UTILITY COMMITTEE

The Utility Committee Meeting was held on June 22, 2015 at 5:20 p.m. with Chairman Hutchison presiding. Members present were Mr. Cole, Mr. Neil, and Mr. Blakeman. Ms. Stewart was absent. Members of Council present were Mr. Anderson (arrived at 5:29 p.m.), Mr. Sudler (departed at 5:21 p.m.), Mr. Hosfelt (departed at 5:22 p.m., returned at 5:33 p.m., departed at 5:35 p.m.), Mr. Hare (arrived at 5:32 p.m., departed at 5:40 p.m., returned at 5:56 p.m.), and Mr. Slavin (departed at 5:32 p.m.). Mayor Christiansen was also present (arrived at 5:34 p.m.).

AGENDA ADDITIONS/DELETIONS

Mr. Neil moved for approval of the agenda, seconded by Mr. Blakeman and unanimously carried.

HOUSE BILL NO. 171 AMENDING TITLES 9 AND 22 OF THE DELAWARE CODE RELATING TO TAXES ON SPECIAL BETTERMENTS

Members were advised that House Bill No. 171 establishes a Telecommunications Tax Modernization Review Group to study and make recommendations for establishing a future funding mechanism to replace the property tax on telecommunications equipment and addressing the projected decrease in revenue to the counties, municipalities and school districts from the transition to new technologies throughout the State. The resulting mechanism should be revenue-neutral to the localities and competitively neutral to providers of like services. To encourage investment in broadband infrastructure, this bill also caps the amount of tax on telecommunications equipment at FY15 rates and eliminates the tax as of June 30, 2018.

Mrs. Donna Mitchell, Controller/Treasurer, advised members that a proposed revision for House Bill House Bill 171 ***(Attachment #1)***. Mrs. Mitchell stated that the revised bill eliminates the provisions of the original bill establishing the Tax Modernization Review Group and eliminates the repeal of the tax as of June 30, 2018. To encourage investment in broadband infrastructure, it retains the cap on the amount of tax on telecommunications equipment at 2015 levels, and clarifies that the cap only applies with respect to communication providers that are currently subject to the tax and specifies that the limitations on county and municipal taxation will apply as well to school districts and Business Improvement Districts. At the present time this tax is paid only by landline telecommunication providers and not cable companies.

Mrs. Mitchell explained that she served with former Representative Darryl Scott on a related committee several years ago and that those in the telecommunication industry felt that they were being taxed unfairly on the betterments tax versus other providers. The committee was to look at different alternatives, but when Rep. Scott did not run again, this did not occur. The proposed amendments aimed for consistency among all providers of telecommunications equipment. Mrs. Mitchell stated her understanding that the current proposal was to work with each community to try to obtain consistency.

In response to Councilman Hutchison, Mrs. Mitchell confirmed that the General Assembly would be voting on the amendment on June 23, 2015. She indicated that she agreed with the proposed amendment but not the bill as originally written, and this is what she relayed to the parties that were involved in this.

Responding to Mr. Neil, Mrs. Mitchell stated that she did not believe the bill would pass during the current session, stating that there did not seem to be enough support for it.

OVERVIEW OF CITY UTILITIES

At the request of Chairman Hutchison and for the benefit of new members of Council, Mr. Scott Koenig, City Manager, provided a brief overview of the various utilities that the City of Dover provides to its residents and customers. Mr. Koenig stated that the City's power system had its 100th anniversary within the last few years and the water system dated back to roughly 1882; therefore, the City had been in the public utility business for many years, which had been a benefit to the City and its customers. *[City Clerk's Office Note: Subsequently during the meeting, Mr. Blakeman advised members that the City's electric utility came online and began generating power on January 1, 1900, and received a 100-year award from the American Power Association in 2000; therefore, the utility had been generating power for the City of Dover for 115 years.]*

Mr. Koenig explained that the City of Dover was granted a Certificate of Public Convenience and Necessity by the State of Delaware to provide electric services in a service territory. The City of Dover proper consists of approximately 24 square miles, and the City's electric territory is approximately 74 square miles, which extends to Little Creek, Port Mahon, down into Kitt's Hummock, which includes the Dover Air Force Base and areas south of Route 10, and then comes up and intertwines with the City limits. On the north side, the territory is in line with City limits. Mr. Koenig informed members that when property is annexed into the City, there is usually a letter of agreement where the franchise providing service prior to the annexation is transferred to the City's electric system. He noted that no financial transaction takes.

Mr. Koenig advised members that the City of Dover built a power plant in the 1960s at McKee Run which included two (2) 17 MW units called Unit 1 and Unit 2. In the early 1970s, Unit 3 was added, which is roughly 103 MW, and in approximately 1990, the VanSant combustion turbine was added. Mr. Koenig stated that at that point the City was producing power for the demands of its service territory; however, over the last two and a half decades the City had gravitated toward being part of a regional power supply grid called the PJM system. The City is no longer a primary producer of power but produces power when called upon by the grid. He indicated that the City's generation capacity is approximately 170 MW.

Mr. Koenig explained that Council voted to retire Units 1 and 2, consisting of 34 MW of power, in Power Year 2018 for budgetary reasons. Council had considered replacing those units with either a purchase power agreement or new units that would offer Dover power generation well into the future. Related discussions had been ongoing for approximately four (4) years, and Mr. Koenig stated that it was hoped that staff would be bringing agreements regarding power supply forward to Council for consideration.

Mr. Koenig stated that the Calpine Corporation had come before Council to obtain authorization for a 618 MW facility for two (2) units, the first of which was for the Garrison Energy Center, which became commercially available on June 1, 2015, began producing power to the grid, and became the City's largest water customer overnight. Prior to the unit coming onto the grid, the thought was that once it did, Dover would not be called upon to generate power; however, that had not been the case.

Mr. Koenig reiterated that power generation is a very fluid and complicated environment, making it difficult to determine when Dover will be called upon to produce power. He stated that there are many producers inside the grid, but some are being retired and coming offline because they are old coal technology. Mr. Koenig stated that the call for who runs and who does not changes on a daily basis. When nuclear power plants are offline for maintenance, many more facilities are called up than when these plants are online and available. Mr. Koenig advised members that there had been some difficulty with gas supply in the last couple of weeks, and he hoped to find out more about that issue in meetings with The Energy Authority and Eastern Shore Natural Gas. He referenced to inconsistences with gas transmission and expressed his belief that this was due to the heavy demand of the new Calpine facility.

Mr. Koenig indicated that the Electric Fund is tagged at roughly $89M of revenue in this year's budget, and this money is used to cover the cost to purchase power from the system as well as the capital plan, which includes vehicle purchases, equipment purchases, line replacements, substation upgrades and/or replacements, and replacement of both large and small transformers. This revenue also supports needs related to facilities and infrastructure and a transfer from the Electric Fund to the General Fund. In the FY 16 budget, approximately $10.85M will transfer from public utilities directly into the General Fund, $10M from the Electric Fund and $850,000 from the Water/Wastewater Fund.

Regarding the electric utility, Mr. Koenig stated that the City serves approximately 23,000 customers, ranging from single-family houses all the way up to the Dover Air Force Base. A cost of service study was performed to properly allocate costs and identify what the rates should be for each class of customer. Mr. Koenig noted that the City of Dover residential electric rates are the lowest in the State of Delaware but the commercial rates are not the lowest.

Mr. Koenig stated that the water and sewer system service territory is not quite as big as the electric service system. He noted that the City serves areas outside its corporate limits and has interconnection agreements with Tidewater Utilities, who purchases water from the City in the northwest portion of the City and supplies subdivisions northwest of the City. In addition, Tidewater purchases water from Dover through the Lakeland interconnection for the Lakeland Mobile Home Park and businesses on South State Street. Mr. Koenig stated that the City's relationship with Tidewater over the last decade had been very good, noting that Tidewater has four (4) of Dover's top 20 meters.

Mr. Koenig explained that the water and sewer systems are accounted for separately to ensure that the cost of water is covered by the water charge and the cost of sewer by the sewer charge; however, these funds are intermingled in a water and sewer enterprise fund. Total revenues expected in FY16 were $19.3M, including new revenue projected from the Calpine facility. Mr. Koenig advised that originally, the water system revenue was estimated to be about $1.6M and the sewer system in the $300,000 range. He indicated that the water system consists of approximately 14,000 to 15,000 meters, requiring a lot of manpower for care and maintenance. Water quality complaints were expected when Calpine came online but not many complaints were received. It was hoped that water quality would improve since water would be moving quickly through the system on that part of the City due to Calpine's demand.

Mr. Koenig stated that improvements were proposed over the long term for the water system, including potentially developing another aquifer, noting that if this will be necessary if Calpine builds a second generating unit. He indicated that the City has a 1.5M gallon water tower under construction presently at the Garrison Oak Technology Park, which is the City's largest tower by about 50 percent and another 1M gallon tower was scheduled to be built in the north middle quadrant of the City pending final resolution on a site. This would offset fire demands and provide additional elevated storage for supply. Additional improvements will be made to the system through pipe replacements.

Mr. Koenig advised members that staff expected to return to Council to review rates, explaining that efficiency had affected the City's water utilities. Plumbing codes had changed, and low-flow fixtures and low-flush toilets had significantly reduced household water usage. In the 1980s, a generic house used 300 gallons of water per day, and now a generic house uses 250 gallons per day, a drop of 50 gallons per day, which was a significant change when multiplied by 8,000 to 10,000 households.

Mr. Koenig stated other changes also affect the water/wastewater utility. In the early 1990s, Proctor & Gamble expanded their paper-making process, which put a significant demand on the water system of approximately 600,000 gallons a day. However, in the last 10 years, they had stopped making that product at that location and water demand decreased by 600,000 gallons per day. He indicated that it is difficult to make up for these types of fluctuations in production and revenue. On the electric side, Mr. Koenig informed members that a push for more efficient air conditioning systems was affecting the electric utility. It was expected that electric load, even with growth, may be relatively flat over the next few years due to the implementation of systems using less power. He indicated that these are the types of variables used to set rates, determine how to recover fixed costs, develop revenue projections for future budgets, and review revenues for current budgets.

In regard to the sewer utility, Mr. Koenig stated that in the early 1970s, the City built a sewage treatment plant at the old PW2 warehouse location at the end of Water Street, which came online in about 1971. The plant was in operation for only a couple of years when the City transferred all of its waste to Kent County. Mr. Koenig expressed his opinion that the City was very fortunate to be with the County system because it is not necessary to do any of the related permitting or worry about the actual treatment of waste water coming out of of Dover. All flow from the City of Dover is sent to the County by contract and they have an obligation, under their Environmental Protection Agency (EPA) permit and Division of Natural Resources and Environmental Control (DNREC) permits, to treat the City's waste and deliver it to the Murderkill River in a state that is equal to or better than drinking water quality. Mr. Koenig indicated that the City was benefitting today from not having to run its wastewater treatment plant.

In terms of infrastructure, Mr. Koenig stated Dover has approximately 40 pump stations, which vary from small stations serving eight (8) to 10 houses, to large pump stations like the Puncheon Run station that serves industrial flow coming out of Kraft and Procter & Gamble. Mr. Koenig pointed out that it is critical that those stations work, noting that Dover had gone through replacement and renewals on the wastewater side, and backup generation was being constructed at those facilities

because the potential for overflows into streams and rivers or onto the ground would be significant if the power goes out. Mr. Koenig stated he is grateful that Dover has such a reliable system with very few system-wide outages, noting the impact a power outage can have, such as sewage backing up in people's homes.

Mr. Koenig pointed out that owning its own utilities places the City in a good position to attract businesses; however, it require a lot of hours and manpower to run those enterprises. Because of the enterprise funds, the City recovers at least the cost associated with running them, and the intent of Dover's public utilities is to return money to the General Fund as internal profit for going through the pain of having to run the utilities, noting that they are 24/7 operations that require a lot of manpower, capital, and time from the Mayor, Council, and staff to keep systems functioning. He expressed his opinion that the City is in much better shape through owning the utilities as it can better control its own destiny.

In response to Mr. Neil regarding the cost to buy power if the City were not a generator, Mr. Koenig explained that the City's power plant and combustion turbine act as a physical hedge for the City, which provides leverage in buying power. It was his belief that Mr. Harry Maloney, Electric Director, may have estimated this cost at roughly $2M. With no ability to generate, the City would be completely at the risk of the market sale price. Because the City has its own generation, the market stops at the City's cost to produce into the market. Even though this cost can be relatively high in some cases, it is much less than if the City were at risk in the market. He noted that during really cold days this past winter, the per megawatt hour cost exceeded $1,000, $1,500, or $1,800 per hour; therefore, having generation gave an actual physical hedge that provided leverage in buying in the market.

Responding to Mr. Neil regarding whether a deal had been attained with Calpine, Mr. Koenig advised that the City did not have a deal worked out with Calpine on paper at this time. He stated that some regulation issues are being discussed with the EPA that have a significant impact on the products and prices that would be offered in the marketplace. Although the framework was in place, no one was willing to strike a price until those issues are resolved. Mr. Koenig stated that once they are resolved, staff would come before Council with a proposed agreement.

Responding to Mr. Anderson regarding the City's industrial rates, Mr. Koenig advised that commercial and industrial rates are grouped together and the City's rates rank in the middle to upper end.

TEA/NAES REPORTS (*MARCH AND APRIL*)

The TEA/NAES Monthly Reports for March and April 2015 were provided to members to enable them to monitor electric sales and revenues received, which will provide a better understanding of any fluctuations that occur and allow the opportunity to make improvements if deemed necessary.

Mr. Blakeman expressed his preference for having actual PJM invoices included in the TEA/NAES reports versus the format used in the April report. In response to Mr. Blakeman, Mr. Koenig stated that would contact TEA/NAES to make this request.

DISCUSSION ITEM PROPOSED DURING THE FY 2015/16 BUDGET REVIEW

Cost-Benefit Analysis of Power Plant Operation

Mr. Scott Koenig. City Manager, stated that a motion was made during the FY 2015/16 budget review that the City consider performing a cost/benefit analysis of its power plant operation. Mr. Koenig stated that in the five (5) year forecast, the power plant was slightly negative in cash during one (1) year but positive in all other years. Mr. Koenig noted that a one (1) year cost/benefit analysis would not be beneficial since a decision could not be made based on a return of one (1) year and stated the need to define the timeline of the analysis. He stated that, without question, owning the physical plant and having the ability to contract its operation and oversee its contracts would be the right thing to do for the benefit of customers. Mr. Koenig felt that reviewing it on an annualized basis would provide only a snapshot, whereas a profile over years showed it had been a benefit to the City and would continue to be in the foreseeable future.

Responding to Mr. Blakeman regarding the life expectancy of Unit 3, Mr. Koenig stated that Mr. Harry Maloney, Electric Director, estimated there would be approximately 10 years before there were concerns regarding its life expectancy. When discussing the life expectancy of Units 1 and 2, North American Energy Services (NAES) engineers had indicated that the units could last as long as desired, depending on what the City wanted to put into them. Mr. Koenig indicated that the projected life expectancy of the turbine was roughly 50 years. He advised members that the City was doing everything it could to get it to 50 years, and when closing in on this time frame, would make decisions on whether to maintain or replace that unit. Mr. Koenig stated that replacement would cost roughly $1M per MW; therefore, replacing it would be more than a $120M expense.

Mr. Blakeman questioned if decreased prices due to the impact of older coal-fired generation units being replaced with gas turbines had been a concern when considering the life expectancy of this unit. He felt that it may be priced out of the market and not be called to run. Responding, Mr. Koenig stated that this was a concern; however, The Energy Authority (TEA) does a good job of looking at those numbers on an annualized basis. He reiterated that in spite of initial concerns that Dover would not be called upon once Calpine was on board, that had not been the case, but could potentially be in the future.

Mr. Blakeman stated his opinion that Calpine may be asking to put in a second unit a year from now. Mr. Koenig concurred that this was a possibility.

Responding to Mr. Hutchison regarding the projected cost associated with keeping Units 1 and 2 running, Mr. Koenig stated that the consensus was that it would be more cost effective to the City to build new generation versus maintaining the current units or to execute a purchase power agreement.

Mr. Neil moved to defer Item #5, Updates, to the July 13, 2015 Utility Committee Meeting. The motion was seconded by Mr. Blakeman and unanimously carried.

By unanimous consent, the meeting adjourned at 5:58 p.m.

James Hutchison, Sr.
Chairman

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Attachments
Attachment #1 - House Substitute No. 2 for House Bill No. 171

SPONSOR: Rep. Bennett & Sen. Hall-Long & Sen. McDowell
Reps. Hudson, Q. Johnson, Keeley, Longhurst, Schwartzkopf, M. Smith, Viola; Sens. Blevins, Lavelle, Poore, Simpson

HOUSE OF REPRESENTATIVES
148th GENERAL ASSEMBLY

HOUSE SUBSTITUTE NO. 2

FOR

HOUSE BILL NO. 171

AN ACT AMENDING TITLES 9 AND 22 OF THE DELAWARE CODE RELATING TO TAXES ON SPECIAL BETTERMENTS.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF DELAWARE:

Section 1. Amend § 8101(e)(8), Title 9 of the Delaware Code, by making deletions as shown by strike through and insertions as shown by underline as follows:

§ 8101. Property subject to county taxation.

(e) Special betterments, whether or not also considered to be improvements, shall include and be limited to the following:

(8) Poles, wires, cable and conduit for distribution of telephone communication services either above or below ground; <u>provided, however, that in no event shall the amount of tax imposed on communications providers that were paying tax on such property as of June 30, 2015, exceed the amount actually paid by such provider to each political subdivision in the fiscal year ending June 30, 2015;</u>

Section 2. Amend §2001, Title 22 of the Delaware Code, by making deletions as shown by strike through and insertions as shown by underline as follows:

§ 2001 Limitation of municipal taxing powers.

(a) Every municipal corporation in this State, regardless of population, shall only have the power to impose, levy, assess, or collect a tax of any kind whatsoever as expressly authorized in its municipal charter or this title.

(b) Any provision in a municipal charter granting the municipal corporation "all powers," or any derivation thereof, shall not be construed as exempting the municipal corporation from the limitation set forth in subsection (a) of this section.

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(c) The amount of tax imposed on a communication provider who was being taxed as of June 30, 2015, by municipal corporations on poles, wires, conduit and cable for distribution of telephone communication may not exceed the amount of tax actually paid by such provider to each municipal corporation in fiscal year ending June 30, 2015.

Section 3. The restrictions imposed on the counties' and municipalities' taxation of poles, wires, cables and conduit for distribution of telephone communication services in Sections 1 and 2 above shall also apply to school districts and Business Improvement Districts.

SYNOPSIS

This substitute bill eliminates the provisions of the original bill establishing the Tax Modernization Review Group and eliminates the repeal of the tax as of June 30, 2018. To encourage investment in broadband infrastructure, it retains the cap on the amount of tax on telecommunications equipment at 2015 levels, and clarifies that the cap only applies with respect to communication providers that are currently subject to the tax and specifies that the limitations on county and municipal taxation will apply as well to school districts and Business Improvement Districts. At the present time this tax is paid only by landline telecommunication providers and not cable companies.