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Nominated JEA Board Members

RE: Letter from Melissa Dykes dated February 26, 2020

Dear Nominated JEA Board Members:

As you may know, our firm prepared a memorandum dated December 26, 2019 that summarized the findings of our investigation into the quality of information provided by JEA's management to the JEA board in connection with the now-terminated strategic planning process. Since then, we have continued our investigation into these issues.

Yesterday, we learned that on February 26, JEA's Interim CEO Melissa Dykes sent a letter that challenges some of our findings. Ms. Dykes's letter continues JEA management's pattern of providing inaccurate and misleading information that has led JEA to its current position: the subject of legislative and criminal investigations, downgraded bond ratings, and a damaged reputation. Instead of working to rebuild the public trust as she committed to do, Ms. Dykes has turned JEA's public relations machine to work on rehabilitating her professional reputation.

This letter addresses the assertions in Ms. Dykes' letter, and raises new concerns we have discovered since our December 26, 2019 memorandum and our recent presentation to the City Council's Special Investigative Committee. But we also observe that Ms. Dykes's letter is notable for what it does not say about our analysis. It fails to offer any rebuttal to or explanation of our findings that:

- JEA management, including Ms. Dykes, misled the JEA board about the terms of the performance unit plan ("PUP"). Interview transcripts from the OGC's investigation establish that Ms. Dykes understood the terms of the PUP but failed to correct false and misleading statements made by Mr. Wannemacher at the July 23, 2019 board meeting.
- JEA management, including Ms. Dykes, misrepresented to the JEA board its intentions with respect to the downtown headquarters as an additional justification for a sale. Ms. Dykes told the JEA board on June 25, 2019

(beginning at 1:13:45 of the videotaped board meeting) that under Scenario 1 or Scenario 2, JEA would be forced to move out of downtown to minimize cost. But at the same meeting, management sought and obtained approval to execute a lease for the new downtown headquarters that gave JEA a 90-day termination right when management knew that there could not possibly be a finally approved sale within such a short period. The lease was used by management as leverage to drive the board towards its predetermined outcome.

- JEA management, including Ms. Dykes, presented the JEA board with strawman alternatives in Scenario 3 (cooperative ownership and initial public offering) that management knew were not viable alternatives. Ms. Dykes continued to characterize those options as viable in her December 9, 2019 appearance before the City Council Committee on the future of JEA (31:20 and 31:49 of the video).

- JEA management, including Ms. Dykes, exaggerated legal restraints on JEA's ability to adapt its business operations and failed to provide the board with strategies that it could pursue within legal constraints to decouple rates from unit sales (including under a pilot rate program that JEA had recently implemented) and address distributed generation. Ms. Dykes asserted to the Future of JEA Committee that JEA's ability to pursue additional opportunities was very limited under current constraints.

We presume that JEA management, including Ms. Dykes, has no defense to and concedes the accuracy of these findings.

The assertions made in Ms. Dykes's February 26, 2020 are incomplete, misleading or false in the following respects:

<u>Ten-Year Site Plan vs. Financial Forecast</u>

Ms. Dykes incorrectly contends that our analysis is flawed because we compare the ten-year site plan (TYSP) to the financial forecast. Our analysis did not do that. We are aware that JEA management began using a flat MWh sales assumption for purposes of the Five-Year Financial Plan that was presented to the rating agencies. This is a sensible practice that presumably gives the rating agencies comfort about JEA's financial stability even if sales remain flat. But this financial planning assumption is <u>not</u> an actual projection of MWh sales. There is no methodology behind this assumption; it simply represents a conservative baseline for financial planning purposes.

We agree that the TYSP is not a financial forecast; rather, it is the best analysis that JEA does to evaluate future electric supply and demand in its service territory, a critical part of understanding the basic economic forces that will influence JEA's business in the coming years. We reject the notion that the TYSP should be disregarded simply because JEA is required to maintain a conservative 15% margin of generation capacity above the TYSP projections.

Further, while we note that although the flat electric sales assumption is used for the Five-Year Financial Plan presented to the rating agencies, JEA does not actually use it in preparing its own annual budget. For example, the 2016 budget assumed sales of 12 million MWh, but the 2017 and 2018 budgets assumed 12.4 million MWh sales.[1]

Reasons for Sales Decline from 2006 to 2018

Ms. Dykes claims that we falsely asserted that 45% of JEA's sales decline from 2006 to 2018 was attributable to the expiration of the contract with Florida Public Utilities. We noted in our memorandum that it often is misleading to compare two years in isolation as management presented to the board rather than looking at trends over time; accordingly, we looked at both the two years cherry-picked by JEA management and trends over time.

Using management's methodology of simply comparing 2006 to 2018 in isolation, it is inarguable that 45% of the sales decline is attributable to the loss of sales for resale (the Florida Public Utilities contract):

Sales (MWh)	2006	2018	% Change	% of Total Decline
Residential	5,650,986	5,414,721	(4.2%)	22%
Commercial and Industrial	7,157,602	6,851,803	(4.3%)	28%
Street Lighting	110,178	59,176	(46.3%)	5%
Sales for Resale	522,134	38,640	(92.6%)	45%
Territorial Sales	13,440,900	12,364,340	(8%)	

[1] Page 213 of the materials for the March 15, 2016 board meeting; Page 368 of materials for March 13, 2017 JEA board meeting.

We also provided a chart showing a modest but steady growth trend in retail sales from 2012-2019 (except for a slight dip in 2017 due to hurricane activity). We believe the retail sales metric provides a more accurate depiction of JEA's performance over this period because it excludes street lights and sales for resale, both of which experienced a fundamental change during the period (the conversion to LED and the termination of the FPU contract, respectively).

Fiscal Year	Residential MWh Sales	Commercial/ Industrial	Total Retail Sales
2012	4,806,144	6,670,200	11,476,344
2013	4,877,264	6,599,249	11,476,513
2014	5,086,866	6,636,445	11,723,311
2015	5,243,002	6,767,836	12,010,838
2016	5,328,245	6,847,583	12,175,828
2017	5,108,945	6,725,201	11,834,146
2018	5,414,721	6,851,803	12,266,524
2019	5,515,428	6,793,603	12,308,985

Ms. Dykes asserts that all sales should be considered. We agree. The significance of our analysis was not to rebut that sales declined by 8% from 2006 to 2018. Rather, this analysis demonstrates that JEA management's representation that 90% of the decline was attributable to energy efficiency was patently false, and was presented to support a false narrative about the downward trajectory of JEA's electric sales. JEA management never provided the board this information because it did not align with management's goal of driving the board towards a sale, and Ms. Dykes's letter does nothing to rebut this point.

Our analysis points out that JEA's modest growth in electric sales is the result of population growth and increased degree days that have more than offset energy efficiency gains. Ms. Dykes's letter asserts that the growth in MWh sales over this period is due to "abnormal weather." This assertion is inaccurate and misleading because while weather is a large factor in MWh sales year to year,[2] it ignores the impact of long-term climate trends on electricity demand.

[2] As context on the impact of weather on electric sales, the record year for JEA's electric sales was fiscal 2010, during the great recession. In fiscal 2010, Jacksonville suffered an unusually cold winter due the Arctic Oscillation Index (polar vortex) entering a negative phase coupled with an exceptionally hot summer.

We analyzed the impact of weather on the entire twelve-year period, including an analysis of trends. The following chart shows heating degree days (HDD) and cooling degree days (CDD) from 2006-2019, usage per residential customer and retail MWH sales.

Fiscal Year	HDD	CDD	Degree Days	Res Kwh/Cust	Retail MWhSales
2006	1299	2715	4011	15,819	12,809
2007	1235	2540	3775	15,038	12,639
2008	1234	2534	3768	14,670	12,677
2009	1456	2605	4061	14,404	12,149
2010	1727	3348	5075	15,481	12,640
2011	1601	2722	4323	14,733	12,353
2012	945	2633	3578	12,932	11,477
2013	1275	2524	3799	12,985	11,477
2014	1327	2638	3965	13,301	11,723
2015	1352	2765	4117	13,468	12,011
2016	978	3098	4076	13,433	12,176
2017	806	2901	3707	12,672	11,834
2018	1131	3082	4213	13,205	12,267
2019	1000	3260	4260		
Averages:					
1981-2010	1350	2664	4014		
2006-2010	1390	2748	4138		
2011-2014	1287	2629	3916		
2015-2019	1053	3021	4074		

This chart shows that the number of degree days during 2012-2019 (when retail sales steadily increased), is consistent with long-term averages and does not reflect "abnormal weather." There are significant changes in the trends, however, due to steady increases over the period in average annual temperature in Jacksonville. Heating degree days have decreased significantly over this period while cooling degree days have significantly increased. Put simply, Jacksonville winters are getting shorter and summers are getting longer as average annual temperatures are increasing.

This long-term trend will increase electricity demand in most of the year and decrease demand in the winter. Weather-normalized data is useful for evaluating short-term trends, but long-term climate trends also should be considered. We are unsurprised by Ms. Dykes' assertion that JEA is on track for 12.17 million MWh year to date; heating degree days for the first quarter of JEA's fiscal year declined by 14% over last year and

JEA has not yet reached the warmer months.[3] Again, the point is not that the data offered by Ms. Dykes now, after the fact, is necessarily wrong, but rather that it was never provided to the board in the first place.

We have not received the McKinsey report, so we are not able to comment on its assumptions. We would note two points, however:

- The energy efficiency projections differ dramatically from the analysis conducted by ITRON for FPL and reported in FPL's TYSP; and
- While we have not reviewed the distributed generation assumptions in the report, JEA management failed to present to the board its existing strategies (*e.g.* Solar Max) to provide renewable energy to large commercial and industrial customers that have made renewable energy commitments.

We have recently uncovered additional concerns about inaccurate and misleading information provided by JEA management to the JEA board and the City Council. These include:

<u>Plant Vogtle</u>

A key rationale that JEA management presented for approving a sale was the Plant Vogtle power purchase agreement. Management, including Ms. Dykes, described it to the JEA board and the City Council Committee on the Future of JEA as "contract debt," asserting that all of JEA's progress in paying down debt over the past several years had been erased by this obligation. But the Plant Vogtle obligation is an obligation to purchase power; it is not debt. If it were properly characterized as debt, there would be a corresponding asset. This obligation is not an existential threat to JEA, but only a cost for purchased power that would be passed on directly to JEA's ratepayers.

Moreover, JEA's obligations under the Plant Vogtle agreement cannot be transferred to an investor-owned utility because of the "private business use" covenants in the power purchase agreement (which tie back to the municipal bond financing on the project). JEA management failed to disclose to the JEA board or the City Council that following a sale, JEA would remain liable for the Plant Vogtle obligation. The Plant Vogtle obligation therefore appears to be yet another boogeyman presented by JEA management to lead the board to a conclusion to sell, when it would actually have no impact whatsoever on JEA.

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[3] There are very few studies predicting long-range cooling and heating degree days by city, but one that we reviewed indicates that Jacksonville is headed toward years with 800 heating degree days (as in 2017) and 4600 cooling degree days. That represents a 35% increase over the last five-year average.

On December 9, 2019, Ms. Dykes represented to the Future of JEA Committee that Plant Vogtle was a key driver for exploring strategic alternatives. But in response to a direct question from Councilmember Cumber about how the Plant Vogtle obligation would be handled in connection with a sale, she refused to answer upon the advice of counsel (54:00 of the video). In stark contrast, JEA management provided an explanation of how the Vogtle liability would be handled to bidders during the ITN process. This means that JEA management was more forthcoming and transparent with outside companies than it was with either JEA's own board or the City Council.

We also would observe that while the cost of the power from Plant Vogtle (estimated at $120 per MWh) is well above current market prices, it would be on par with, or less expensive than, coal if a $50 per ton carbon tax were implemented.

JEA Rates

Another key rationale given for evaluating a recapitalization was JEA management's representation that JEA would be required to raise rates by 51% if JEA remained publicly owned. Despite this, JEA management never provided information to the JEA board or the City Council regarding the impact of a sale on rates. In fact, Ms. Dykes and Mr. Wannemacher both ducked a question from Councilmember Dennis at the same December 9 Committee hearing, claiming that they did not have enough information to assess what the rates would be upon a sale, or to compare those rates to current rates.

But they did have access to that information at the time, because JEA had obtained and provided to bidders a study from FTI that modeled the rates upon a sale. Moreover, two days after the Committee hearing—on December 11 and 12—Ms. Dykes participated in a management presentation to bidders that provided the key metrics upon which these rates would be calculated.

By December 2019, JEA management had already conceived a plan to increase JEA rates immediately prior to a sale to goose the rates that a buyer could charge during the three year "stable rate" period described in the terms of the ITN. This plan would have increased rates from approximately $68/MWh to: (i) $81.46/MWh in 2021, $82.94/MWh in 2022 and $84.45/MWh in 2023 plus (ii) JEA's pass-through charges for the costs of the Plant Vogtle power. The proposed "stable rates" would therefore have actually represented a minimum rate increase of almost 20%.

We fully recognize the difficult position that JEA management has put the current and future board members in, and your willingness to serve our community through this critical time is commendable and deserves our gratitude. We would be pleased to meet with you to discuss any of our findings or to meet with Ms. Dykes if she has questions or concerns about our analysis.

Very truly yours,

Daniel B. Nunn

Lee D. Wedekind, III

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