Item No. 160846
June 1, 2017

UAB Statement 2

GREC rejected our offer. This was expected. In fact, before our last meeting I was talking with Justin Lock, and I said GREC will immediately reject this offer if the commission takes the UAB recommendation. It's in their interest to test our initial resolve, especially after such a close vote with the City Commission. It's in their interest to further test our resolve when two new city commissioners take their seats on May 4th. Expect another immediate rejection if we hold.

Companies follow the patterns of their leadership. GREC has shown one pattern over and over again. In my opinion, GREC lives on the edge of propriety, and they test that boundary constantly.

They lost a lawsuit with Wood Resource Recovery because they abandoned contractual terms that allowed yard waste to be delivered to their facility. Evidently, despite many claims to the contrary, the biomass plant cannot take yard waste.

They did not perform an annual maintenance, as required by our contract with GREC. This amounted to 21 days of overcharging GRU on the demand rate, which equals over $4 million dollars. This has gone to arbitration.

We pay a demand fee of over $70 million dollars a year. In addition to that, we pay incremental cost when the plant is on and these days it is rarely used. Imagine what we could have done with that $70 million dollars a year to improve our city.

The pattern seems to be a wake of destruction for their counterparties and enrichment for themselves. Good business is about a fair exchange of value for both parties, not about one party feeding off the other like a parasite.

Mayor Poe mentioned game theory in the last City Commission meeting. There are several strategies in game theory based on how the players play. Are they cooperative or zero sum? Cooperative outcomes tend to bring both parties gain, maybe not quite as much gain as an out and out win, but there is no loss to either party. Both win. It's a fair exchange of value. This is what I define in business terms as good business. Then there is the zero sum philosophy where no trust exists between the players and no cooperation occurs. One must win and one must lose. This is what I consider bad business philosophy. We've been playing a cooperative game while GREC has been playing a zero sum game. They are maximizing their outcomes at our expense because we are playing the wrong game and have been playing the wrong game since the beginnings of negotiation with GREC all the way back to 2009. Based on their patterns, $750 million dollars is way too much.

I asked our own CFO, Scott Thomas, to analyze the Goldman Sachs report. Prior to coming to our company, Scott was an investment banker for Bank of America and prior to that for UBS. His focus was the utility sector, specifically financing needs of the utility sector. He looked into the Goldman Sachs analysis and agrees with it. Remember Goldman Sachs valued the plant between $540 – 719 million.

Furthermore, I asked Scott to look at the possibility of someone else buying the biomass plant. Based on his analysis, to get the rate of return needed for a merchant plant and the borrowing cost, another buyer would not offer more than what we were offering at $675 million. In fact, another buyer would probably offer substantially less. Just to give you a sense of scale, FP&L has an A- rating, and based on their filings with FPSC, their borrowing rate to build regulated power plants is 6.61 percent. This might be higher for a merchant plant with one customer. Based on Scott's analysis and not factoring in expected values on risk, he indicates that an entity like FP&L would offer between $640 million and $730 million, but this doesn't take into account any of outcomes of arbitration

In any event, we know that so far no buyers with an acceptable price to GREC have come forward. We know this because we have the Right of First Offer (ROFO). They've had over three years to find one. This tells us something.

I already laid out much of the expected value risk in my last statement. Suffice it to say GREC could lose everything because the contract could be abrogated based on a material breach. At 10 percent risk, the expected value would be $134 million dollars. Also, a 50 percent chance of winning the question of how an outage is defined had a $55 million dollar expected value. We've received very little discovery and very few documents from GREC. Based on their patterns as written above, there is a good chance there are some incendiary documents we have not seen. Why would they not have sent them yet, unless there is something they don't want us to see?

An interview question I often ask to prospective employees illustrates this point. I ask, "Assume you own a company with 300 employees and an opportunity presents itself that has a 90% chance of doubling your net profits from 5 million to 10 million dollars for the year. It has a 5% chance of making some money or losing some money of little consequence, and a 5% chance of bankrupting the company. Would you take that opportunity?" The answer I look for is no for two reasons, there is a real chance you could go bankrupt and all of your employees would lose their jobs and you would lose a venture you've taken years to develop, all on one bet. Two, it creates a pattern of betting everything and when you do that often, eventually you lose everything even if the odds of success on any single one bet are high. GREC does not want to lose everything.

These risks have not been put into consideration in the $750 million dollar offer price. Commissioner Hayes-Santos mentioned that the City of Gainesville would be playing roulette if we didn't take the deal. Our worst outcome is the status quo. Their worst outcome is not just roulette but Russian roulette. They metaphorically die.

By my back of the envelope calculations, nearly a third of the savings to county residents will be eaten away because costs will shift from the fuel adjustment charge to regular charges, which is subject to the 10 percent surcharge tax. So an 8-10 percent savings turns into a 6-8 percent savings for county residents.

The easiest choice would be to accept the $750 million dollar MOU and put this behind us. Many are advocating this position, but the easiest choices aren't always the best choices, and in this case I firmly believe we'd be making another colossal blunder. The road I'm advocating will be painful in the short term. It will require resolve, a commodity in short quantity in today's world. It will require you to trust the cold hard analysis and displace the passions of retribution or the sin of complacency through acceptance. They are counting on the latter.

With this in mind, I advocate signing the MOU at $675 million. We write the first contract. We once again ask that all savings be transferred to the customer. In addition, let's put a 30-day time limit on this MOU and send it signed whether they reject it tomorrow or not. In the meantime, we should not stop arbitration.