

## MEMORANDUM

TO: Lawsikia Hodges, Esq.  
Jason Gabriel, Esq.

CC: Lynne Rhode, Esq.

FROM: Kevin E. Hyde

DATE: September 25, 2019

RE: JEA Performance Unit Plan

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This memorandum addresses the Long Term Performance Unit Plan (the "PUP" or the "Plan") approved by the JEA Board on July 23, 2019 and the application, if any, of various federal and state laws relating to securities and deferred compensation. We also comment on whether the PUP constitutes "extra compensation" under Florida law.

### Description of the PUP

The PUP allows eligible employees to defer compensation in order to purchase a specified number of performance units from JEA and redeem them for a cash payment equal to the redemption price. The PUP is entirely voluntary. Any eligible employee may decide to participate or decline.

Eligible employees include all full-time employees (including full-time attorneys from the Office of the General Counsel dedicated exclusively to JEA, appointed employees, and represented employees) actively employed with JEA for at least three months prior to the performance units purchase date. The eligibility of employees to participate in the program is dependent solely on their employment status and execution of and compliance with a performance plan participation agreement. To participate, the employee must agree in a performance plan participation agreement to comply with the following covenants: (i) devote his/her best efforts to faithfully discharge his/her duties on behalf of the JEA and not take any action that would be contrary to the best interests of the JEA and (ii) not disclose confidential JEA information except as required by law or to perform employment duties. A breach of these covenants would result in the forfeiture of unvested units except for a return of the aggregate purchase price for such units. The agreements regarding the Plan will be subject to sections 409A and 457(f) of the Internal Revenue Code and will be governed by the laws of Florida and subject to arbitration in Duval County.



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A pool of units will be allocated<sup>1</sup> amongst employees based on his/her position level and the most recent annual performance review. The units will be available for purchase at \$10.00 per unit on January 15th of the calendar year following the calendar year in which JEA's annual financial audit statement is completed. Unpurchased units will return to the pool. Eligible employees will pay the purchase price of the unit by electing to defer a portion of his/her salary (equal to the aggregate purchase price for the performance units) into an FDIC-insured savings account. At redemption, the employee will receive a cash payment in the amount of the redemption price that will include the purchase price paid per unit. JEA's Chief Financial Officer will calculate the redemption price, and it will be certified no later than 30 days following the completion of JEA's annual financial audit statement.

The calculation of the redemption price is dependent on JEA's current year value, which is defined as the sum of JEA's net position per JEA's annual audited financial statement, the aggregate consideration paid, distributed, credited, or otherwise provided to the City of Jacksonville during the 12-month period prior to the end of the performance period, and the aggregate consideration paid, distributed, credited, or otherwise provided to JEA's customers during the 12-month period prior to the end of the performance period. Depending on the increase or decrease of JEA's current year value, the redemption price for the units will increase or decrease. Payments made regarding the units will be paid less applicable withholding taxes.<sup>2</sup>

The employee must be actively employed on the vesting date for the units to vest. If an employee is involuntarily terminated (without cause or due to death or disability) prior to the vesting date, then the employee will receive a payment for the units at the same time as the amounts would have been paid had the employee not been terminated. If the employee's termination of employment is voluntary, then the employee forfeits the units. If an employee is retirement-eligible and retires prior to the vesting date, the units will vest on the normal vesting date.

1. The PUP Does Not require Registration Under the Securities Laws

As described above, the PUP is an opportunity for JEA employees to defer compensation, purchase units within the PUP, and realize gain, if any, if the enterprise value of JEA increases. The PUP is designed to allow employees to personally invest in the enterprise growth of JEA in the next three years (i.e. encourage employees to have "skin in the game" with respect to improving the health of the utility). JEA's performance will be measured on the change in JEA's net position during the performance period.

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<sup>1</sup> The allocation of performance units available to each employee for purchase will be directed by the JEA Compensation Committee Chair, who is the Administrator of the Plan.

<sup>2</sup> As a part of the JEA's Board's exploration of alternative scenarios to address the utility's fiscal challenges, JEA is also considering selling the utility. If that occurs, the performance period ends, the amount owed to the employee will be paid, and the Plan will be extinguished.



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A security may be considered any situation where individuals invest money in a common enterprise with the expectation that they would earn a profit solely through the efforts of someone other than themselves. However, since the performance units are being issued and sold by JEA, then the performance units are exempt from registration under both the federal and state securities laws. The units are exempt from registration since they are being issued by a public instrumentality of a state. Section 3(a)(2) of the Securities Act of 1933 and Section 517.051(1) of the Florida Statutes provide this exemption.

As long as the total subscription for the PUP does not exceed \$1,000,000.00,<sup>3</sup> the municipal securities disclosures required for offerings of \$1,000,000 or more as provided by Rule 15c2-12 of the Securities Exchange Act of 1934 will not be applicable.

2. The PUP is Akin to Deferred Compensation Plans Allowed by Florida Law

Florida law and the JEA Charter allows employees of a governmental unit to participate in a deferred compensation plan.

The relevant Florida statute, F.S. 112.215, states in part:

In accordance with a plan of deferred compensation which has been approved as herein provided, the state or any state agency, county, municipality, other political subdivision, or constitutional county officer may, by contract or a collective bargaining agreement, agree with any employee to defer all or any portion of that employee's otherwise payable compensation and, pursuant to the terms of such approved plan and in such proportions as may be designated or directed under that plan, place such deferred compensation in savings accounts or use the same to purchase fixed or variable life insurance or annuity contracts, securities, evidence of indebtedness, or such other investment products as may have been approved for the purposes of carrying out the objectives of such plan. Such insurance, annuity, savings, or investment products shall be underwritten and offered in compliance with the applicable federal and state laws and regulations by persons who are duly authorized by applicable state and federal authorities. (F.S. 112.215(3)) (Emphasis added)

The statute further provides the basis for establishing the plan and criteria for approving the various accounts and investment accounts or vehicles. (F.S. 112.215(5-6)).

Article 21.07(j) of the JEA Charter specifically provides that "JEA shall have the option to establish an employee deferred compensation program separate from the city's employee deferred compensation program." Under this authority, the JEA 457 Deferred Compensation Plan was established in 2002 for the purpose of providing employees of JEA and employees of

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<sup>3</sup> As written, the PUP is scheduled to have 100,000 units at \$10.00 per unit.



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the (now former) St. Johns River Power Park System with a voluntary method deferring taxation on compensation until death, retirement or certain other events. See memo dated July 6, 2018 from Aaron Zahn to JEA Board and as approved by JEA Board on July 30, 2018.

The PUP is not a traditional deferred compensation plan such as the one currently in place with JEA. However, the PUP is akin to and fits with the deferred compensation plan allowed by F.S. 112.215. Specifically, the JEA Board has approved the PUP; JEA will seek a determination that the compensation deferred by employees to purchase the PUP is not currently taxable (F.S. 112.215(5); and that the proceeds to the employees from the PUP, if any, will not be included in the employee’s taxable income until proceeds are actually received (F.S. 112.215(6)(a)). Finally, the PUP does not impose any liability on JEA, “except to show that the payments have been [or will be] remitted for the purposes for which the compensation has been deferred.” (F.S. 112.215(9)). Specifically, Section 9(c) of the JEA Long-Term Performance Unit Plan states, “[t]his Plan is intended to constitute an ‘unfunded’ program, and no amount shall be set aside to fund any payments hereunder prior to the end of the Performance Period. JEA’s obligations under this Plan are unfunded and unsecured, and the Participants have no rights other than those of general unsecured creditors of the JEA Group with respect to any payment hereunder.” Further, a JEA Employee stands to gain nothing if the Threshold Value Target is not attained during the applicable Performance Period. (Section 2(t) of the JEA Long-Term Performance Unit Plan).

If requested, we can provide a more detailed analysis but our initial review is that the PUP appears to be a permissible form of deferred compensation under F.S. 112.215.

In addition to the requirements under F.S. 112.215, the Administrator of the PUP should consult F.S. 112.21 to determine the applicability of requirements of custodial accounts in which the deferred compensation used to purchase performance units will be held. It is our understanding that JEA intends to hold the deferred compensation in an interest-bearing FDIC insured account such as those currently used for other existing JEA deferred compensation plans.

3. JEA is Not Pledging Credit to Participating Employees

Article 7, Section 10 of the Florida Constitution prohibits JEA from becoming a “joint owner with, or stockholder of, or giv[ing], lend[ing] or us[ing] its taxing power or credit to aid any corporation, association, partnership or person.” As indicated above, JEA is not giving or using its taxing power or credit to help any JEA employee who purchases a PUP with deferred compensation. The Florida Supreme Court has described the pledging of credit as follows:

As used in Article VII, section 10, “credit” means “the imposition of some new financial liability upon the State or a political subdivision which in effect results in the creation of a State or political subdivision for the benefits of private enterprises. This Court has explained that the lending of public credit means:



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[T]he assumption by the public body of some degree of direct or indirect obligation to pay a debt of the third party. Where there is no direct or indirect undertaking by the public body to pay the obligation from public funds, and no public property is placed in jeopardy by a default of the third party, there is no lending of public credit.

Under this definition, we conclude that the COP's in this case do not contemplate a pledge of the District's credit, and that only a public purpose, and not a paramount public purpose, need be shown.

*Miccouskee Tribe v. South Florida Water Management District*, 48 So.3d 811, 823 (Fla. 2010) (internal citations omitted).

As earlier explained, a participating employee only realizes a gain on the deferred compensation used to purchase the PUP if the Threshold Value Target set forth on the Redemption Price Schedule is attained during the applicable Performance Period, i.e. there is an increase in value of JEA itself. No public property is placed in jeopardy by default of the participating employee or any other third party.

Given that no credit is being pledged, Article VII, Section 10 requires only that a public purpose be met. The PUP's stated public purpose is to "provide a means by which employees of JEA may be given incentives to (i) remain with JEA, (ii) drive value for customers, (iii) drive value for the community of Northeast Florida; (iv) drive environmental value, and (v) drive financial value for JEA and the City of Jacksonville. (Section 1(a) of the JEA Long-Term Performance Unit Plan)."

The Florida Attorney General has opined that "if the expenditure primarily or substantially serves a public purpose, the fact that the expenditure may also incidentally benefit private individuals does not violate Article VII, section 10. "AGO 2005-02. The AGO further stated that the determination of whether the expenditure of funds fulfills a public purpose is one that the legislative body, in this case the JEA Board, must make. *Id.* As noted above, the PUP specifies the public purpose, and the JEA Board has approved the PUP.

3. The PUP is Permissible under Florida Laws related to "Extra Compensation"

JEA's PUP gives employees the choice of purchasing units that can increase in value if the value of JEA increases and decrease in value if the value of JEA decreases. The Plan is voluntary and requires employees that wish to participate to buy-in by deferring their personal compensation to purchase the units and to execute an agreement pertaining to the Plan. As developed below, the Plan does not therefore constitute "extra compensation" under section 215.425, Florida Statutes.



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Section 215.425 provides that "no extra compensation shall be made to any [public employee] after the service has been rendered or the contract made." The intent behind this provision is that public employees should not receive gratuities for services that were already rendered. AGO 2005 07 ("The purpose of such a provision is to prevent payments in the nature of gratuities for past service, and the restriction pertains to extra compensation given after service has been performed, not to compensation earned during service.").

We have reviewed the applicable legislative history of section 215.425 and have not identified anything suggesting that plans such as the PUP are, or are intended to be, prohibited by the statute. The provision applies principally in instances where public employees were to receive retroactive compensation for work already performed. *See* AGO 92-49 (holding that the Police Pension Board of Trustees could not pay a cost of living allowance to a retired police officer already receiving pension benefits for prior services); *see also* AGO 91-51 (holding that severance payments in lieu of notice violated the provision because the employee renders no service after termination and the payments were compensation for work already performed).

JEA's PUP plainly does not constitute "extra compensation" because the redemption payments are not compensation for the services that the employees render as part of their employment with JEA. Rather, the PUP allows all eligible employees to participate through a voluntary payment in enterprise creation at the risk of not receiving a return on the investment made to purchase the performance units. The PUP also does not serve to provide gratuities to the employees for their past service that they have been previously paid for and does not serve as a bonus program or incentive program to reward employees. Indeed, to participate in the Plan, JEA employees must opt-in at their sole discretion and expend their personal funds to purchase the units. The number of performance units available for purchase by each employee is directed by the Plan Administrator and is based on the employee's position level and annual performance review. The redemption payments for the units depend solely on the change in value of JEA. Thus, section 215.425 does not apply to the Plan, and the Plan does not constitute "extra compensation."

#### Conclusion

We appreciate the opportunity to review the PUP. Please call if there are any questions.