

UTILITY OVERSIGHT TRANSFER COMMITTEE

DATE: July 6, 2010

CALLED TO ORDER: 6:02 p.m.

ADJOURNED: 8:36 p.m.

ATTENDANCE

ATTENDING MEMBERS

Ryan Vaughn, Chairman
Paul Bateman
Maggie Lewis
Bob Lutz
Brian Mahern
Barbara Malone
Angela Mansfield
Marilyn Pfisterer
Angel Rivera
Joanne Sanders
Mike Speedy

ABSENT MEMBERS

AGENDA

PROPOSAL NO. 197, 2010 - approves and authorizes the execution of asset purchase agreements to provide for the transfer of the water system and the wastewater system of the City of Indianapolis, Indiana and amending the Revised Code to create the utility monitoring fund
"No Action Taken"

UTILITY TRANSFER OVERSIGHT COMMITTEE

The Utility Transfer Oversight Committee of the City-County Council met on Tuesday, July 6, 2010. Chairman Ryan Vaughn called the meeting to order at 6:02 p.m. with the following members present: Paul Bateman, Maggie Lewis, Bob Lutz, Brian Mahern, Barbara Malone, Angela Mansfield, Marilyn Pfisterer, Angel Rivera, Joanne Sanders and Mike Speedy. General Counsel Robert Elrod and Chief Financial Officer James Steele represented Council staff.

PROPOSAL NO. 197, 2010 - approves and authorizes the execution of asset purchase agreements to provide for the transfer of the water system and the wastewater system of the City of Indianapolis, Indiana and amending the Revised Code to create the utility monitoring fund

Chairman Vaughn stated that the Utility Transfer Oversight Committee came about as an agreement between Minority Leader Sanders and himself. He said that they felt it would be best to create a limited dedicated committee to address the issue of the transfer and sale of the water and wastewater utilities, and only that issue. He said that this agreement and creation of the committee was then memorialized in the same ordinance that approved the memorandum of understanding (MOU) and approved moving forward with negotiations. He said that the Republican members of this committee were appointed by himself, and Councillor Sanders appointed the Democrat members. He stated that the committee will meet again on Monday, July 10, 2010, at which time Citizens Energy Group (CEG) and the Mayor's Office will be asked to answer any of those questions brought up at this meeting that have not yet been addressed. Chairman Vaughn stated that all Councillors were given a binder on June 25, 2010 with a significant amount of information, including the definitive agreements, a letter from the Mayor and CEG, the MOU, and many other supporting documents and schedules. He said that tonight's meeting will consist of a presentation by CEG and the Mayor's Office regarding how these definitive agreements coincide with the MOU. He asked that public comments be kept germane to the topic, and that if someone has already voiced the same opinion, that comments be kept brief. He added that the Mayor's Office and other staff will also accept questions up until the next meeting and will be prepared to answer any outstanding issues at that second meeting. He thanked Committee members for giving up their time to serve on yet another committee as a part of this very demanding part-time job.

Chris Cotterill, Chief of Staff, Mayor's Office, reviewed the history of this process involving the water and wastewater utilities, beginning with the release of a request for expression of interest (REI) last year. He reminded members and the public of the challenges facing the city that make this transaction necessary: rising water and wastewater rates and a significant infrastructure deficit that has not received enough investment for many years to even keep up with minimum standards. He said that doing nothing, water rates are expected to increase 100%, with wastewater rates increasing up to 400%. Against these challenges, the Mayor set the course with the

REI, receiving more than 24 responses. Staff worked through those responses with the help of the Infrastructure Advisory Commission (IAC) and public input, and the Mayor proposed this transaction on March 10, 2010. Mr. Cotterill said that this proposal will result in more than \$425 million being appropriated for infrastructure improvements, provide a 25% rate mitigation for ratepayers, and will put the city's utilities into the safety of a public charitable trust for non-partisan control. He said that they have held a number of meetings and received widespread support for this initiative, but he realizes there are still some questions unanswered. He said that some have raised concerns about the acquisition price, and why the city expects to receive a minimum of \$434.7 million and maximum of \$458.7 million from this transaction to invest in infrastructure. He said that they also expect to realize approximately \$1.94 billion in savings over 30 years from synergies of utility operations. He introduced Carey Lykins, president and chief executive officer of CEG, to explain more about how the operation will work.

Mr. Lykins stated that vision and values guide CEG, with a customer-focused culture, a commitment to community, and a goal for transparency and public input. He said that they have been asked the question that if they are truly a not-for-profit entity, why would they want to do this transaction. He said the only answer he can give is that it fulfills CEG's mission to the community to benefit the citizens with utility service at the best cost. He said that he believes they can also benefit economic development and the quality of life in the city by keeping five utility rates as low as they can be. He said that they are very customer-focused, answering over 650,000 phone calls in their call center last year. CEG wrote approximately 66,000 payment arrangements last year, and pledges to work with any customer for flexible payment to continue providing service, as well as assistance as needed. He said that all stakeholders are customers, and that includes city staff, legislative bodies, regulatory entities, employees, and contractors. Because of their nature, Citizens is deeply rooted in and committed to the success of their community, focusing resources on economic development, neighborhood revitalization, education issues, and other philanthropic opportunities. CEG has invested over \$50 million in the past 10 years in these philanthropic endeavors, not a penny of which comes from rates. He said that CEG is sensitive to public input. They live here, work here, are committed to this community, and do take local concerns seriously. Mr. Lykins said that he believes their history and track record clearly show that. He said that the charitable public trust allows for local ownership, so that decisions are made here and will remain here. He said that CEG has a track record of providing safe, dependable utility service, and will continue to do so. He added that both utilities will be regulated by state and federal regulatory bodies, as well as retaining highly skilled technical staff to serve in both utilities. CEG is committed to achieving the \$43 million in annual savings, after the transition period, through consolidation and synergies, as an obligation to their customers. Mr. Lykins further reassured members that this savings will not be achieved through any layoffs, and emphasized that Citizens will need current employees for their expertise. CEG plans to apply their same customer satisfaction record to the water and wastewater utilities, while providing safe and reliable service. Citizens is dedicated to the conclusion of the combined sewer overflow (CSO) problem and the septic tank elimination program (STEP). He said that

they are working on a smooth transition plan now, with the city, with stakeholders, and with Veolia and United Water, and hope to speak more regarding specifics of that plan on the 19th. He said they intend to have the proper expertise in place so that the Council can be assured that they will be fully capable of operating these utilities.

Mr. Lykins introduced Richard Thrapp, partner at Ice Miller and counsel to CEG in this transaction, to walk members through the definitive agreements. Mr. Thrapp stated that the MOU approved on May 17, 2010 is included in the binder and set the tone for subsequent negotiations. Both parties, the city and Citizens, negotiated in earnest and used just about every minute possible to provide detail and define assets and liabilities through the drafting of these definitive agreements. He said that each definitive agreement is over 70 pages long, and is very detail-oriented. They found that the water utility was a little easier to provide detail on, as it had changed hands in 2002, and they knew a little more about it. Both definitive agreements follow the same customary format for transactions of this size, with 16 articles that can be summarized in six categories:

- Assets (acquired and excluded)
- Liabilities (assumed and excluded)
- Purchase Price/Assumed Debt/Payments in Lieu of Taxes (PILOT)
- Representations, warranties, indemnifications, escrow, dispute resolution
- Pre-closing conditions
- Ongoing Agreements and Covenants

Mr. Thrapp began with discussion regarding the wastewater definitive agreement. He said that with regard to assets, there was quite a bit of discussion about where the stormwater system, which is not being acquired, ends and where the combined sewer and wastewater systems, which are being acquired, start. He said that many of the assets come with required repairs or upgrades, and therefore requires a commitment to maintain those assets to the benefit of citizens. There was also quite a bit of discussion about property held for future expansion of the systems, as to whether they were necessary or important to the operation of the system. With respect to the dividing line between the combined sewer system assets and the stormwater assets, the city proposed to look at the way the line is divided in the National Pollutant Discharge Elimination System (NPDES) of the Environmental Protection Agency (EPA). He said that they also looked at the EPA consent decree, which also had provisions dealing with this dividing line. He added that there are bonds outstanding on both the stormwater and wastewater systems, and the expenses associated with an asset are accounted for, usually in one bond issuance or another. Looking at all these factors, Citizens agreed with the combined terms included in the definitions section of the agreement. Mr. Thrapp detailed the acquired assets and excluded assets as listed on the first page of Exhibit A (attached...begins with page 18). He further reviewed assumed and excluded liabilities (pages 19 and 20 of Exhibit A). Mr. Thrapp reviewed the total purchase price of \$262.6 million, with \$170.6 million paid at closing, less \$1.2 million for a surety downgrade and \$1 million to cover environmental insurance on both systems. The

remaining \$92 million will be paid on October 1, 2011. The city had asked for security on this deferred payment, and the ultimate arrangement was to issue a bond to collateralize that \$92 million payment. Citizens will assume a total of \$611,992,250 in debt as a part of this transaction: \$434,094,250 of state revolving fund (SRF) debt, \$39,290,000 in non-SRF debt, \$85,000,000 of a Wells Fargo line of credit, and \$53,608,000 in general obligation (GO) debt. Mr. Thrapp added that the PILOT payment CEG will be taking on in accordance with a recently passed ordinance is also addressed in this section of the definitive agreement. The sanitary district payment to CEG is directly provided for in the MOU, with financing detailed in the definitive agreements in the amount of \$4.7 million for STEP financing cost obligations. Mr. Thrapp said that the bulk of the agreements are statements and schedules that include representations, warranties, indemnification obligations, escrow and dispute resolutions. These schedules are living and breathing documents and account for developments right up until the time of signing, and are continually updated so that they are accurate and fresh, and are therefore not locked in until closing. These documents, however, form the knowledge base for due diligence to insure that CEG can meet the commitments under the agreements and run the system as it should be run. With respect to claims that may exist under these representations and warranties, the parties have agreed on a \$40 million combined cap cash escrow, which will be put into a separate account; and if there are issues that come up under the agreement, amounts will be paid out of that account. This is a liquidated sum and cannot go above the \$40 million, with very few exceptions. There is also a \$1 million threshold to keep the parties from matters that do not warrant significant attention in a \$1.7 billion transaction. He added that there are dispute resolution provisions in the agreement to maintain a business-like, civilized transaction. He said that there are standing panels that are empowered to deal with different aspects, such as financial issues and real estate concerns, that do not reach this \$1 million threshold. Both sides have chosen representatives that they can rely upon to make informed wise decisions to serve on those panels.

Mr. Thrapp said that the closing timing is somewhat driven by the water agreement, and will occur after the water rate case is decided by the Indiana Utility Regulatory Commission (IURC), and is roughly estimated to be some time in the first quarter of 2011. He reviewed ongoing agreements and covenants as detailed in the definitive agreement and listed on pages 24 through 27 of Exhibit A. He said that there are currently MOUs with each of the contracted vendors (United Water on the wastewater side and Veolia on the water side), whereby Citizens has agreed to negotiate with them toward a longer-term arrangement, provided that certain goals CEG has established are met, such as achieving and maximizing synergies and optimizing systems. Should these goals not be met and a termination is necessary with financial obligations, this would be paid for out of that escrow account. CEG has agreed to indemnify the city for any amount beyond that \$40 million. With respect to a smooth transition for waterworks and union employees, they have taken steps to insure that no one will lose their job, and CEG has agreed to take 34 of the non-union positions, and the city will retain the others within city government. The agreement contains specific provisions regarding

the union positions and no one losing their job. There are lengthy provisions in both agreements regarding the public charitable trust and how it operates, allowing CEG to hold assets in order to provide reasonable service at reasonable rates for the benefit of the citizens of this city. He added that CEG holding the assets also distances it from partisan political control and will help to produce synergies. He stated that the city had asked from the beginning that the city have the right of first refusal should Citizens seek to sell the water utility. Citizens maintains that the trust prohibits the sale, lease or disposal of assets, except for surplus property, and that this is not an issue. However, provisions for the right of first refusal are included in the agreements to insure that the systems will never be transferred to, or owned by, a for-profit entity for the benefit and profit of private investors or shareholders. He said that provisions are included limiting rate increases to no more than 10.75% annually until 2013, and allowing for rights-of-way repairs. He added that the minority business enterprise, women business enterprise and veterans business enterprise (MBE/WBE/VBE) benchmarks will be met in accordance with city minimum standards of 15% for MBE, 8% for WBE, and 3% for VBE. He said that these are minimum goals, and Citizens hopes and expects to exceed these goals.

Mr. Thrapp then reviewed highlights of the water system agreement (beginning on page 28 of Exhibit A) that differ from those in the wastewater agreement. With regard to assets, this agreement includes Geist Reservoir, Morse Reservoir, the Canal and Wellfields as acquired assets, while Eagle Creek Reservoir remains an excluded asset. Mr. Thrapp explained that Eagle Creek was a flood control project, whereas Geist and Morse were projects to specifically create water supply and were part of the water company up until 2002, when the city acquired those assets. While Eagle Creek is a flood control project, as well as a recreational area, there is water that is used in the water system, and there will be a negotiated water usage agreement as a part of the transaction. The main difference in the assumed liabilities is with regard to retiree medical benefits specifically covered by the Veolia agreement. Most other provisions are the same, but there are provisions regarding the water rates remaining at the rate case level for at least two years. Citizens will continue to provide the same public access to the reservoirs and canal as is currently available, subject to the safe operation of the system. Geist has certain license agreements for access, and those will be assumed by Citizens. With respect to the headquarters of the Water Company, after a determination is made by Citizens as to whether or not that property is integral to water operations or synergies, the city will have a 10-year option to purchase the property if CEG decides to market or sell, with some lease options if the option to sell is exercised before January 1, 2012.

Chairman Vaughn called for public testimony at 6:59 p.m.

Glenn Pratt, citizen, stated that he has been involved in environmental management positions at both the state and federal levels, and the combined sewer overflow (CSO) situation is an inherited situation for this administration that has been ignored for years. For years, there were federal grants available to help with some of these larger

infrastructure projects, but those grants are no longer available, yet the city finds itself needing to put in sidewalks so that children can walk safely to the bus stop or school. He said that no other cities have the raw sewage problems that Indianapolis has had, and he is glad to hear the STEP program will continue. He added that he hopes they will find a way to do the same thing regarding private water, as most cities have banned septic tanks and well water. He said that with the consent decree, many things have to be done to rectify these problems. He said that the city is going down the right road, but he hopes they provide a marriage of equals, and while transferring the water and sewage systems, he hopes they put qualified staff in place to run those systems efficiently.

Larry Vaughn, citizen, said that this is like a Billy Mays infomercial "Sham Wow" deal, and every problem this city faces seems to always be someone else's fault. He said that he does not believe a private corporation that has been shown to abandon brownfields will do what is right for the citizens. He said that there are people in the city who can solve these problems, and they do not need a foreign corporation to come in and secure Build America Bonds to address this problem. He said that this administration seems to simply be desperate to fund other obligations that they have not been collecting enough tax dollars to fix. He said that doing this transaction is stabbing the citizens in the back, and Citizens Energy Group did not put Councillors into office. He said that they are jeopardizing the water system, which is doing well right now. He said that there are four water company properties valued at over \$3.5 billion (Geist, Morse, Canal, Canal Towpath), and yet Citizens is only coming to the table with \$100 million. He added that they will never come back to the table with more, because they have the option to deduct their assets at fair market value, which the city is literally giving away. CEG says they do not have any money, because they are a charitable trust, yet that is not true. He said that Mr. Cotterill testified at three prior hearings that he would present the trust documents, and he has yet to provide them, because they do not exist. Mr. Vaughn said that CEG is a private, for-profit organization that is going around the country tricking people and saddling cities with forfeited bond repayments, after they have sold all the assets. He said that they need to scrutinize this deal more and he would have expected more from the attorneys on the Council. He said that the city will maybe get \$20 million from this deal when it is all said and done, which will not be enough to address the city's infrastructure needs. He added that he does not know how the Council can support this transaction for a legislative charter.

Andrew Troemner, economic student at Indiana University-Purdue University of Indianapolis (IUPUI), stated that he has concerns about the economic consequences of this deal. He said that the two major goals of this transaction seem to be an upgrade of the city water system and an upgrade of street infrastructure, which rightfully probably should have been done 10 to 15 years ago. He said that it has been testified that they are funding these upgrades partially through bonds, and the rest through increasing efficiency through synergies, and the ultimate rate increases that have been assumed in all the scenarios that the city has looked at. He said that the economy is sick right now, and is not getting better. The forecast is extremely poor, and consumer confidence has

plummeted. He said that the worst thing the administration could do during an economic downturn like this is to increase rates or taxes. He said that he worries about the consequences for consumers. While CEG has portrayed itself as a good corporate citizen who has helped to alleviate bills for some individuals, the burden for meeting the needs of these individuals is borne through increased charges for services on everyone else. He said that there is already a way to deal with poverty issues, which is through a progressive tax structure, charging higher taxes on people who have more. A regressive tax squeezes the middle class, and he worries about the health of the city and unemployment rates when a regressive tax structure is used. He said that the administration needs to reconsider how they finance critical investments.

Tina Simpson, concerned taxpayer, said that in 2005, the city refinanced \$550 million in fixed rate bonds to raise money to finance its acquisition of the Water Company, and now in 2010, they are selling the water and sewer systems for a net gain of \$425 million. She said that her concern is that the city, and therefore, the citizens, are being sold short. She said that she assumes an appraisal report has been done on the water company, but she has not seen such a report. She would like to know if an appraisal has been done and if it has, why it has not been made available to the public. She said that such reports should include critical assets like Geist, Morse, the Canal and the wellfields, and the administration should consider the highest and best use for these properties.

Chairman Vaughn stated that appraisals have been done, and he asked Mr. Cotterill if this information is available to the public. Mr. Cotterill responded in the affirmative, and said that such documents are available on the website at www.indy.gov/utilities and also at their FTP (file transfer protocol) site: [ftp.indygov.org/utilities](ftp://ftp.indygov.org/utilities), with more than 500 other documents. He said that the FTP site will prompt for a username and password, both of which should be entered as "public." He said that appraisals were performed by a private accounting firm, RW Beck, and the value of the additional properties was indeed taken into consideration. He said that a subsequent loan taken out on the water company after its purchase and a five-year rate moratorium has essentially made the water company worth its debt, and therefore, the water system is essentially being transferred for its debt. He said that if they transferred it for any extra value, the ratepayers would have to bear that increase through a rate increase, because of further debt issued five years ago.

Eva Startek, general manager of Heartland Read-Mix, stated that they are a minority-owned concrete company with both CEG and Veolia as customers. She said that their association with CEG has allowed them to expand and grow, and they support the transaction and look forward to continuing to work with CEG and Veolia in the future.

Steve Corbitt, president of Corbitt and Sons Construction, stated that his is also a minority-owned business which shares a great relationship with Veolia and United Water. He said that these entities have expressed a great interest in diversity, which has helped his company grow. He said that Corbitt & Sons has been in business for 32

years, and for the last 18 years, during his presidency, they have had a relationship with CEG which has allowed the company to grow and thrive in Indianapolis. He said that the company started in 1992 with three employees, and had a terrible gas explosion in their first year, but CEG embraced their company and helped them hire and train individuals and overcome that tragedy. He said that with the help of CEG's commitment, last year alone they had \$262,000 of W-2 payroll dollars that went to ex-offenders, and this transaction will retain and create new jobs to continue to address these types of community issues. He said that he has been a member of the Chamber of Commerce for many years, and there has long been a need to fix infrastructure, which will help with economic development and job growth. He said that this transaction will help to provide hope and employment for individuals and move the city forward in a positive manner.

Tim Harris, founder of Harris & Ford, LLC, a minority-owned business in the city, stated that they started in 1994, and United Water expressed an interest in doing business with certified MBE companies. Now they are supplying United Water in 25 different cities around the country, and when Veolia first came in to operate, he was against them because he had a track record with United Water. But Veolia was awarded the business, and also contacted him to improve MBE business participation, and he has subsequently also had a great working relationship with them in Indianapolis, as well as other cities. His longest association, however, is with CEG, which goes back to 1985, before there was a Harris & Ford. He said that CEG gave him an opportunity to prove himself, and Harris & Ford is now the largest black-owned business in the state of Indiana, doing over \$200 million of business a year. He said that it is because of companies like CEG that they have had the opportunity to become successful, and he enjoys his working relationship with this company and hopes to continue and expand his business even more.

Chris Pryor, Metropolitan Indianapolis Board of Realtors (MIBOR), stated that MIBOR supports the proposal, as it represents a good opportunity for homeowners to receive some rate mitigation due to efficiencies. He said that it will also address the health and environment of neighborhoods, while providing safe reliable utility service and addressing infrastructure, CSO and STEP needs. He said that MIBOR believes this will help increase property values and be a good thing for economic development in the city. He said that it is important to remove politics from the utility systems, as past politics have resulted in the challenges the city faces today. He asked the committee to support the transaction.

Grant Smith, Citizens Action Coalition, stated that they represent ratepayers for the IURC and lobby mainly at the State House on energy and utility issues. He said that it is refreshing to hear how important the public sector is to economic development, and a lot of businesses could not survive in this city without the help of the public sector. He said that the appeal to both the ratepayer and taxpayer in this deal has been the projected savings. He said that the ordinance states that savings will occur in the amount of approximately \$40 million a year in synergies and a reduction of \$100 million

in debt management. He asked if CEG can guarantee this savings to the ratepayers of Indianapolis. Mr. Lykins said that it is Citizens' firm belief that they will be able to achieve the \$40 million annual savings, or better, after the transition period of two years. He said that these savings were estimated with the help of a consulting company, and they compared scenarios with examples of savings of a similar nature to other transactions in the past. Their due diligence has confirmed that this is the likely amount of savings, and CEG feels good about achieving such. He said that there is no guarantee written into the contract, as they do not live in a world where they can offer that type of a guarantee, due to unexpected factors like financial collapse or hyper-inflation. He said that Citizens expects to be held fully accountable in their efforts to achieve those savings by IURC and their board of directors, and he feels confident that they can deliver on that promise.

Chairman Vaughn recognized State Senator Greg Taylor, and stated that following questions by members of the committee, the Utility Transfer Oversight Committee will adjourn without taking a vote on the proposal. The committee will then re-convene on Monday, July 19, 2010 at 5:30 p.m. where outstanding questions can be answered. Councillor Sanders asked if this evening concludes public testimony or if the public will be allowed to speak again at the meeting on July 19. Chairman Vaughn said that he will again allow public testimony at the July 19th meeting.

Councillor Mansfield said that she is concerned that the final documents do not have claw-back provisions if the projected savings do not occur. She said that she also has concerns that the estimates of savings are based on a 20% assumed increase in water consumption, and she does not know how that increase is assumed, given the economic climate and lack of growth. She added that a self-appointed board does not provide the same accountability as an elected body. Mr. Cotterill answered that putting the systems into a public charitable trust in perpetuity will actually aid in accountability, as has been evidenced by the history of the gas company. He said that the Mayor's vision was to remove the politics from utility operation, and putting it into the hands of the public trust does that. He said that there are many provisions in the trust that act as its own claw-back, and they feel the protections the trust offers are a governance model that works, where political appointments have not always seemed to work.

Councillor Speedy asked with respect to the two payments that make up the purchase price and the bonds which will be issued to pay the city, what the best estimate in terms of savings is that would give a bondholder security for this debt. Mr. Lykins said that the bondholders will look at the revenue streams of the individual utilities. They are only issuing bonds on the wastewater system, not the water system, and the bondholders would want to see that the revenues after operating expenses would cover the debt service. He said that bondholders typically require that the debt coverage service ratio be 1.1 times what is needed to make the annual principal interest payments. Bondholders do not necessarily look at the projected savings. Councillor Speedy asked if Mr. Lykins knows the range of the debt service. Mr. Lykins said that he does not know the annual debt service off-hand, but they are hoping to market Build America Bonds at

a debt service of \$15 to \$18 million a year. Councillor Speedy asked if that is then less than half of the savings projected. Mr. Lykins said that he believes the bonds will be issued at a third, or less, than the projected savings. Councillor Speedy asked Mr. Lykins to provide him with the actual debt service estimates by the next meeting.

Councillor Sanders said that she has concerns about the intrinsic value of the assets included in this transaction. She said that it sounds like a unilateral decision was made to determine that the value of the water company was equal to its debt, without any consideration beyond assessing the debt. She said that she is concerned that the intrinsic value of a natural resource has not been taken into consideration. She also has a hard time getting a grip on the idea of the city transferring assets to itself. As a public trust, the city essentially owns the assets of Citizens Gas, so the city is in effect transferring its own assets to itself and somehow garnering equity with borrowed money to the tune of \$425 million. She said that she does not understand this transaction. She added that she also does not understand how they can include the option to buy back the headquarters in 10 years even though they own the property as a part of the public trust. Mr. Cotterill said that he is not sure how they would have addressed the intrinsic value of the water system properties. To determine the value, they looked at the debt on the books, the rate increase request at the IURC, and the revenue required to operate the system. He added that the water company has been abused over the last several years, and it was time to put it in a better place. He stated that the agreement related to the waterworks is a pure transfer. He said that there are other ways to assess utilities as to their value, but they started with the proposition that taking any additional value out of the water system would only be borne by the water ratepayers who were suffering from a 10% emergency rate increase because of the variable debt several years ago. He said that the administration felt the ratepayers had paid enough and they wanted to provide the benefit of a 25% rate mitigation. He added that the intrinsic value of Geist, Morse and the Canal is probably best embodied by the retention of public access, even though they are not retaining the monetary value. Mr. Thrapp said that the public trust exists separately from the city and is not under political control. The statute that creates the board of directors for utilities by the Indiana Legislature specifically created a separate body that is chosen by a board of trustees and established with separate powers and authorities and is not under the political control of the Mayor and the City-County Council. It is an entity in and of itself, is controlled separately, its assets are held separately, its liabilities are separate, and the obligations of the city are not obligations of CEG, and vice versa. With respect to this particular situation, there is also another distinguishing feature, which is the existence of a public charitable trust, which is provided by the judiciary branch of government with long-standing case law. CEG is proposing that the benefits and history associated with its existence as a public charitable trust also continue with respect to the wastewater and water systems to provide that separateness, which allows the sale to occur.

Councillor Sanders said that she still believes there are other ways to determine the true value of this resource and these properties, whose value will only increase. She said that Mr. Thrapp mentioned that CEG is separate, but she has asked for the public

charitable trust documents, and has not seen those. She asked if Mr. Thrapp believes the city owns the assets of the gas company. Mr. Cotterill said that the public charitable trust documents were provided to the Council after Councillor Malone requested them, and they have been available on the website for several months. Councillor Sanders said that there is no real document, only court proceedings that define the entity. Mr. Cotterill said that it is not one document, but is a collection of documents embodying the public charitable trust. He asked if Councillor Sanders is suggesting they should transfer the water system, but get more money for it because of its intrinsic value. Councillor Sanders said that she is more accurately suggesting that they should transfer the operations of the water system, but retain the assets. Mr. Cotterill said that a strict operating agreement could have been one approach, but the Mayor's proposal contemplates transfer of both ownership and operation, as the ownership is fundamental to the protections of the charitable trust, which will continue to be debated.

Councillor Bateman asked how parks are included in the aggregate and what will happen to them. Mr. Cotterill said that some people characterize Geist, Morse and the Canal as parks, and the definitive agreements allow for continued public access to these assets. However, these entities transport more than 80% of the water system, and therefore are essential to providing the water utility, and that is why those assets are being transferred with the sale. In the 1940s, public access began on Geist, and it was allowed through all previous owners and will continue. He said that transferring the assets will protect the water supply, but public access will still be provided for in the agreement. He said that there are no other parks being transferred in the transaction.

Councillor Mahern said that Mr. Cotterill made the statement that the administration did not want to burden ratepayers in terms of water any longer, but asked if there are wastewater customers who are not water customers, who will then be burdened with additional rate increases due to debt financing. Mr. Cotterill said that water and wastewater customers are primarily one and the same, but as Councillor Mahern well knows, there are customers outside the borders of the county on the water system, and some within the borders who receive water, but are on a septic system, and others who receive sewage service, but own their own well. He said that the administration believes the water system had been greatly leveraged, maybe not fully, but substantially; and they felt that it was time to say "enough." The proposal for the wastewater system is not a cashless transfer, although some have suggested it should be. He said that he believes a 25% rate mitigation is a tremendous benefit to the ratepayers, as opposed to doing nothing. While ratepayers could possibly see up to a 29% rate mitigation without the \$425 million purchase price financing, there would be no investment in infrastructure. The Mayor, therefore, felt this was the best proposal to get the needed funds for infrastructure. While 4% of additional rate mitigation is not insignificant to individual ratepayers, it is not anywhere near as significant when comparing a \$425 million investment against an \$11 million road resurfacing budget in 2007. Mr. Cotterill said that the ratepayers are getting 96% of the benefit of the savings projected; yet given the other challenges facing the city and quality of life of citizens, such as roads, sidewalks, bridges and abandoned homes, the Mayor felt the \$425

million was a much more significant investment. Councillor Mahern said that he is not challenging what amount the city will get, but he is challenging the fact that there is still no clarity on the true amount of savings, as Mr. Lykins testified that it cannot be defined or guaranteed. He said that his concern is that if those savings are not achieved, there are no claw-back provisions in place for the city to have any further say on that effect on citizens. He added that while Mr. Lykins says he will be held accountable by the IURC and CEG's board, the Council no longer has any clear indication of what occurs if those savings do not happen. Mr. Cotterill said that everyone wants a guarantee, but the only guarantee he can offer is that if they do not do this transaction, there is no savings. He said that there has been a tremendous amount of work and thought put into this by a lot of people, along with multiple discussions with advisors and paid consultants, public meetings, due diligence, and investigation by multiple boards. Based on what they know, all parties believe this savings can be accomplished. He said that even if they were not to achieve the mitigation they project, he believes the history of the charitable trust has its own intrinsic value.

Councillor Speedy asked with regard to the escrow account, if that \$40 million is for both parties and issues or contingencies on either side, and who ultimately owns that money and where it would go if not used. Mr. Thrapp said that the escrow serves many purposes. It backs up the city's warranties to CEG and is the source by which parties would be able to get out of existing contracts if an agreement is not reached with the contracted vendors. He said that there is a provision that if CEG minimizes the amount used from that escrow fund, they have a vested interest and would receive 37.5% of unused funds, causing them to think twice before making claims against the escrow. Councillor Speedy asked when that fund would no longer be needed and could be dissolved. Mr. Thrapp said that there is a two-year period before that fund would lapse, and at that time, CEG would receive 37.5% of the remaining funds, and the city would receive the rest.

Councillor Lewis asked how other MBE/WBE companies can be invited to the table for involvement in this process, as it is her understanding that CEG does not follow the same bidding process that the city or state does. Mr. Lykins said that he is not familiar with the city's bidding process, but they currently employ 98 to 100 MBE/WBE vendors and conduct a couple of fairs each year, working with agencies that certify vendors. They want to insure that appropriate contractors are given the opportunity to bid on any work available. Councillor Lewis said that the percentage benchmarks included in these agreements seem pretty standard, and she thought that CEG had agreed to meet or exceed the current numbers of Veolia or United Water. She asked what has changed. Mr. Lykins said that nothing has changed, and these are the same minimum goals outlined in the city's guidelines, as well as the contracts for Veolia and United Water. United Water and Veolia have exceeded these goals, and it is CEG's intention to continue to work to exceed these goals. Chairman Vaughn added that he believes during the minimum goals discussion, it was discovered that Veolia and United Water's goals were actually lower than the city's benchmark goals. Mr. Cotterill stated that this is correct. Chairman Vaughn said that his recollection is that United and Veolia's

contracts provided some incentive to reach a certain level of participation in excess of benchmarks, and in comparing the contracts side by side, the new agreements seem to actually have a higher minimum goal than the contracts currently in place, even though the participation numbers exceed those benchmarks. Mr. Lykins said that he does not want to leave the impression that CEG just stuck some minimum numbers in an agreement and does not have a commitment and passion for supporting MBE/WBE/VBE enterprises. He said that they have plans to exceed those minimum numbers and expect to be successful. Councillor Lewis said that from previous conversations, she understood Citizens was committing to meet or exceed the current numbers of Veolia and United, but by including these standard minimum numbers, they seem to be back-pedaling out of that commitment. Mr. Cotterill said that those percentages are based on a historical disparity study, and these goals are based on historical discrimination. He said that Veolia and United contracts include incentives to reach above those goals, and CEG is also committed to reaching above those goals. Mr. Lykins added that they are not stepping back from their promise to make every effort to exceed those goals, and are now in the process of re-negotiating those contracts, and would adhere to their same previous standards. He said that he never meant to say, if it was implied previously, that CEG would set their minimum goals at Veolia and United's previous attainments, even though it is certainly their intent to exceed the goals set forth.

Councillor Sanders referred to the escrow account, and asked if that \$40 million is coming out of the \$262 million sale price. Mr. Thrapp said that in addition to the \$262 million purchase price, there will be an additional \$75 million of general fund dollars, and the escrow will come out of that pool of money. Councillor Sanders asked if he is referring to the Sanitary General Fund. Mr. Thrapp responded in the affirmative. Councillor Sanders asked what the balance in that fund is currently. Mr. Thrapp said that at the time of closing, that balance is estimated at approximately \$75 million. Nate Feltman, transaction counsel to the city, Baker & Daniels, stated that he believes it is between \$75 and \$80 million currently. Councillor Sanders asked if those monies are used for debt service at this time. Mr. Thrapp said that this is the general operating fund, where revenues over expenses go, and it continues to build. Councillor Sanders said that as she recalls, that balance was \$50 to \$60 million two months ago. Mr. Thrapp said that he believes that is correct. Councillor Sanders asked if the \$4.7 million will come out of that, as well, reducing the overall purchase price by about \$45 million for two years. Mr. Cotterill said that on page 12, question 17, of the memo he sent Councillor Sanders on June 25, 2010, the \$262 million purchase price is broken down into the \$170.6 million payment at closing and the \$92 million payment on October 1, 2011. The proceeds to the city include another \$140 million from the PILOT bond issuance, \$75 million from the Sanitation General Fund, and \$13 million projected in accounts payable and receivable from the wastewater system; which totals \$490.6 million. Question 18 on that letter then asks what costs the city anticipates, which includes \$1.2 million for SRF debt service, \$4.7 million for the city's obligations on an aggressive timeline to move forward with the STEP program, \$1 million for two environmental insurance policies, and \$9 million in city transaction costs. All of those

taken into consideration, plus the \$40 million in escrow, leaves the proceeds at a minimum of \$434.7 million.

Councillor Sanders asked for more explanation regarding the creation of the CWA, which is a corporation that does not exist at this time. Mr. Thrapp said that the CWA Authority is a non-profit authority included in the intergovernmental agreement, and the authority to run the sanitary district would be transferred to this entity. The CWA's board would be essentially the same board that governs CEG, and the authority is an instrumentality of Citizens with provisions in the agreement regarding its status. He said that it would be exempt from federal tax, and would be the entity that would own the wastewater system. Councillor Sanders asked if this authority would be a private not-for-profit under Indiana law. Mr. Thrapp said that it would not be a private non-profit, but would be an instrumentality of CEG, and therefore, in the nature of a public non-profit. Councillor Sanders said that it is important to know, given IURC's oversight, whether it is a private utility or a municipal utility. Mr. Thrapp said that their existence as a non-profit entity operating a wastewater system would, per IURC statutes, give them jurisdiction over that. The authority would either be governed by the IURC as a non-profit entity, or IURC may regulate it under Citizens' statutory authority. In either event, the assets would be held in a separate entity for purposes of paying the PILOT payments. The separate authority would help facilitate the IURC jurisdiction and better assist in making sure gas system repairs would not be paid for CSO projects in the consent decree. This insures that the utilities remain separate, so that operations are not subsidizing one another. Councillor Sanders asked if the non-profit entity is in the public trust. Mr. Thrapp answered in the affirmative. Councillor Sanders asked if they can do this even though wastewater is not defined in state statute for the public trust. Mr. Cotterill said that it is complicated, and although wastewater is not one of the express utilities run by the Department of Public Utilities as water is, there are other provisions in CEG's case law that allow it to run the wastewater system. Councillor Sanders asked if they will not know if this entity will be treated as a governmental entity or not-for-profit until it goes before the IURC. Mr. Thrapp said that the authority will be formed pursuant to the intergovernmental agreement and will have the characteristics that it has. He said that when it goes before the IURC, there will be briefings regarding the regulation of this entity as a non-profit. Mr. Cotterill said that through the course of the negotiations, the city focused on insuring that this authority was included in the public trust and was operated on a non-profit basis, or never operated on a for-profit basis. If they were regulated as a municipality, as opposed to a non-profit, they worked with Citizens to include language to restrict what a "return" could be, to protect them from the authority becoming a for-profit entity. This would give CEG some flexibility to protect them from becoming a for-profit enterprise. Chairman Vaughn said that as he recalls, one of the key reasons for providing this flexibility was to give CEG the ability to normalize rates long-term, as opposed to rate fluctuation based on consumption year to year. Mr. Lykins said that this is correct, and it is their proposal that this regulation would be the same model as Citizens Gas has been regulated for many decades. He said that they do not have provision for any "returns" in their plan today. Although he has been told that some of his predecessors considered a return during the hyper-

inflation period of the late 1970s because of the lag in proceedings taking up to nine months, they are not proposing anything new. They are proposing the same type of regulation CEG has had with the gas utility for the past several decades.

Councillor Mahern said that Mr. Lykins testified that the \$50 million in community philanthropic investment was not borne by ratepayers, and that this would not be appropriate. However, he wonders if this is not exactly what they are doing with this transaction, as the surplus amount of money paid for utilities will be going to make infrastructure improvements and will not be spent on putting pipes in the ground or for actual service. He said that Citizens is essentially funding benefits that are not related to the utility service through ratepayer rates. Mr. Lykins said that Citizens is selling bonds to raise money to fund the purchase of assets. With this transaction, utility customers will be getting lower rates, and what the city chooses to do with the proceeds of the sale is a different matter entirely. Councillor Mahern said that ratepayers will be paying more because of the bond issuance, and Mr. Lykins testified that they would not consider, after acquisition, using ratepayer money to fund anything other than providing the utility service. However, that is exactly what they are doing through this transaction and pretending not to know what those funds are used for does not change that fact. Mr. Lykins said that he does not want to give the pretense that he does not know what the city is going to do with the money from the purchase price, but it is ultimately not his decision on how those funds are spent. He said that after CEG owns the wastewater assets, which they are issuing the bonds in order to purchase, they are only able to use ratepayer dollars for wastewater system improvements.

Councillor Lewis said that the agreements indicate that money is being set aside for monitoring, and since this body will no longer have oversight, she asked how that process will work. Mr. Cotterill deferred to Chairman Vaughn, who has made it clear what he would like to see with regard to monitoring, and they have taken his advice. He said that one of those requests is for advisors to the Council, which is embodied in the approving ordinance. He said that there is an appropriation included in the ordinance to fund that advisor to the Council to oversee the transfer. Chairman Vaughn said that although it is subject to public records requests, its board meetings are open to the public, and it is regulated by the IURC, Citizens has a separate appointing board and there is no elected representative or appointment from an elected representative engaged in their day-to-day operations. That cuts both ways and is somewhat by design, so that the utility is run free from political influence, but as a consequence, is somewhat removed from accountability. He said that he worked with the Mayor's Office and CEG to come up with a means to monitor the process and advocate for ratepayers, yet not intrude on their ability to operate free of political control. He said that the tool they came up with is pretty much a mirror image of the surrounding counties' service advisory board, which is made up of members of the surrounding counties who receive some benefits of a service but are not citizens or elected officials in Marion County. These boards are typically funded to hire legal professionals to monitor the city and make sure they are not out of step with the needs of their own communities. He said that using that model, they set aside no less than \$100,000 annually, not to exceed

\$300,000 if not used, to hire professionals to be an advocate for ratepayers and be the Council's eyes and ears to keep them informed of what is happening and provide some accountability.

Councillor Mahern asked if this provision might be the mechanism whereby the claw-back, which is not in the agreement, might be effectuated to oversee compliance with performance and savings benchmarks. Chairman Vaughn said that he does not want to overstate the power that this position would have, as they are not a voting member of the board or trustees, and do not necessarily have any influence over Citizens' day-to-day actions. However, they would be there to inform the Council of what is happening, to do the research to make sure the decisions being made are the best decisions for the citizens, or to advocate at ratepayer case hearings. He said that it would not really be a position of influence, but rather accountability.

Councillor Sanders asked if there is a document that creates this board or position. She said that the approving ordinance creates the fund, but asked where this service advisory board is created. Chairman Vaughn said that the service advisory board currently exists, and will continue to do so. He said that these funds will be for a separate position or positions to be hired by this Council outside of the service advisory board. Approval of that mechanism is also found in the approving ordinance. Mr. Cotterill said that it can be found in Section 2, division 5.

Councillor Mahern said that during discussions, a belief was stated that the city would not need a clause to buy back the utility, because Citizens believed it could not be sold, once in the trust. However, the provisions added to the agreements indicate that the city could purchase the utility back at a fair value or the outstanding bond obligations. Mr. Thrapp said that the provision is for the fair value of the utility, provided the bonds are taken care of. He added that the bondholders need to see that the bonds will be covered, should any situation occur, even though remotely unlikely. Councillor Mahern asked if there is a sense that there are more bonds being issued than the fair market value, and that is why the provision was included. Mr. Thrapp said that he believes Councillor Mahern is overstating the concern. He said that bondholders simply want to know that the bonds will be taken care of if this provision is triggered and the right of first refusal is exercised. Councillor Mahern said that it is not far-fetched to say that the debt might be the driving force in the fair value. Mr. Thrapp said that debt is always a key component in determining fair value. Councillor Mahern asked if the city would then potentially have to cover bad decisions on debt issuance made by Citizens in the time that it held the assets. Mr. Thrapp said that this would only happen if there were to be a transfer and the city wanted to exercise the right of first refusal. He said it is not a mandatory buy, but is simply a right of first refusal. Councillor Mahern said that Mr. Cotterill has testified on many occasions that it is important that this utility be held by the city or a non-profit entity. It seems this could be a situation where the city would forego purchasing the utility in order not to take on the debt. At that point, a for-profit private entity could then acquire the assets. Mr. Thrapp said that Councillor Mahern is talking about a situation that Citizens does not think can occur. He said that early on, CEG

was not interested in talking about a right of first refusal, because they do not see it existing in reality. He said the reason CEG agreed to this language being included, is that without it, there might be a hindrance in marketing the bonds. Councillor Mahern said that he appreciates that CEG does not think this can happen, but the fact is that the language has been added, which in his opinion is an improvement. He added that there is a legitimate concern and asked if the debt is such that the city believes it is not prudent to acquire those assets back, if CEG could then sell the assets to another entity. Mr. Thrapp said that Citizens does not believe it can sell, so he does not feel this is a fair conclusion. Mr. Cotterill said that in the unlikely case of the failure of the trust, the city would decide to purchase or not to purchase only with the Council's approval, and therefore, the Council body would have a very strong say in such a transaction.

Councillor Mahern said that the city is to retain accounts receivable, and there was some discussion regarding state law prohibiting the disconnection of service to customers of one utility because of money owed to another utility. He asked how the city would deal with their lack of ability to force payment, when the customer is then receiving service from another utility. Mr. Cotterill said that they are working through the due diligence process to find more effective mechanisms, separate from shut-off, to collect on outstanding bills. Mr. Thrapp said that James Steele, Council Chief Financial Officer, has suggested a mechanism to aid in collection of a bill when a customer's billing cycle straddles that closing time frame. He said that with regard to an incentive on the part of CEG to continue service in order to increase accounts receivable, even though the customer may not have paid a previous bill prior to the transfer, there is a transition services agreement with mechanisms to protect the interests of both the city and CEG. He said that these mechanisms are still being worked out, and he believes the city's interests will be fully covered by the time this transaction is finalized. Councillor Mahern asked what the magnitude of the accounts receivable during that transition period might be. Mr. Thrapp said that he does not know off-hand, but will get that information to Councillor Mahern by the next meeting.

Chairman Vaughn asked if the public or Councillors have more unanswered questions, that they make those available to himself or Mr. Cotterill before the next meeting, so that a response can be provided.

There being no further business, and upon motion duly made, the Utility Transfer Oversight Committee was adjourned at 8:36 p.m. to be re-convened at 5:30 p.m. on July 19, 2010 in the Public Assembly Room of the City-County Building.

Respectfully Submitted,

Ryan Vaughn, Chairman

RV/ag