power agreement for a 206MW share of the power output of Units 3 and 4 of the Plant Vogtle nuclear plant under construction in Waynesboro, Georgia, the first new nuclear reactors to be constructed in the U.S. in the last 30 years. JEA made the decision to commit to purchasing power from the plant in 2008 for several reasons, including: 1) a JEA Board decision to meet 10% of its power needs by 2018 from non-carbon, nuclear generating sources; 2) steadily growing energy demand in Jacksonville; 3) serious discussion by the federal government about severely limiting carbon dioxide emissions, particularly from carbon-burning power plants; and 4) the relatively high cost of natural gas at the time.

The plant was permitted for site work in 2009 and received a construction and operating license (COL) in 2012. Westinghouse Nuclear, the contractor for the project, declared bankruptcy in 2017 and some parties urged the Georgia Public Service Commission to shut down the project. The GPSC gave Georgia Power the approval to complete construction of the plants, but without the contract that made Westinghouse responsible for most cost overruns. The construction cost of the project has grown since the purchase power agreement was first executed, and JEA is required to pay for the contracted capacity on a "take-or-pay" basis (that is, whether or not either additional Vogtle unit is completed or is operating or operable, and whether or not its output is suspended, reduced or terminated, in whole or in part). JEA's agreement to purchase power from Plant Vogtle does not have a cap on construction costs (although the primary companies involved in the construction do have a cap of another $1 billion, after which they could pull the plug on the project). The PFM report calculated a potential liability of $1.2 billion as a share of future construction costs for the plant, which would accrue as a share of debt service even if the plant never produces power. JEA's power purchase obligations to Plant Vogtle end 20 years after power begins being produced, although the expected lifespan of the plant is 40 years.

5. <u>St. Johns River Power Park</u>

As mentioned earlier, JEA and Florida Power and Light, the joint owners of SJRPP, made the decision in 2017 to decommission and demolish the plant before the end the Joint Operating Agreement. JEA determined that its share of the plant represented excess generating capacity that was more expensive to maintain and operate than the cost of purchasing power from other sources in the short term, and that eventually JEA's share of the output of the Plant Vogtle nuclear plant under construction in Georgia would supplant the need for the SJRPP output when that plant comes on line. The shutdown of the coal-fired SJRPP will also reduce JEA's CO^2 output by 30% by 2020. Melissa Dykes, President and Chief Operating Officer of JEA, estimated that the total savings to JEA's customers over the next 10 years resulting from the closure would be $450-460 million, representing the difference in purchasing the needed 150 - 200MW of power rather than operating a 1,000MW plant to supply that amount. She distributed a table showing the operating cost of SJRPP ($122.9 million in FY16, $140.1 million in FY17) versus purchasing 200MW of power from the natural gas-fired Plant Wansley in Georgia ($35.2 million in FY18, $44.1 million in FY19).

6. <u>Legal and regulatory issues and procedures</u>

The Special Committee learned early in its work that, pursuant to the City Charter, JEA has the authority to issue an RFP to privatize the utility without City Council's prior approval. Sale of more than 10% of JEA (defined by the Office of General Counsel as 10% of assets as of the last audit report) does require City Council approval, and sales cannot be done in multiple increments of less than 10% to avoid Council approval. General Counsel Jason Gabriel told the committee that a decision to consider a sale of JEA must take into account at least four components: 1) interlocal and franchise agreements with St. Johns and Nassau Counties; 2) real estate assets and obligations; 3) required regulatory approvals (state and federal); and 4) a water/wastewater "public interest determination" required by state law. In response to a question posed by several council members about a potential role for the voting public in a potential sale of JEA, the Office of General Counsel ruled that voters cannot use the petition and referendum method to amend the City Charter to give themselves a role in a proposed JEA sale.

The PFM February 2018 evaluation study listed as a "Key Value Driver for Sales Price" an item entitled *Utility Rate Guarantees* which read "Acquirers will often agree to keep rates the same or lower for some period of time following the acquisition. Rate regulation for a private buyer of JEA's assets will ultimately transition to the Florida Public Service Commission (PSC). The pricing and duration of rate constraints may have a significant impact on acquisition price." In response to a question about the potential for utility rate guarantees during his presentation to the Special Committee in May, Keith Hetrick, the General Counsel of the Florida PSC, said that local governments do not have the power to impose rate freezes, which would probably constitute a "taking." Utilities have the right to request rate increases of the PSC to recover their operating and capital costs and to generate a reasonable rate of return on invested capital.

7. <u>JEA's rates compared to other public and private utility rates</u>

The Special Committee heard that rate comparisons among utilities can be tricky because factors aren't uniform from jurisdiction to jurisdiction (i.e. differing franchise fee and utility service tax rates, presence or absence of storm recovery surcharges by investor owned utilities, etc.). Generally speaking, JEA's rates have historically been somewhere in the middle of the range of rates for utilities in Florida, both municipally owned and privately owned. From 2010 through 2018, JEA's residential electric rate (assuming 1,000 kWh of consumption) was in the middle of the four major private utilities, with Florida Power and Light and TECO being less expensive and Progress Energy/Duke Power and Gulf Power being more expensive each year by varying amounts. [**See Exhibit 12**] In April 2018 JEA's residential rate was in the bottom half of all Florida utilities, public and private. [**See Exhibit 13**] Similarly, in April 2018 JEA's water and sewer rates ranked in the bottom third of 18 water and sewer systems in Florida (based on residential service with 5/8 inch meter and 6,000 gallons of consumption). [**See Exhibit 14**]

The Florida Public Service Commission regulates the rates charged by private utilities based on reasonable recovery of certain costs of operation (fuel, environmental compliance, conservation programs and nuclear pre-construction costs) and a reasonable rate of return on the utility's base rate (facility and equipment cost) and debt expense. The rate-setting process is codified in state law and is a litigated process with sworn testimony, witnesses and experts testifying on both sides. Rates for private utilities must be uniform within rate classes across their entire contiguous service areas in Florida. The PSC also allows investor-owned utilities (IOUs) to impose approved surcharges for storm damage restoration following major storms, and these surcharges apply to all of a utility's customers within the state, regardless of whether a particular area suffered storm damage or not.

8. <u>JEA's current and projected business model</u>

As mentioned earlier, JEA's number of customers has steadily grown but electric and water consumption has declined for a number of years following the Great Recession and the growth projections for both are basically flat if not slightly declining for the foreseeable future. Overall

JEA has experienced actual declines in both electric and water volume sales from their peaks in 2006 and 2007 (respectively) to 2017 – a 10% decline from peak in electric sales and a 14% decrease in water sales. JEA makes several different forecasts of future sales trends for different purposes, including one for JEA's financial planning purposes and another for the Florida Public Service Commission for capacity planning purposes.

On-site solar power generation on business and residential properties is a small but growing trend as the quality of solar panels and battery technology improves. 1,436 residential customers and 59 commercial customers currently have customer-owned solar systems, so self-produced power serves a small proportion of the total demand and is not yet a threat to JEA's centralized generation model, but the trend bears watching. JEA currently needs to have a certain amount of generating capacity available at all times to serve its customers, including those who generate their own solar power, so JEA is acting as the backup power supply for solar users who will need its services when weather or other conditions reduce solar generation capability. The development of affordable, efficient customer-owned on-site storage batteries will be a key to the growth of solar power use and the timing of its impact on JEA's generating capacity needs.

Given the trends in electric and water sales, JEA has given some thought to expanding into other lines of business to produce additional revenues, including pole attachment revenues, wireless colocation leasing revenue, dark fiber leasing, natural gas sales, solar panel leasing, fuel cells and micro-turbines. [**See Exhibit 15**] Other utilities around the country, facing the same challenges of declining sales, have diversified into energy marketing, liquefied natural gas (LNG) processing and sales, renewable energy development (wind and solar), distributed generation (i.e. combined heat and power generators, fuel cells, batteries), and telecommunications (fiber optics, tower leasing, internet services).

JEA's Interim CEO Aaron Zahn informed the Special Committee that the JEA board will spend the next six months to a year mapping a strategy for its future in consultation with its employees and stakeholders. He said he has instructed the employees and management of JEA to focus on five priorities for the present: 1) focus on core business – serving electric water and sewer customers with excellence; 2) look forward – implement a smooth transition of leadership; 3) listen and align our purpose with shareholder trustees - JEA's board of directors, City Council and the Mayor will establish consensus around a framework upon which to measure a strategic plan for the future of JEA; 4) question the possibilities of greatness and innovate; and 5) be stewards of a united community and lead with integrity. Mr. Zahn plans to have the JEA board thinking strategically and planning for a changing future. He said that board agendas will include several categories of issues – routine operational issues, deep dives into particular topics, and long range planning discussions. Issues will undergo a 3-step progressive process of "discuss, deliberate and decide".

9. <u>Independent evaluations of JEA's value and role in the community still underway</u>

Two independent evaluations of JEA are still ongoing. The Jessie Ball duPont Fund, a national foundation headquartered in Jacksonville, carries on the philanthropic tradition of Mrs. duPont by making grants to organizations that she supported during her lifetime with the aims of "building the capacity of eligible organizations, building the assets of people, families and communities, and promoting civil society." As a recipient of a gift from Mrs. DuPont, the City is an eligible recipient of the Fund's grant-making. As mentioned earlier, the Jessie Ball duPont Fund offered to assist the Special Committee's efforts to study a vital community issue by funding the services of a consultant. The Fund eventually opted to hire a consultant itself rather than make a grant to the City to hire a consultant through its procurement process. The Fund contracted with the Public Utility Research Center at the University of Florida to assist the City. Dr. Ted Kury, the Director of Energy Studies for the Center, explained why the Center is interested in studying the JEA privatization issue. Privatization of municipal utilities is a relatively rare occurrence and the Center is interested in exploring the question of "value" in the context of the overlap of utility owners and users (the citizens of Jacksonville) and how they consider making such a decision. He said that he can find no similar research on this question of value to municipal utility owners/customers, and is excited by the prospect. He is particularly anxious to explore the "quality of service" aspect – what do customers really value about JEA? Dr. Kury anticipates that study should be completed by the end of 2018.

The other study of JEA has been commissioned by the Jacksonville Civic Council. The Civic Council is a nonpartisan, nonprofit organization which brings together chief executives from the nonprofit, business and government sectors of Jacksonville to study important community issues. The Civic Council assembled a team of local business executives, co-chaired by CSX former CEO Michael Ward and Bobby Stein, Managing Director of Chartwell Capital Management, to examine issues related to JEA's value to the community. At a Special Committee meeting Mr. Ward said that fundamentally the proper question to be asked is not whether to sell JEA or not, it's how to best maximize the value of the asset to the City and its taxpayers. The group will perform a cash flow analysis that will lead to ideas for enhancing JEA's value (i.e. sale/leaseback of assets, leveraging JEA's very strong balance sheet, alternative operating models, etc.) as one part of its analysis. The Civic Council has retained Gerry Hartman, an engineer and certified appraiser from Central Florida, as a utility industry expert to provide in-depth analysis of JEA. Mr. Ward said the nature of the study will depend in part on the ultimate goal – is it to determine how much JEA might be worth to private buyer? Is it to run JEA better in its current business lines? Is it to determine how to monetize various JEA assets to generate cash? He also said that the study, which will take 9-12 months, will definitely produce some good ideas and suggestions, some of which JEA will likely want to adopt to make itself a better utility.

10. Unanswered questions

One issue that the special committee heard several times in different contexts concerned unfulfilled promises from the city/consolidation era in the late 1960s: do the City and/or JEA have any legal or moral obligation to provide water and sewer service to areas of the pre-consolidation city that do not have those services? Who will pay to extend the mains and hook up the individual properties? Can JEA legally use its operating revenues to pay for extension of service to new customers?

The broader questions that underlie the creation of the Special Committee are:

- What is the true value of the utility to the City government and to the citizen/taxpayers who are its ultimate owners?
- What factors should be considered relevant in determining whether the JEA should be privatized or not?
- How should purely monetary considerations be balanced against the intangible value that JEA provides to the region?
- What process should be used to perform that balancing test and involve the citizens in helping to make a final privatization decision?

11. Conclusions

Based on the hours of testimony provided by invited speakers in Special Committee meetings, the hundreds of facts identified by numerous presenters, and extensive discussion among the committee members, the following conclusions can be reached:

- Regardless of any of the various measures of its monetary worth, JEA is one of Jacksonville's most important civic assets and decisions about its future should be made with the utmost care.
- Having a utility headquartered in and solely focused on serving Jacksonville and the immediately surrounding counties has both tangible and intangible value, in large part because the utility's decisions will be made by board members who are local residents and who will make those decisions based solely on what's best for the customer/owners in the immediate service area.

- The ability of JEA, as a municipal utility, to receive FEMA reimbursement for damages caused by natural disasters has value because it shifts part of the cost burden of restoring and rebuilding infrastructure after a storm from the ratepayers to the federal government.
- Because of the success of energy conservation measures in reducing electric and water consumption and sales, JEA needs to consider expanding its operations into other related business lines to diversify its revenue streams and ensure continued financial health.
- JEA's Plant Vogtle obligations have the potential to adversely affect the utility's financial position for several decades to come, depending on how long the construction process takes, how much the plant eventually costs, whether it eventually produces power or not, and what that power costs when finally available in comparison with the cost of power from other sources (i.e. natural gas or solar) at the time, and the then-current state of the regulatory environment.
- As a municipal utility owned by the City of Jacksonville, JEA is more likely to enter into voluntary agreements with the City to tackle community needs and opportunities (i.e. septic tank phase-out, transfer of water quality credits, environmental conservation efforts, cost-sharing on projects of mutual interest, etc.) on financial terms favorable to the City than would an investor owned utility whose primary responsibility is to maximize shareholder value.
- Expansion into new business lines may require an amendment to JEA's Charter to authorize entry into new fields.