

LAZARD

April 4, 2018

Lisa Atkins
CAWCD Board President
PO Box 43020
Phoenix, AZ 85080-3020

Dear Ms. Atkins:

RE: Navajo Generating Station

As described in the letter dated February 1, 2018, Lazard has been engaged by Peabody, with the support of several key stakeholders, to facilitate ownership transition alternatives for the Navajo Generating Station (“NGS”) that would enable the plant to remain in long-term operation.

This process, which began in 2017, was initiated to transfer ownership in NGS to new owners that would continue plant operation beyond 2019. As previously described, interest in NGS has primarily come from well-respected financial investors with strong track records in the power generation sector, all of which understand that NGS will need to be competitive with the current power price environment in order to operate post-2019. As part of the process to transfer ownership in NGS, Lazard received interest from over 15 highly reputable and experienced private equity firms and power plant operators.

There are a number of favorable factors influencing an interest in NGS. First, based on a provision in the EPA rule relating to NGS (i.e., Alternative “B”), a sale of the power plant will allow the new owner to forego almost \$500 million worth of capital expenditures that current owners would be required to spend. Additionally, the Kayenta Mine can efficiently adjust its mine plan to reduce input costs, offering NGS a more competitive position with natural gas. Finally, the highly reputable and experienced private equity firms and power plant operators who expressed interest in NGS believe the power plant can operate more efficiently from a fixed cost basis, further increasing the competitiveness of NGS with natural gas and other generation sources.

Over the course of the past two months, Lazard, alongside a highly reputable and experienced potential new owner (the “Potential Investor”), has performed a significant amount of work in finding a solution for NGS that would allow the plant to supply power at market competitive prices. This has included a visit to Phoenix, Page and Kayenta between March 12 – 14, a subsequent visit to Phoenix and Tucson on April 2 – 3 (including a meeting with Ted Cooke and Tom McCann) and countless hours of operational due diligence and discussions with key stakeholders since February.

Based on their findings to date, the Potential Investor can deliver power at prices cheaper than what was recently received from third parties during the CAWCD’s baseload RFP process. Our question, to you and the Board of CAWCD, is why would CAWCD decide to pursue more expensive power options when an existing resource (i.e., NGS) can deliver cheaper power?

In addition to the power-cost comparison, CAWCD has a debt obligation of over \$1 billion to the federal government and the U.S. taxpayer for the construction of CAP infrastructure, including NGS. Continued

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operation of NGS provides a mechanism to help repay that debt; however, the early retirement of NGS triggers decommissioning and reclamation costs of \$110 – \$150 million.

The ownership transition process remains on track with the timeframe outlined by operating agent Salt River Project, who has agreed to help facilitate an ownership transition subject to negotiation of definitive agreements. Given the significant complexities surrounding NGS, we believe that selecting a highly credible and experienced potential investor to perform detailed diligence and engage with key stakeholders would result in the highest probability of success. Therefore, over the past couple of months, Lazard has engaged the “Potential Investor to perform detailed due diligence of NGS. In addition to the Potential Investor, there are several interested counterparties that are currently on the “sidelines”, awaiting direction from Lazard on next steps.

It is our view that NGS will be sold and the plant will run well beyond 2019.

As described above, the Potential Investor has devoted significant time and resources in evaluating the viability of operating NGS post-2019 over the past couple of months. This has included conducting preliminary on-site diligence of NGS and the Kayenta Mine, engaging with the Navajo Nation and Hopi Tribe and beginning preliminary discussions with the current owners on ownership transition and power purchase agreements (including representatives at CAWCD), among other efforts. Based on these preliminary discussions and diligence efforts to date, the Potential Investor believes there is a significant opportunity to supply power to the current owners and the CAWCD at market competitive prices, allowing NGS to operate post-2019.

It is our understanding that CAWCD has a legal obligation to procure its power requirements from NGS if the plant remains open. In addition, based on publicly available information, it appears that the current CAWCD RFP process resulted in baseload power supply proposals at levels that are higher than the price at which the Potential Investor and Lazard believe NGS could supply CAWCD, therefore exposing CAWCD to significant merchant power price volatility (i.e., 40% - 60% of baseload energy needs). CAWCD should avoid entering into any additional contracts to purchase power that precludes it from fulfilling its obligation to take power from NGS.

Based on the current diligence efforts conducted by the Potential Investor and the significant potential cost savings in electricity that can be generated by a new owner for the reasons noted above, we believe it is your fiduciary obligation to pause the RFP process for a short period of time to determine if the plant will continue to operate and if it can deliver power at a more stable and lower cost than is currently offered under the RFP process. If you have any questions regarding this information, please contact me at 312-407-6673.

Sincerely,



George W. Bilic
Vice Chairman of Investment Banking
Global Head of Power, Energy & Infrastructure
Head of Midwest Investment Banking

CC: Members of the CAWCD Board

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The Honorable LoRenzo Bates, Speaker Navajo Nation
The Honorable Timothy L. Nuvangyaoma, Chairman HOPI Tribal Council
The Honorable Stephen Roe Lewis, Governor Gila River Indian Community

OVERVIEW OF LAZARD

Lazard, one of the world's preeminent financial advisory and asset management firms, operates from 43 cities across 27 countries in North America, Europe, Asia, Australia, Central and South America. With origins dating to 1848, the firm provides advice on mergers and acquisitions, strategic matters, restructuring and capital structure, capital raising and corporate finance, as well as asset management services to corporations, partnerships, institutions, governments and individuals.

Lazard's commitment to the Global Power, Energy & Infrastructure Industry is of the highest priority. In that regard, we believe that we have the greatest allocation of resources and effort among any investment bank. Further, we have an ongoing and intense focus on strategic issues that require long-term commitment and planning.

Selected Recent Transactions in the Power, Energy & Infrastructure Industry

- Advisor to Sempra on its pending acquisition of EFH's 80% ownership interest in Oncor
- Advisor to Calpine on its pending sale to Energy Capital Partners
- Advisor to FirstEnergy Solutions on its ongoing strategic review
- Advisor to Great Plains on its pending merger with Westar
- Advisor to WGL on its pending sale to AltaGas
- Advisor to Invenergy on the capital raise for Lackawanna Energy Center
- Advisor to Dynegy on its restructuring of Illinois Power Generating Company (Genco)
- Advisor to BlackRock on its take private of Gas Natural
- Advisor to the Special Committee of the Board of Directors of SolarCity on its sale to Tesla
- Advisor to the Official Committee of Unsecured Creditors in the Chapter 11 cases of SunEdison
- Advisor to China Three Gorges on the acquisition of wind portfolios in Poland and Italy from EDP
- Advisor to Clean Line Energy Partners on a range of strategic advisory matters
- Advisor to Columbia Pipeline Group on its sale to TransCanada
- Advisor to Dynegy on its acquisition of Engie's U.S. fossil portfolio
- Advisor to SDIC Power on its acquisition of Repsol's UK wind assets
- Advisor to the Board of ITC Holdings on its sale to Fortis
- Advisor to Enel Green Power on its integration into Enel
- Advisor to Williams on its proposed combination with Energy Transfer Equity (terminated)
- Advisor to TerraForm Power on its proposed acquisition of the operating assets of Vivint Solar (terminated)
- Advisor to Iberdrola on the merger of Iberdrola USA and UIL and the formation of AVANGRID
- Advisor to TerraForm Power on its acquisition of the operating assets of First Wind
- Advisor to NiSource on the spin-off of Columbia Pipeline Group and formation of an MLP
- Advisor to Dynegy on its acquisition of the Duke Ohio and EquiPower generation portfolios
- Advisor to Integrys on its sale of Integrys Energy Services to Exelon
- Advisor to Acciona on its sale of one-third of its renewable generation business to KKR
- Advisor to Integrys on its sale to Wisconsin Energy
- Advisor to the Unsecured Creditors' Committee of Energy Future Holdings
- Advisor to Pepco on its sale to Exelon
- Much more significantly, Lazard continues to advise a large number of Industry participants on ongoing strategic and ordinary course matters on a strictly confidential basis