

**Written Testimony of
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**Before the House of Representatives Natural Resource Committee
Hearing on the “Rebuilding and Privatization of the Puerto Rico Electric Power Authority (PREPA)”
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Chairman Grijalva and members of the committee, thank you for the invitation to testify today. I am the director of finance for the Institute for Energy Economics and Financial Analysis (IEEFA). IEEFA has been closely following and analyzing Puerto Rico electrical system issues since 2015. Our publications have focused on the physical and financial condition of the Puerto Rico Electric Power Authority (PREPA): specifically pre- and post-hurricane energy planning and priorities; debt management; consultant hiring and fee structures; renewable energy opportunities; management challenges; political interference; budget and fiscal plan; federal oversight; fuel oil contracting; and other procurement issues and irregularities. My opinions and that of my coauthor on many pieces in Puerto Rico, Cathy Kunkel, have been cited in The Bond Buyer, The Hill, El Nuevo Día, El Vocero, Caribbean Business News, Fortune, Vox, The Intercept, USA Today, and Inside Climate News.

Prior to my tenure at IEEFA, I spent 17 years at senior management levels at the New York City and New York State Comptroller’s Offices. I left state service in 2007 as the First Deputy Comptroller of New York State (and served for a short period as the State Comptroller due to an early resignation). In those positions, I had responsibility for the oversight of a \$150 billion pension fund; a 1 million member retirement system; a \$250 billion state and local bond portfolio; 40,000 annual contracts valued at \$85 billion; the audit program for all public authorities (including the state’s largest energy authorities, the Long Island Power Authority and the New York State Power Authority) and state and local governments; monitoring of the state budget and expenditures (including payrolls); and review of the finances of 1,400 units of local government. My work on state government finances has appeared in the New York State Oxford Handbook on Politics and Government.

Part of my responsibilities concerned the problem of local government fiscal distress. The New York City Comptroller is a member of the New York State Financial Control Board and monitors the New York City government budget. During my tenure, the New York State Comptroller had statutory obligations for existing control boards in New York City and Yonkers (including Yonkers’ exit from oversight). The office initiated new control boards in Troy, Nassau County, Erie County and Buffalo. As part of the Comptroller’s Executive leadership team, I had direct responsibility for most of these initiatives.

I have also served on the advisory board of the Long Island Power Authority, the New York electric utility whose privatization has often been cited as model for PREPA.

I am here today to testify on the current effort to privatize PREPA, which, based on IEEFA’s research, is unlikely to achieve the island’s policy goals of affordable electric rates and a more resilient and reliable power system.

Transformation or business as usual?

The privatization of PREPA was authorized by the passage of Puerto Rico Law 120-2018 in June 2018. Law 120 establishes a process for a series of contracts through which PREPA's electrical transmission and distribution system will be leased to a private third party via long-term concession; PREPA's existing power plants will be sold or retired, and electricity will be purchased from private generators via long-term contracts; and other aspects of PREPA's operations (customer service, for example) could be outsourced.

This process is moving forward. The Puerto Rico Public Private Partnerships Authority (P3 Authority) issued a request for qualifications for a battery energy storage project and for the transmission and distribution concession.¹ Four companies have been prequalified for the concession.²

Yet, to speak of this process as a transformation of PREPA is a misnomer. PREPA today is publicly-owned in name only. A pre-hurricane budget for PREPA showed almost seventy percent of the rate dollar paid by Puerto Rico's households and businesses going towards debt service and imported fuel.³ In other words, private investors and fuel companies have been the principal beneficiaries of PREPA's budget. While a small portion of the investor dollars have gone to on-island investors, the overwhelming share of investment repayment has gone off-island. For more than a decade, PREPA has been operated in a manner to benefit the interests of fuel suppliers, bondholders and other private interests via lucrative and poorly-managed contracts, at the expense of the people of Puerto Rico, as I will explain in detail below.

The current privatization process is designed in a way that will only make this problem worse. The process provides limited opportunity for input from Puerto Rico's energy regulator, the Puerto Rico Energy Bureau. IEEFA has requested information from PREPA, under Puerto Rican access to information laws, regarding how it arrived at some of its proposed privatization projects (including multiple proposed natural gas projects) and received no response. The process allows for privatization contracts to be exempt from Puerto Rico's long-term energy plan.

The privatization plan lacks the transparency and stringent contract monitoring and oversight requirements that would be needed to instill confidence in this process. Puerto Rico law gives the P3 Authority, PREPA and the Puerto Rico Fiscal Agency and Financial Advisory Authority the responsibility to "oversee the performance and compliance of the Contractor," but does not define this responsibility beyond the production of annual reports to the Governor and Legislature on contract compliance.⁴ It is also unclear how the enforcement responsibility would be split among the three agencies. For a contract relating to the provision of electricity, this means that agencies without any mandate to protect the electricity grid and the people it serves will have the right to an ongoing role in the interpretation and

¹ Puerto Rico Public Private Partnerships Authority, "RFQ: Puerto Rico Electric Power Transmission and Distribution System", Issued October 31, 2018 and "RFQ for the Puerto Rico Electric Power Authority Utility Scale Energy Storage System Project" issued June 22, 2018. Available at: <http://www.p3.pr.gov/assets/p3a-rfq-2018-2-td-system-project.pdf> and <http://www.p3.pr.gov/assets/rfq-energy-project-june-2018.pdf>

² "Cualifican a cuatro proponentes para operar el día a día en la AEE," El Nuevo Día, January 17, 2019.

³ Puerto Rico Electric Power Authority, [Monthly Report to the Governing Board](#), June 2015.

⁴ Law 29-2009, Section 10(d). The P3 Authority's "Regulation for Procurement, Evaluation, Selection, Negotiation, and Award of Partnership Contracts and Sale Contracts for the Transformation of the Electric System under Act No. 120-2018, as amended" (March 8, 2019) adds a requirement of quarterly reporting from PREPA, but does not offer additional clarity on contract enforcement.

adjustment of these contracts. The result is a process with ample opportunity for politically-driven contract awards and inappropriate interference in the ongoing relationship with the contractor. While the “privatization” of PREPA under Law 120 has been touted as a means of depoliticizing Puerto Rico’s electrical system, it is highly doubtful that the process—which guts the idea of a rationally planned electrical system in favor of a piecemeal series of contracts—will achieve this stated goal. The management of the generation, transmission and distribution system by private entities will do little to depoliticize the system if the contracts themselves are entered into via a non-transparent, politically driven process, as Law 120 facilitates.

It appears that few lessons have been learned from PREPA’s past history of contracting failures, which have contributed to the authority’s financial ruin. This history includes:

- In a fuel contracting scandal, PREPA paid full price to oil suppliers for sub-quality oil for well over a decade.⁵ Laboratory testing results were falsified to determine that sub-standard oil met PREPA’s fuel quality specifications, and internal audits were suppressed. PREPA spent \$23 billion on fuel—almost entirely oil—from 2002 to 2014, at times incurring debt to cover the costs of its outsized fuel budget. Lawyers for a class action lawsuit brought by PREPA ratepayers estimate that over this period, the fraud cost customers more than \$1 billion, or nearly 5% of the total fuel budget.⁶

While this scandal was occurring, PREPA failed to meaningfully diversify into renewable energy, despite a legal mandate to do so. As of 2015, 1.4% of PREPA’s electricity came from renewable energy sources,⁷ in flagrant violation of the island’s renewable portfolio standard of 12%. The few renewable energy contracts that PREPA entered into with private developers were significantly overpriced.⁸

The scandal is not a secret. A Puerto Rico Senate investigative committee published a report in 2016, Puerto Rico’s Comptroller completed an audit in 2002, a New York Times article covered the scandal, ratepayers are in court on a class action suit, and a referral was made to the FBI.⁹ Yet no corrective action plan has been publicly identified or adopted by PREPA or the governor. It is entirely possible that PREPA continues to over-pay for oil today.

- PREPA borrowed nearly \$11 billion from 2001 to 2013 and currently has approximately \$9 billion in legacy debt outstanding. Despite the growing risks that should have raised red flags with creditors during this period—including declining sales, the poor condition of PREPA’s physical

⁵ Sanzillo and Kunkel, “Multi-billion dollar oil scandal goes unaddressed in PREPA contract reform and privatization,” Institute for Energy Economics and Financial Analysis, July 2018.

⁶ Hagens Berman, Puerto Rico Electric Power Authority (PREPA), <https://www.hbsslaw.com/cases/puerto-rico-electric-power-authority-prepa>.

⁷ June 2015 Monthly Report to the PREPA Governing Board, <https://aeepr.com/es-pr/investors/FinancialInformation/Monthly%20Reports/2015/June%202015.pdf>

⁸ Puerto Rico Energy Commission Case No. CEPR-AP-2015-0002, Commission Order, September 23, 2016, pp. 59-60.

⁹ Puerto Rico Senate, Special Commission for the Study of the Standards and Procedures Related to the Purchase and Use of Oil by the Puerto Rico Electric Power Authority and of Government Integrity, Final Report, December 5, 2016; Puerto Rico Office of the Comptroller, Audit Report CP-02-26, May 13, 2002; *Marrero-Rolón v. PREPA*, Civ. No. 15-1167 (JAG) (D.P.R. Feb. 24, 2015.) ECF No. 367 (“Third Amended Class Action Complaint”); M. Williams Walsh, “In scandal at Puerto Rico utility, ex-fuel buyer insists he took no bribes,” New York Times, March 2, 2016.

assets, and the practice of borrowing to pay operating expenses—PREPA was able to continue borrowing money, in part due to the services obtained from law firms, accountants, financial advisors, engineers and credit rating agencies.

The Puerto Rico Commission for the Comprehensive Audit of the Public Credit conducted a pre-audit report on PREPA's 2013 bond issuance and called into question PREPA's process for selecting auditors, potential conflicts of interest with PREPA's consulting engineer, and overly optimistic financial and operating assumptions that were endorsed by PREPA's consulting engineer and financial advisor.¹⁰ The legislature and Governor Rosselló subsequently disbanded this commission.¹¹ Similarly, an investigative report by the law firm Kobre & Kim LLP on behalf of the Financial Oversight and Management Board (FOMB) faulted underwriters for failing to monitor PREPA's actual use of proceeds from bond issuances. Kobre & Kim further detail legal avenues available for pursuing claims against the legal, financial and technical advisors involved in Puerto Rico's debt crisis.¹²

Beginning in 2014, PREPA hired a financial restructuring firm, AlixPartners, and a host of other private consultants to manage the restructuring of the authority's debt. The Puerto Rico Energy Commission (now Bureau¹³) identified several red flags with the tens of millions of dollars of contracts that PREPA has entered into with financial and legal advisors: a lack of competitive bidding,¹⁴ a complicated contracting process,¹⁵ poor monitoring of costs¹⁶ and a lack of preparedness to discipline costs.¹⁷ PREPA ultimately paid between \$36.9 and \$45 million to Alix Partners, plus tens of millions more to other financial and legal advisors, for a bond deal that was rejected by the FOMB.¹⁸ Now PREPA has a \$21.6 million contract with Filsinger Energy Partners, its new chief financial advisor.¹⁹

- In the immediate aftermath of hurricane Maria, PREPA bypassed the mutual aid resource available from mainland electric utilities to aid in the emergency reconstruction of the grid and instead awarded a contract to Whitefish Energy Holdings, a small firm that was ill-equipped to handle the needs of the Puerto Rican people during the crisis. The contractor failed, and the

¹⁰ Puerto Rico Commission for the Comprehensive Audit of the Public Credit, "Pre-audit Survey Report: Puerto Rico Electric Power Authority Power Revenue Bonds, Series 2013A", (no date).

¹¹ Luis Valentin Ortiz, "Puerto Rico government repeals commission to audit debt," Caribbean Business News, April 19, 2017.

¹² Kobre & Kim, [Final Investigative Report to the Financial Oversight and Management Board of Puerto Rico](#), August 20, 2018.

¹³ In August 2018, Governor Rosselló signed a bill that consolidated the Energy Commission with several other regulatory commissions, expanded its membership to five commissioners and renamed it the Energy Bureau. Governor Rosselló has appointed four of the five current commissioners. ("Gov signs law to establish Puerto Rico Public Service Regulatory Board reorganization," Caribbean Business News, August 13, 2018).

¹⁴ Puerto Rico Energy Bureau, [Restructuring Order](#), Case No. CEPR-AP-2016-0001, ¶ 262.

¹⁵ *Ibid.*, ¶ 260.

¹⁶ *Ibid.*, ¶ 261 and 265.

¹⁷ *Ibid.*, ¶ 271.

¹⁸ The final publicly available [contract](#) with AlixPartners on PREPA's website reports the contract amount at \$36.9 million. News reports [noted](#) the final amount at \$45 million.

¹⁹ "Third Interim Fee Application of Filsinger Energy Partners," United States District Court of Puerto Rico, No. 17-04780 (LTS), Exhibit N. According to news reports, PREPA had tried to expand Filsinger's contract to \$32.7 million, but the FOMB objected (J. Gonzalez, "La Junta de Supervisión Fiscal advierte sobre contratación en la AEE," El Nuevo Día, August 3, 2018).

contract was canceled amid the ensuing scandal. Yet the Puerto Rico Comptroller never issued its investigation into the contract, despite a promised release date of October 2018.²⁰ An investigation by the Homeland Security Inspector General has also not materialized.²¹ Nor have there been any reports on the effectiveness of a contracting reform implemented by the Governor in response to the scandal.²²

These past contracting failures show a history of poor contract management, lack of transparency in awarding of contracts, limited oversight and suppression of external reviews.

Most recently, PREPA has entered into a contract with a firm called New Fortress Energy to convert two units at the San Juan power plant to burn natural gas and to supply natural gas to the plant for five years. The project itself—reinforcing generation capacity in the San Juan area—meets a longstanding need. Puerto Rico currently generates the majority of its electricity in the sparsely-populated south and brings it to the north via long-distance transmission lines that are vulnerable to severe storms.

However, the contracting process for this project indicates that PREPA and the governor have learned few lessons from recent history. The contract was awarded outside the bounds of Puerto Rico’s energy planning process.²³ The process by which the contract was awarded to New Fortress Energy—a small, politically connected private equity company with a limited track record in the natural gas business—is shrouded in mystery, and members of the Puerto Rican business community are suing for greater transparency.²⁴ If New Fortress succeeds in selling the volume of natural gas forecasted for this single project, it will more than triple the company’s current revenue.²⁵ By contrast, competitors in the process were bond-rated businesses with a history in Puerto Rico. The main rationale for the contract is the ability for PREPA to achieve fuel cost savings to help it out of its financial morass. This topic has been treated with the utmost cynicism, with the contractor making claims to the Securities and Exchange Commission that it will save \$285 million per year and PREPA making several projections lower than

²⁰ Amanda Pérez Pintado, “La contralora no encuentra irregularidades en la contratación de Whitefish,” *El Nuevo Día*, September 22, 2018.

²¹ José Delgado Robles, “Valdivieso defends Whitefish contract,” *El Nuevo Día*, October 28, 2018.

²² In the immediate aftermath of the Whitefish controversy, Governor Rosselló issued Executive Order 2017-66. The Order established the Office of Contract Procurement and Compliance (OCPC) within PREPA. The mission of the office was to ensure that PREPA’s future procurements complied with existing local and federal law and were efficient. The Office was charged with responsibility for approval of all contracts more than \$500,000 and using “independent review” from technical experts to ensure compliance. However, there are no public reports of the newly formed office on the FAFAA, PREPA or FOMB websites. We have only an indirect concern raised by the FOMB that PREPA and many other Commonwealth agencies are not complying with quarterly budget reporting requirements. Without those reports there is no evidence of the effectiveness of this reform.

²³ “[T]he implementation of this project will result in the [operational] reconfiguration of the generation assets located in the north and, most likely, the reconfiguration of several other assets throughout the electric system... Without an integrated analysis of these effects, it cannot be concluded that the conversion of San Juan Units 5 and 6 will result in the least-cost option to supply Puerto Rico’s long-term energy demand. PREPA’s fragmented approach to resource analysis and acquisition is what the public policy of integrated resource planning seeks to avoid.” (Dissenting Opinion of Commissioner Angel Rivera, Case No. CEPR-AI-2018-0001, October 4, 2018).

²⁴ “[El ICSE busca revocar contrato para la conversión a gas en la central de San Juan](#),” *El Nuevo Día*, February 18, 2019.

²⁵ According to its [Form S-1](#) filed with the SEC, New Fortress Energy’s operating revenues in 2017 were \$97 million. Selling 25 million MMBTU per year of natural gas to PREPA at an approximate price of \$10 per MMBTU will generate revenues of \$250 million per year, resulting in total revenues of nearly \$350 million, all else equal.

that.²⁶ Like the long list of poorly documented savings initiatives from PREPA we have seen over the past few years, this critical budget savings project is being treated as little more than marketing hype.²⁷

The contract has also been criticized by a commissioner of the Energy Bureau because it uses PREPA's fuel budget to cover capital expenditures, a practice prohibited by Puerto Rico law.²⁸ This is another indication that PREPA and the governor have learned nothing from the current debt crisis. Rather than increasing transparency, they have chosen to hide the payments and to further distort an already troubled budget picture.

PREPA is now moving forward with a new set of multi-billion-dollar privatization contracts as if the past had never happened. History is poised to repeat itself in Puerto Rico.

PREPA transformation plan will raise, not lower, electrical rates

Affordable electric rates are essential for the recovery of the Puerto Rican economy and are PREPA's stated goal. However, IEEFA estimates that, under the current plans for the transformation of PREPA, electric rates will go up, not down.²⁹ Specifically, our analysis finds that the current plans will result in electricity prices for consumers of 27 cents/kWh in 2024. That is 18% higher than 2018 levels and 35% higher than the 20 cents/kWh goal established by PREPA's financial plan. The system would risk future price increases tied largely to volatility in the natural gas markets. The result will be a step backwards for affordable electricity, an economically uncompetitive system and a lost opportunity to maximize least cost renewable energy.

This high-cost electricity is a result of several factors: the high cost of capital that private developers will demand given Puerto Rico's financial risks, the likelihood of overbuilding natural gas generation, and the high cost associated with PREPA's legacy debt.

Any investor seeking to build new generation in Puerto Rico and enter into a long-term power sales contract faces numerous risks, including Puerto Rico's overall weak economy; declining demand for

²⁶ New Fortress Energy, [Form S-1](#), November 9, 2018, p. 5; PREPA, "[Motion in compliance with order](#)," Puerto Rico Energy Bureau Case No. CEPR-AI-2018-0001, August 16, 2018, p. 198; Puerto Rico Energy Bureau, [Resolution and Order](#), Case No. CEPR-AI-2018-0001, January 25, 2019, p.3.

²⁷ We also note that PREPA has failed to provide quarterly budget reports to the Financial Oversight and Management Board. These quarterly budget reports are supposed to inform the FOMB and PREPA's various stakeholders of the progress that PREPA is making on its certified fiscal plan and annual budget. These reports should document the specific goals of individual budget initiatives, tasks and timelines, individual staff accountability, chain of command, standards for achieving savings or revenue enhancements, corrective actions identified and taken and new budgetary resources quantified and integrated into actual revenue and expenditure accounting and budget documents. These reports are crucial for the early identification of slippage in execution of the many initiatives that comprise PREPA's road back to sound management and fiscal stability. (See: January 14, 2019 letter from FOMB to Governor Ricardo Rosselló, https://drive.google.com/file/d/1udjNofZUTLdhBIC7VMr-DmJL_QovaV3m/view)

²⁸ "PREPA intends to treat the CAPEX associated to the conversion of San Juan Units 5 and 6 as a fuel cost ... San Juan Units 5 and 6 CAPEX costs are not directly related to the purchase of fuel. Nor such CAPEX costs are directly related to the fluctuations due to price changes in fuel and purchased power. Therefore, according to the provisions of Section 6A of Act 83, and Section 6.25(b)(9) of Act 57-2014, PREPA is precluded from recovering such costs through the fuel adjustment clause." (Dissenting Opinion of Commissioner Angel Rivera, Case No. CEPR-AI-2018-0001, January 25, 2019.)

²⁹ Sanzillo and Kunkel, "PREPA privatization will hurt consumers and slow economic recovery," Institute for Energy Economics and Financial Analysis, January 2019.

electricity; the likelihood that legacy debt repayments will be given primary lien status on future electrical system revenues; the likelihood that a high legacy debt repayment rate coupled with expensive new privatization contracts will result in future financial defaults; the divisive and contentious relationship between Commonwealth political leaders and the FOMB; and the risk of political interference in the tariffs or other terms of privatization contracts. For these reasons, we believe that—in the absence of federal loan guarantees or other public subsidies that have not been discussed—private capital will demand high returns to invest in Puerto Rico.

Additionally, if implemented as currently planned, the privatization process will result in overbuilding private natural gas generation in Puerto Rico. The release of PREPA's long-term integrated resource plan (IRP) last month shows how long-term planning is being manipulated to further the political aims of the privatization process. An IRP is supposed to model future scenarios to determine the optimum mix of generation resources over the planning horizon (including a timeline for generation retirements and acquisitions) to achieve affordability and reliability goals. PREPA's IRP included a scenario that was based on a set of pre-determined investment decisions specified by PREPA's advisors and representing the privatization plans that are currently underway. This scenario—despite not being cost-optimized in PREPA's modeling—somehow emerges as one of PREPA's two preferred long-term plans and forms the basis for PREPA's five-year action plan, i.e. the investment decisions that PREPA is actually preparing to move forward with. This scenario achieves only 24% renewable energy by 2038 and includes no new renewable energy between 2023 and 2038.

The five-year action plan in PREPA's integrated resource plan will result in 60-70% of Puerto Rico's electricity coming from natural gas by 2025, with an additional 27% from the island's coal plant.³⁰ This creates a contradiction with Puerto Rico's new energy policy bill passed last month, which calls for the island to achieve 100% renewable energy by 2050. Such renewable energy mandates have a history of being ignored in Puerto Rico. The renewable energy goal is important, not just for environmental reasons, but also for financial reasons. Investments in low-cost renewable energy, which carries no fuel cost, are needed to stabilize PREPA's budget and keep more money circulating in the Puerto Rican economy.

Despite the widespread public consensus in favor of microgrids and distributed renewable energy to support grid resiliency in the aftermath of hurricane Maria, the projects that have been publicly mentioned as part of the privatization are all large-scale projects. By overbuilding the centralized generation system through a series of long-term contracts, PREPA or its successor will have an incentive to maintain electricity consumption at levels that support payment of those contracts, which could lead to erecting barriers to make it more difficult for customers to self-generate their own power.

Finally, current plans for PREPA to repay a high portion of its legacy debt will drive up electricity rates. The most recently proposed debt restructuring agreement, which has yet to be approved, will result in a legacy debt surcharge on electric rates starting at 2.6 cents/kWh and growing to 4.3 cents/kWh over time.³¹ This charge will result in \$300 to \$400 million a year from Puerto Rico's electrical customers to pay off the legacy debt, based on the electricity sales assumptions in PREPA's IRP. In 2060, Puerto Ricans

³⁰ IEEFA further estimates that between one-third to one-half of Puerto Rico's electricity in 2025 will come from new natural gas plants (depending on whether or not the EcoElectrica contract is successfully renegotiated), rather than the conversion of existing units to natural gas.

³¹ Financial Oversight and Management Board, "[Unanimous Written Consent Approving Execution of Preliminary Restructuring Support Agreement of Puerto Rico Electric Power Authority](#)," July 30, 2018, Exhibit B.

will be paying for oil burned in 2008. While the debt restructuring process is separate from the privatization of PREPA, the result of this process directly impacts the affordability of PREPA's rates and hence the likelihood of the privatization process's success.

Law 120 privatization does not resolve PREPA's workforce problems

PREPA faces major challenges in attracting and retaining a skilled workforce, as recognized by the FOMB. PREPA has lost more than a third of its workforce since 2012. News reports have highlighted the problem with workers retiring early to take advantage of benefits before they disappear, or moving to the mainland for higher-paying utility jobs.³²

At the same time, one of the major causes of PREPA's weak management, as identified by the FOMB's independent investigator Kobre & Kim LLP, is the plethora of political appointees within PREPA. According to Kobre and Kim, the patronage army consists of 150 to 300 political soldiers from the major political parties, many of whom have been appointed to technical and professional positions without regard for qualifications.³³ PREPA has allegedly been one of the largest sources of political fundraising on the island.³⁴ It is therefore no surprise that PREPA management has been historically unable to make sound judgements on contracts when the sole goal of those in charge and a large phalanx of people supporting them is the reelection of the Governor.

Weakening PREPA's ability to make its own decisions—by underinvesting in its own workforce and increasingly relying on short-term outside consultants with no institutional memory—facilitates the control of PREPA by outside interests, not the development of a well-planned and professionally managed electrical system.

Nevertheless, despite the widespread recognition of these problems, the FOMB, governor and PREPA management have chosen to take a one-size-fits-all approach to PREPA's workforce, imposing wage and benefit cuts across the board (but not, as noted above, cutting costs of the external consultants). PREPA's Executive Director Jose Ortiz has supported these efforts, arguing that the Board's fiscal plan supersedes collective bargaining agreements.³⁵ Although the recently passed energy policy bill contains language supportive of collective bargaining agreements, the attitude of the governor and PREPA management make it clear that each new privatization contract will be an opportunity for further cuts to labor.

PREPA's labor force has been an important source of middle-class jobs on the island. Yet the Governor and upper-level management of PREPA would rather use their privatization scheme to deny the collective bargaining rights, and reduce the salary, health and pension benefits of the people who actually provide services to the people of Puerto Rico, instead of turning PREPA into a well-managed operation governed by the professional standards of the utility industry—an industry that on the mainland is a stable producer of revenues, a good employer and an accountable corporate citizen.

³² Yaritza Rivera Clemente, "Asoma incremento en renunciias," *El Vocero*, December 17, 2018; Laura Isabel Gonzalez, "Impacta la falta de celadores," *El Vocero*, February 2, 2018.

³³ Kobre & Kim, [Final Investigative Report to the Financial Oversight and Management Board of Puerto Rico](#), August 20, 2018, p. 113-120.

³⁴ *Ibid.*, p. 120.

³⁵ Gerardo Alvarado León, "José Ortiz: 'El plan fiscal va por encima de los convenios colectivos'", *El Nuevo Día*, January 15, 2019.

The Long Island Power Authority is cited often as a model for PREPA. In some instances, the analogy is useful. For example, PSEG (the private operator of LIPA's assets) and LIPA have an operating agreement that acknowledges the collective bargaining agreement with the International Brotherhood of Electrical Workers.³⁶

Puerto Rico's electrical system needs real reform, not more of the same

The question facing Puerto Rico is not whether or not to privatize the Puerto Rico Electric Power Authority. Indeed, such a question makes little sense: private contractors and private capital already play a significant role in the electrical system and, at the same time, future plans for the electrical system are heavily reliant on public (federal) investment for rebuilding transmission and distribution assets.³⁷

The question therefore is not whether or not to "privatize" PREPA, but rather what ownership and governance structure(s) best results in modernizing and depoliticizing the electrical system to achieve the policy goals of affordability, resiliency and 100% renewable energy by 2050. As detailed in the previous sections, the Law 120 privatization model is unlikely to achieve these ends.

The federal government could be enlisted to assist in the rebuilding of PREPA in a constructive manner, but the current privatization effort seems designed to avoid the transparency that this would require. Strong federal support coupled with a willing Puerto Rico government could rebuild the grid and meet electricity and resiliency needs and, in doing so, it could also reduce PREPA's two largest costs—debt and fuel. The federal government has a broad array of financial resources and tools—grants, loan guarantees, demonstration projects and other federal supports—that could be deployed to support the development of renewable energy and decentralized electricity generation projects in Puerto Rico. Under such a scenario, the private sector would be more likely to support investment in Puerto Rico because private companies and investors would not be expected to shoulder all of the risk of a very difficult financial environment.

Together the government of Puerto Rico, federal government and private sector could support the innovation needed to improve the resiliency of the electric grid and to introduce a new cost structure that is lower than the current fossil fuel driven plans.

However, in order for this to occur, there must be a serious effort to reform the governance of the electrical system. PREPA's creditors are currently calling for the appointment of a receiver to replace PREPA's management. IEEFA supports the introduction of the Independent Private Sector Inspector General (IPSIG) model, which is distinct from the role of a typical receiver because of its focus on elimination of waste, fraud and abuse.³⁸ An IPSIG would be empowered to investigate PREPA's

³⁶ [Amended and restated Operations Services Agreement between Long Island Lighting Company d/b/a LIPA and PSEG Long Island LLC](#), December 31, 2013.

³⁷ PREPA's August 1, 2018 Fiscal Plan certified by the FOMB calls for nearly \$7 billion in federal funding as the "'floor' on funding necessary to support suggested resilience build while maintaining long-term rates which meet target criteria." (PREPA Fiscal Plan, August 1, 2018 p. 48).

³⁸ As Deputy State Comptroller of New York, I oversaw the implementation of an IPSIG at the New York Racing Authority when it was facing criminal liabilities. The IPSIG resulted in real financial savings, new organizational options, staff and board accountability, and renewed commitment to internal controls and integrity in the organization's financial disclosures. (See: <http://ieefa.org/wp-content/uploads/2017/08/IEEFA-letter-to-Chairman-Carrion-and-Governor-Rossello-080317.pdf>)

operations, implement reforms to eliminate wasteful and/or illegal activity,³⁹ and report violations of law to enforcement authorities.⁴⁰ Once PREPA has been stabilized as a functional utility, reforms would be needed to significantly curtail the governor's power to appoint PREPA board members, and the executive director should be hired via an open and transparent hiring process conducted by the board.

Finally, the repayment of PREPA's legacy debt at the level currently proposed is not financially viable and will seriously impede the transformation of the electrical system.⁴¹ A restructuring agreement that prioritizes repayment of a large fraction of the outstanding legacy debt would be problematic for attracting private capital, as recognized by members of the FOMB. The likelihood of successfully transforming PREPA under any ownership and governance structure is greatly enhanced by eliminating the ratepayer obligation to repay legacy debt.⁴²

Chairman Grijalva and the members of this committee, thank you again for the opportunity to address you. I come from New York State with more than twenty years' experience as a public finance officer serving elected officials. I am neither naïve nor cynical about the role of politics in the process of turning private citizens' tax and rate dollars into public goods. My state produced a building called the Tweed Courthouse. It is almost 150 years old and stands in lower Manhattan, an exemplary architectural feat that is on the National Register and serves the public today. It is also the site of perhaps the biggest construction kickback scheme in the history of the United States. The first case tried in the courthouse was the conviction of the political boss who was the mastermind of the scheme.

PREPA has spent \$9 billion of money borrowed from investors that it is unable to repay. Yet, even before the 2017 hurricanes, the electrical system was in a state of extreme disrepair. And no one is going to jail.

Without addressing the mistakes of the past, Governor Rosselló's privatization scheme will fail.

³⁹ The IPSIG model was used to monitor contracts for debris removal from the World Trade Center site in New York after the 9/11 attack. A Congressional subcommittee concluded the use of the IPSIG was an "overwhelming success". See: Subcommittee on Management, Integration and Oversight Committee, Committee on Homeland Security, Staff Report, An Examination of Federal 9/11 Assistance to New York: Lessons Learned in preventing waste, fraud, abuse and lax management, U.S. House of Representatives 109th Congress, August 2006.

⁴⁰ Hon. Margaret Finerty, "[Monitorships, IPSIGs and Independent Investigations](#)," International Association of Independent Private Sector Inspectors General, October 19, 2005.

⁴¹ Sanzillo and Kunkel, "PREPA debt restructuring deal won't restore agency to financial health," Institute for Energy Economics and Financial Analysis, August 2016.

⁴² Bondholders have additional options for pursuing partial recovery of the legacy debt, including from insurers (on the approximately \$2.4 billion of outstanding legacy debt that is insured) and from claims against legal advisors, underwriters and financial advisors on the debt deals.