

EU Case Study ~ Privatizing Utilities

Thursday

Background:

The Utilities enterprise at a large public university is a self-sustaining unit funded by billing each building for steam, electricity, and water. Utilities maintains excellent safety, reliability, and service to the campus. Thanks to careful fuel management and other operational decisions, major billing rate changes have been avoided over the years. However, the addition of several large new buildings is straining capacity and aging infrastructure requires major renewal projects. Additionally, the state has reduced its financial support to higher education due to budget shortfalls.

The Utilities group has aggressively pursued renewal energy goals and have committed to eliminate the purchase of coal sourced electric within ten years. Additionally, carbon emissions have been reduced by almost 20% in the last year. While the renewable energy sources are currently more expensive coal, it is anticipated that, in the long term, costs will reduce. These initiatives are popular with students and the community.

Situation:

The university is weighing an offer from ACME Electric to purchase its Utilities enterprise. ACME Electric is a large for-profit utility that has completed similar utility purchases at two other universities within the last five years. Under the terms of the proposed deal, AMCE would pay a large upfront fee where they would own, operate, and maintain all energy infrastructure. This infrastructure includes a large, combined heat and power plant, distribution lines, and chiller plants. The proposed contract will be for 25 years and at the end of the term AMCE Electric may elect to extend the term or sell the assets back to the university for a nominal fee. The initial purchase would result in a generous endowment that could fund multiple significant academic programs.

All current Utility employees would be offered a position at their current salary, but it may not be their current position. ACME Electric's benefit package is less generous than the university's, but stock options will be available.

ACME Electric will have the ability to determine billing rates to the campus, how to operate the plants, and what fuels to use. The university negotiated a cap on rate increase at 6% per year, which is higher than historically charged increases. There have been no service complaints regarding AMCE Electric at the other two universities, but rate increases have all been the maximum allowed by the contract.

Your team is part of the evaluation committee, representing Facilities:

1. What factors should influence the university's decision on privatization?
2. From the Facilities Management's perspective, what are the pros and cons?
3. Identify the internal and external stakeholders and who would be impacted. How would you involve them in the decision?
4. What short-term and long-term risk do you see with privatization?
5. What risk mitigations would you recommend?
6. What else should be considered?